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PAPER

***“PAYMENT PROVISIONS OF
THE HGCRA 1996 ”***

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PAYMENT PROVISIONS OF THE HGCRA 1996

Introduction

Construction is big business. It is an entrepreneurial venture, engaged in for profit. It is a cut-throat business where profit margins are very tight. The client wants best value at best price – the penny and the bun. Cash flow is essential to the success of the industry. The contractor wants prompt payment for work done. The client only wants to pay for what has been properly done. In order to maximise cash flow the contractor needs to ensure that the construction contract provides a mechanism for payments. The client will often seek to maximise cash flow by paying as late as possible (if at all). Furthermore, the client will seek to ensure that any contract payment mechanism safeguards against payment for work not successfully completed. Cashflow and timely payment were central to the considerations of the Latham Report. Consequently, the Housing Grants Construction and Regeneration Act 1996 (hereinafter referred to as the HGCRA) directly addresses and seeks to provide solutions to the problem of ensuring cash flow in the industry. Sections 114 to 117 provide for the Scheme, giving of notices, periods of time and Crown application. The remaining 5 sections, 109 to 113, deal solely with payment provisions. These provisions apply generally. They are not restricted to adjudication and are thus equally applicable to litigation and arbitration.

Cash flow is also affected on a broader level by disputes under the contract. Indeed the amounts involved in claims for damages for breach of contract may well exceed the monies due for work done under the contract. Prompt settlement of claims and prompt payment are also essential to the industry and to facilitate this the HGCRA introduced adjudication by virtue of Section 108. The adjudication process of course, is available for the settlement of disputes in respect of payment, but has wider application. Finally, to put all of Part II HGCRA into context, Sections 104 to 107 deals generally with Construction Contracts, Construction Operations, exemption of general consumers and contracts in writing.

Sections 109 to 113 mandate the provision of payment terms in construction contracts regardless of the parties wishes, and in default of party provision in the contract will impose conditions set out in the Act and/or the scheme for construction contracts. Although both the provisions for adjudication and the payment process are contained in the same Act there are some differences in the manner in which they are introduced. If a contract's adjudication provisions do not strictly comply with the requirements of section 108 (1) to (4) then, as per s108 (5), the Scheme for Construction Contracts applies. In the event that a contract's payment provisions fail to comply with the relevant sections of 109 to 113 then it is only the particular provisions, which fail to comply that are superseded by the Scheme. If some provisions are compliant they remain valid with the Scheme replacing the invalid ones only.¹

S 109 - The right to periodic payments

Traditionally, with the exception of perhaps a true turnkey contract, all standard forms of construction contract make provision for regular on account payments for ongoing works. Section 109 of the Act clarifies the entitlement of parties to regular payments.

109(1) A party to a construction contract is entitled to payment by instalments, stage payments or other periodic payments for any work under the contract unless –

- (a) it is specified in the contract that the duration of the work is to be less than 45 days, or*
- (b) it is agreed between the parties that the duration of the work is estimated to be less than 45 days.*

The Act is clear in establishing a party's rights to regular payment.² The only exception is for projects that are either stipulated to last no longer than 45 days or it is agreed by the parties that the work is estimated to last no longer than 45 days. The 45 day qualification rule is really a pragmatic one, as it is normal practice that payments are made monthly. In the event that a contract is for less than 45 days, the absence of an interim payment is not likely to be a heavy burden for a party to bear.

¹ See **EXPLANATORY NOTE TO THE SCHEME** (*This note is not part of the Order*) : Part II of the Housing Grants Act 1996 makes provision in relation to construction contracts. S114 empowers the Secretary of State to make the Scheme for Construction Contracts. Where a construction contract does not comply with the requirements of s108 to 111 (adjudication of disputes and payment provisions), and s113 (prohibition of conditional payment provisions), the relevant provisions of the Scheme for Construction Contracts have effect.

² The devil however lies in the detail. See **Maxi Construction Management Ltd v Mortons Rolls Ltd** [2001] Outer Ct of Session The court held that a failure to deal with an application for evaluation of interim payments does not automatically lead to a dispute : Clause 12 of the Scheme requires submission of the full basis of a demand.

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The Act does not clarify any differences between payments by instalments, payments by stage or periodic payments and it is assumed that the terms are generally intended to mean the same thing. The Act is also silent on the definition of duration.

109(2) The parties are free to agree the amounts of the payments and the intervals at which, or circumstances in which, they become due.

There is no specific requirement that a party must be paid monthly or four weekly. The Act only seeks to provide for the making of an interim payment. The parties are free to agree any arrangements / terms for interim payments, even to the extent whereby interim payments are either infrequent or of minor monetary value. It should be noted however that monthly payments are still the norm and dominant parties in construction contracts have generally not abused the flexibility of the system.

109(3) In the absence of such agreement, the relevant provisions of the Scheme for Construction Contracts apply

If a contract does not make the necessary provision for interim payments then the relevant sections of the Scheme are imposed on the parties. These provisions are contained in Part II of the Scheme. Paragraphs 1 to 8 deal with both entitlement to and the amount of payment and also when payments become due under the Scheme.

S 110 Dates for payment

Whilst section 109 states that a party to a construction contract is entitled to payment by instalments or on an interim basis, the details of the required mechanisms are provided in section 110.

110(1) Every construction contract shall-

- (a) provide an adequate mechanism for determining what payments become due under the contract, and when, and*
- (b) provide for a final date for payment in relation to any sum which becomes due.*

The parties are free to agree how long the period is to be between the date on which a sum becomes due and the final date for payment.

It is necessary, as per section 110 (1) (a), that a construction contract provides a mechanism, both enabling the parties to establish the value of due payment and when the payment is due. However in **Shimuzi Europe Ltd v LNJ Fabrications Ltd**,³ some potential for manipulating the system was identified. Shimizu made it a condition precedent of a contract that payment did not become due until a VAT invoice was issued. Shimizu then declined to advise their sub contractor as to the value of monies to be paid, effectively preventing the issue of an accurate VAT invoice. The Court held that this was acceptable and that payment did not become due until a VAT invoice was issued.

Section 110 (1) (b) requires that a final date for payment must be stipulated.

It is normal for a period of time measured in days to be used as the basis for calculating a final date for payment. For example, as we will discuss below, paragraph 8 of the Scheme stipulates that the final date for payment is 17 days after the due date. The final sentence of section 110 (1) makes it clear, that subject to compliance with the mechanism's requirements, the parties are at liberty to decide on how long the period is between the due date and the final date for payment. Despite the obvious potential for abuse there does not appear to have been a significant trend for dominant parties to impose unusually long time periods from due date to final payment.

Section 110 (3) states that if a contract does not comply with the requirements in 110 (1) then the relevant provisions of the Scheme apply⁴. It would generally be in the interests of the parties to ensure that any construction contract complies with the requirements of section 110 (1). In particular a main contractor should seek to ensure that the payment provisions in their sub contract agreements mirror the main contract with the employer⁵. Failure to do so could result in the main contractor being liable to make payment to their

³ **Shimuzi Europe Ltd v LNJ Fabrications Ltd** [2003] EWHC 1229 (TCC). The relevant form of the DOM/1 permitted an adjudicator's payment decision to be set off against a subsequent claim and further gave the adjudicator power to rule on his own jurisdiction

⁴ **Hills Electrical & Mechanical plc v Dawn Construction Ltd** [2003] Ct of Session CA 98/02. Default scheme's payment provisions only apply to aspects where a contract fails to provide for payment.

⁵ **Karl Construction (Scotland) Ltd v Palisade Properties Plc**. [2002] SLT 312 P/872/00. Parties to a Construction Contract cannot agree that their provisions are in accordance with the Act's payment provisions. It is an adjudicator or other authorised third party who is able to make that decision. Obviously the parties do not need to refer a dispute regarding payment terms and therefore prevent the intervention of a third party.

sub contractor before they are due to receive payment from the employer. This is particularly important now since, as discussed in Section 113 below, “pay when paid” provisions have been largely outlawed.

If a construction contract fails to comply with the requirements of section 110 (1) then the relevant paragraphs of the Scheme are imported into the contract. As stated above the relevant paragraphs dealing with payment, are contained in Part II of the Scheme. Rules 1 to 8 are those, which deal with the issues of calculating payment entitlements, when they are due and the final date for making payment of any monies due.

Rule 4 Any payment of a kind mentioned in paragraph 2 above shall become due on whichever of the following dates occurs later –

- (a) *the expiry of 7 days following the relevant period mentioned in paragraph 2 (1) above, or*
- (b) *the making of a claim by the payee.*

Rule 12 defines “*relevant period*” as being 28 days⁶. In order to simplify the dates when interim applications may be made it is quite common for parties to agree to submit monthly applications rather than adopting the 28 day period. It is important to note that paragraph 4 provides two alternatives.

If an application is submitted promptly then that payment becomes due 7 days after it’s receipt. For example if the relevant period ended on the 1st of March, and assuming that an interim application was received that day, then payment would become due on the 8th March. The establishment of the due date is critical, as the final date for payment is calculated from the due date.

If however an application is submitted later than at the end of the relevant period, it is necessary to consider whether 4 (a) or (b) applies in determining the due date for payment. Generally if the submission date is later than 7 days after the last day of the relevant period then option (b) viz, “upon the making of a claim by the payee”, will apply.

Rule 8 provides the mechanism for determining the final date for payment. In essence if the contract fails to stipulate a final date for payment then in accordance with paragraph 8 (2) the final date for payment shall be 17 days from the date that payment becomes due.

In order to avoid any misunderstanding it is necessary that the terminology of the Scheme relating to payment is clearly understood. There are two important dates in the payment process. The payment “**due date**” is the date upon which the payment process really begins. It should be remembered that if the timescales are properly complied with the payment due date does not occur until 7 days after receipt of the application (paragraph 4 a). The second important date is the “**final date for payment**”, whereby all money due must be paid.

Whilst sections 109 and 110 (1) deal with the entitlement to interim payments, calculation of payment due and the establishment of and or calculation of dates for payments, section 110 (2) requires that all construction contracts “**must provide**” a facility for the giving of a payment notice.

110 (2) Every construction contract shall provide for the giving of notice by a party 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.

This section strives to ensure clarity in the payment process. The paying party has a clear obligation to provide details of both the amount due for payment and also to provide details of the calculations used in determining the amount due. This need not be an onerous obligation for the paying party in that the information does not have to be set out in an extensive or cumbersome document. Frequently the paying party will simply, but clearly, annotate a copy of the application for payment, which had been submitted by the party claiming payment. The annotations will comprise calculations used and any comments necessary to detail differences between the application and the actual payment ascertained as being due. Perhaps the

⁶ However if the contract actually provides necessary information relating to payment periods then the relevant period will be in accordance with the contract.

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most onerous element of section 110 (2) is the requirement to issue the payment notice within five days of the due date for payment, particularly if paragraph 4(b) applies since the responding party only has five days to both consider what could be a very detailed or complex application for payment prior to issue of the payment notice.

The Act places an obligation on the part of the paying party in a construction contract in that they must issue a payment notice. Most people would agree that the provision of such a notice should prevent disputes that might otherwise arise because of poor communications which lead to misunderstandings about what is to be paid and when and can even lead a party to falsely believe that their requests for payment are being ignored.

Even though problems may arise where a party fails to comply with their obligation to issue a notice, the Act makes no express provision to deal with a failure to issue a notice. It is for these reasons that the failure to issue a payment notice is regarded as being a minor breach of contract.

Section 110 (3) states that in the event that a contract does not include provisions which satisfy the requirements of section 110 (2) then the relevant parts of the Scheme apply.

Rule 9 : A party to a construction contract shall, not later than 5 days after the date on which any payment–

- (a) becomes due from him, or*
 - (b) would have become due, if -*
 - (i) the other party had carried out his obligations under the contract, and*
 - (j) no set-off or abatement was permitted by reference to any sum claimed to be due under one or more other contracts,*
- give notice to the other party to the contract specifying the amount (if any) of the payment he has made or proposes to make, specifying to what the payment relates and the basis on which that amount is calculated.*

Rule 9 is very similar in it's wording to section 110 (2). It is important to ensure when preparing a payment notice that all the necessary information has been included. Typically the notice should state the payment that the payee considers is due and sufficient detail demonstrating the basis upon which the due sum has been calculated. A simple means of testing whether the level of information satisfies the requirements of 110 (2) and/or paragraph 9 is to consider if a third party could determine the sum due by referring to the notice and application (an objective test).

Section 111 Notice of intention to withhold payment

If the paying party does not intend to make full payment of a sum due under the contract, section 111 requires that they issue a withholding notice, advising the other party of the sums to be withheld.

111 (1) A party to a construction contract may not withhold payment after the final date for payment of a sum due under the contract unless he has given an effective notice of intention to withhold payment. The notice mentioned in section 110 (2) may suffice as a notice of intention to withhold payment if it complies with the requirements of this section.

111 (2) To be effective such a notice 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.*

111 (3) The Parties are free to agree what that prescribed period is to be. In the absence of such agreement, the period shall be that provided by the Scheme for Construction Contracts.

111 (4) Where an effective notice of intention to withhold payment is given, but on the matter being referred to adjudication it is decided that the whole or part of the amount should be paid, the decision shall be construed as requiring payment not later than –

- (a) seven days from the date of the decision, or*
- (b) the date which apart from the notice would have been the final date for payment, whichever is the later.*

The requirement to issue a notice of withholding is only a mandatory requirement if the paying party did not intend to pay all monies due under the contract. Section 111 (1) is clear; a paying party is not allowed to withhold payment if a withholding notice has not been issued⁷.

⁷ **Palmers Ltd v ABB Power Construction Ltd** [1999] BLR 426. : No effective withholding notice had been issued. The court also held that a scaffolding is a construction operation and further that a court can deliver a declaration as to jurisdiction.

If monies due are withheld without a notice then a dispute has arisen which can be referred to adjudication⁸.

It must however be noted that section 111 (1) only applies to a sum due under the contract. If there is any dispute as to the validity of sums claimed, then it is the claimant's responsibility to satisfy the burden of proof. ⁹ An exception arises where a contract states that payment is due once a payment certificate has been issued. Normally a certificate can be challenged but if the contract makes it final then once issued payment becomes due and a withholding notice will be of no avail.¹⁰

The failure to issue a withholding notice will however prevent a party from using contra charges as a means of justifying a failure to make payment. Providing that the claimant is able to substantiate entitlement for money claimed, the paying party by failing to issue the notice loses the right to withhold against that particular payment¹¹. The loss of right is only temporary. If there are valid reasons to withhold payment then, subject to a compliant notice, the paying party can withhold monies during any future payment process.

The actual terms of a contract must be considered carefully. The Act only requires that a notice of withholding be issued if monies are to be withheld and that the contract must state what the prescribed period is for issuing the notice. There is no requirement with regards to the wording of any contractual clause in relation to the sum being due. In the UK a commonly used standard form for design and build contracts, the JCT 98 With Contractors Design, actually states that in the absence of a withholding notice the amount claimed shall be paid. Therefore even if the amount claimed is incorrect and not actually due under the contract the paying party will become liable for that amount. Many other contracts do not contain this type of provision. Furthermore, many consultants amend the contract as a matter of course, to remove this provision, placing it back in line with the default provisions of the Scheme.

A notice must deal with each item of withholding separately. Any attempt at wrapping up all of the withheld items into a lump sum withholding notice, which therefore fails to identify and explain why and how much is being withheld from each item, will render the notice invalid.

The parties are free to decide on the time requirements of any withholding notice. It would be acceptable for the parties to agree on any time from and between the submission of application to 1 day before the final date for payment. If a contract does not provide a prescribed period as required by section 111, Paragraph 10 of the Scheme states that any withholding notice must be issued not later than 7 days before the final date for payment.

Set off against adjudication decision and monies otherwise due.

It is one thing for the adjudicator to decide that money is due, but if the other party can set off that sum against other sums allegedly due, the value of the decision is undermined from the claimant's perspective, but provides protection for the payer where the sums due to the payer from the payee exceed what the adjudicator has ordered him to pay, particularly if there are question marks over the payee's financial status and thus over the ability to recover payment and guards against the potential of any sum paid disappearing into a black hold.

However, the courts have developed rules to withhold enforcement if a payee is in liquidation. Where an enforcing party is in receivership the court is entitled to stay enforcement.¹² Furthermore, where a defendant is in administration it is unlikely under s11 Insolvency Act that permission will be granted for an

⁸ **Strathmore Building Services Ltd v Colin Scott Greig t/a Hestia Fireside Design CA** [2000] Outer Ct of Session CA 19/00. Withholding notice must be issued after an application for payment to be valid.

⁹ **S L Timber Systems Ltd v Carillion Construction Ltd** [2001] BLR 516 : Payment ordered by adjudicator because of absence of withholding notice. The court held that the claimant must still prove entitlement. In the event even though the adjudicator was wrong in his determinations on entitlement, still the decision would be enforced, forcing the party to move to final determination in order to recover any payment made in compliance with the decision.

¹⁰ **London Borough of Barking & Deagenham v Terrapin Construction Ltd** : [2000] CA QB ENF 99/0756 Pre-1998 JCT Clause 30.8.11 Design & Build : Led to amendments to later contracts.

¹¹ **Rupert Morgan Building Services Ltd v David Jervis & Harriett Jervis**, [2003] EWCA Civ 1563. A sum incorrectly certified by an Architect was not paid by the Employer as he was aware of the error in the certificate. However no withholding notice had been issued. It was held that the sum had to be paid in compliance with the adjudicator's decision. It was then open to the payer to commence a separate action for subsequent recovery of the payment.

¹² **Rainford House Ltd (in Administrative Receivership) v Cadogan Ltd** [2001] HT 01/014 :

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adjudication.¹³ However, less specific allegations of the payee being in a poor financial state are more difficult to sustain.¹⁴ The permission of the court is required to commence adjudication once a firm enters into administration.¹⁵ Conversely the court needs to be robust when it is the payer who is in financial difficulty¹⁶ and an adjudicator's decision can be the subject matter of a statutory demand.¹⁷

It is clear that set off is not allowed to provide funds to settle undetermined claims some time in the future, but is available against liquid debts and concurrent judgements.¹⁸ The question that therefore is whether or not an adjudication decision may be set off against liquidated damages claims during enforcement proceedings. In **Solland** the court held that it could not.¹⁹ An unsuccessful attempt was made in **Riverbrae**²⁰ to set of payment against other sums due. Any withholding notice must be issued before an adjudication and the validity of the notice and the grounds for withholding can be ruled upon by the adjudicator, but if the withholding notice is issued to late no set off is permitted.²¹ Further more, in order to be effective, a withholding notice must be in writing.²² Note that the withholding notice provisions are of general application including applications for summary judgment and not restricted to adjudication.²³ The terms of a contract that stated that on termination no further sums would be payable was called into play in an attempt to defeat an adjudication decision in **Levolux**.²⁴ The termination was issued after the decision was delivered and the court refused to countenance the attempt. An attempt to issue a withholding notice against an adjudicator's decision was recently frustrated in **Conor**.²⁵

If at first you don't succeed, try, try and try again. If a party does not like an instruction to pay, can he go back and have a fresh adjudication to recoup the monies as opposed to moving on to arbitration or adjudication? The rules on double jeopardy, it has been held, apply to adjudication so the answer is no.²⁶ The appropriate course of action is to advise the adjudicator of a lack of jurisdiction. If the adjudicator goes ahead then enforcement may be resisted on the grounds of double jeopardy. A stay will not be issued

¹³ **Canary Riverside Development v Timtec International** [2000] R.Ct of Justice 69/2000 .: See also **George Parke v The Fenton Gretton Partnership** [2001] CILL 1712 : Bankruptcy loomed for a party with a valid claim against the claimant seeking to enforce adjudication via a statutory demand : Stay ordered. Compare **Guardi Shoes Ltd v Datum Contracts** : [2002] 5816 OF 2002 : Lock out – non-payment : Adjudication : non-payment : Statutory demand issued. The other party asserted a counterclaim. Notwithstanding, the Statutory demand was enforced by the court.

¹⁴ **Harwood v Lantrode** [2001] TCC. Challenging evidence of decision and equitable set off not grounds to resist enforcement. Since however an Insolvency hearing was pending the court ordered that the award be paid into court. See also **Isovel Contracts Ltd v ABB Technologies Ltd** [2001] CH.Div : Court ordered enforcement despite the fact that business was in administration and asserted set off claims.

¹⁵ **Straume (A) (UK) Ltd v Bradlor Developments Ltd** [1999] CILL 1520.

¹⁶ **Re A Company (number 1299 of 2001)** [2001] : Thee claimant had a payment certifies. There had been no withholding notice. The court held that the claimant had the right to assert debt and proceed to motion for winding up. Applications for set off and counterclaim were refused by the court.

¹⁷ **Jamil Mohammed v Dr Michael Bowles** [2002] 394 SD 2002

¹⁸ **Bovis Lend Lease Ltd v Triangle Development Ltd** [2003] BLR 31 HT 02/0375

¹⁹ **Solland International v Daraydan Holdings Ltd** [2002] EWHC 220 HT 01/481 ; See however **C & B Scene Concept Design Ltd v Sobars Ltd** [2002] EWCA Civ 46, [2002] BLR 93. The Court of Appeal decision was however confirmed and followed in **Dumarc Building Services Ltd v Mr Salvador Rico** [2003] KT203081 Epsom C.C.

²⁰ **Allied London & Scottish Properties Plc v Riverbrae Construction Ltd** [1999] BLR 346

²¹ **Hart Builders (Edinburg) Ltd v St.Andrews Ltd** [2002] A69/02 : No after the event set off permitted against decision where issue not put to adjudicator and no withholding notice had been issued : see also **Construction Centre Group Ltd v Highland Council** : **Highland Council v Construction Centre Group Ltd** [2002] BLR 476 CA 127/02 XA 123/02 : Liquidated damages formed the subject matter of a withholding notice issued after adjudicator's decision . Held issued too late to prevent enforcement. See also **VHE Construction PLC v RBSTB Trust Co Ltd** [2000] BLR 187 HT 99/241.

²² **Strathmore Building Services Ltd v Colin Scott Greig t/a Hestia Fireside Design** [2000] Outer Ct of Session CA 19/00

²³ **Millers Specialist Joinery Company Ltd v Nobles Construction Ltd** [2001] TCC 64/00

²⁴ **Levolux A.T. Ltd v Ferson Contractors Ltd** [2002] BLR 341; [2002]EWCACiv 11

²⁵ **Conor Engineering Limited v Les Constructions Industrielles de la Méditerranée (CNIM)** [2004] EWHC 899 : The court had first to decide whether or not the primary purpose of the site was power generation or waste disposal in order to apply the provisions of s105 HGCRA. In the circumstances the court held that it was waste and so the HGCRA applied. Following on from that the court found that a withholding notice issued against the decision was not effective because in the circumstances it was out of time. Time counted from the date of drafting the decision. This opens up the possibility that if the contract is appropriately worded to allow withholding against monies due consequent upon the decision of an adjudicator and the notice is issued in time, then enforcement of the decision could be prevented.

²⁶ See also **Ron Jones (Burton-on-Trent) Ltd v Mrs JS & Mrs JD Hall** [1998] EWCH 328. An attempt was made to keep items out of jurisdiction of arbitrator and submit them to a separate arbitration. The court held that this was not permitted in the circumstance of the case and that the first arbitrator's decision ruling out the items was final.

against the second adjudication.²⁷ Perhaps the best way of dealing with this is to seek a declaration to prevent further waste of time and monies.²⁸

However, where the second dispute is deemed to be a separate dispute and not a re-submission of the same dispute there is no infringement of the double jeopardy rule. Thus a sequence of disputes in relation to separate interim orders may be submitted to separate adjudications.²⁹ A consequence of this is that if a party is over-paid on an interim payment the monies may be recovered or deducted from subsequent payments.³⁰

A question has arisen as to whether an adjudication decision stands or falls in its entirety. If correct elements of the decision can stand the claimant can seek enforcement of part of a decision. If not, the entire claim will fail. Cherry picking or dissecting a decision will not usually be permitted, particularly if the wrong doing of the adjudicator goes to the root of the matter.³¹ By contrast, there is scope for an adjudicator to amend minor mistakes under the slip rule.

Final Accounts

A number of cases have dealt with aspects of payment in respect of final accounts. Recovery of retainers is always a highly contested matter. In **Cook (F.W.) Ltd v Shimizu (UK) Ltd**.³² the court held that a decision on entitlement on final account does not override contractual retainer provisions, and thus payment would occur in due course as per the contract provisions. Similarly in Buxton the court recently held that retention money should not be released until claims have been addressed.³³

Some employers regard retainers as a windfall profit rather than as a fund to guard against defects. Small contractors have great difficulty recovering retainers and the small sums involved mean that they often fail to pursue recovery. A major hurdle to triggering repayment of retainers is the issue of a final certificate. Often they are not issued or delayed for inordinate periods of time, thereby wearing the other party down by attrition. Whilst repayment is not normally due until the certificate is issued, nonetheless, if there has been undue delay and the employer has prevented issue of the certificate, repayment may be ordered.³⁴

An attempt to turn an interim payment into a final settlement which could not be opened up was defeated in **Hurst Stores and Interiors Ltd v M.L.Europe Property Ltd**.³⁵ The standard wording of an interim account was changed to make the account final. The project manager signed it off without noticing the change of wording. A claim for £2M was met with the response that the amount due was final, agreed and signed off so no further claim would be accepted. The court held that the project manager had no contractual capacity to alter the terms of the contract so the additional claim could be put forward.

Section 112 Right to suspend performance for non-payment

Traditionally construction companies have used the threat of suspending works when problems with payment occur. To do so has previously been risky, as to suspend the works would itself be classed as a breach of contract.

112 (1) Where a sum due under a construction contract is not paid in full by the final date for payment and no effective notice to withhold payment has been given, the person to whom the sum is due has the right (without prejudice to any other right or remedy) to suspend performance of his obligations under the contract to the party by whom payment ought to have been made ("the party in default").

²⁷ **William Naylor t/a Powerfloated Concrete Floors v Greenacres Curling Ltd** [2001] Outer Ct of Session P514/01

²⁸ **John Mowlem & Co plc v Hydra-Tight Ltd** [2000] HT 184

²⁹ **Skanska Construction UK Ltd v ERDC Group Ltd** [2002] Ct of Session P1193/02 : Application to stay adjudication on grounds of trying same dispute : Court held, whilst same contract, issues concerned different stages of contract.

³⁰ **Holt Insulation Ltd v Colt International Ltd** [2001] LV01 5929 TCC : Following an adjudication a 2nd dispute was referred to adjudication. Court held that it was not the same dispute. It involved different issues so the adjudicator had jurisdiction. Similarly in **Mivan Ltd v Lighting Technology Projects Ltd** [2001] an interim payment was enforced because no withholding notice had been issued. In a 2nd adjudication a counterclaim was successfully put forward. There was no double jeopardy since this was a separate issue.

³¹ **Barr Ltd v Law Mining Ltd** [2002] 80 Con LR A single dispute can have several parts : the court can uphold valid decisions and order stay ultra vires part. However compare **Sherwood & Casson Ltd v Mackenzie** [2000] CILL 1577 where the court opposed cherry picking elements of a decision, since the matter went to jurisdiction. **KNS Industrial Services (Birmingham) Ltd v Sindall Ltd** [2000] HT 00/164 : **Farebrother Building Services Ltd v Frogmore Investments Ltd** [2001] CILL 1762.

³² [2000] BLR 199 ; HT 99/289

³³ **Buxton Building Contractors Limited v Governors of Durand Primary School** [2004] EWHC 733

³⁴ **Pitchmastic v Birse No1 (Dyson)** [2000] 19981 TCC 159 Q per Dyson J.

³⁵ [2003] EWHC 1650 : [2004] EWCA 490

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112 (2) The right may not be exercised without first giving to the party in default at least seven days notice of intention to suspend performance, stating the ground or grounds on which it is intended to suspend performance.

112 (3) The right to suspend ceases when the party in default makes payment in full of the amount due.

This section introduces a clear right for parties experiencing payment problems in respect of sums which have “**become due**”, to suspend their works. In order to suspend the works it is essential that they provide a written notice, giving details of the grounds upon which performance is to be suspended. The defaulting party then has 7 days in which to remedy the breach. If after 7 days the breach has not been remedied the contractor may suspend the works.

Contractors in the UK are gradually beginning to employ their right to suspend the works more frequently. If there is a significant amount of work still to be completed on a project, the use of this section can produce remarkable results. The last thing which an employer or contractor would want to be faced with halfway through a project is an unnecessary delay. Even if they disagree with the grounds upon which section 112 has been employed, what can they do, other than make payment, to force the other party to recommence work? A referral to adjudication is likely to take in excess of 4 weeks and that would normally be the quickest option available. A realistic interim settlement is about as good an option as any available to the alleged debtor.

112 (4) Any period during which performance is suspended in pursuance of the right conferred by this section shall be disregarded in computing for the purposes of any contractual time limit the time taken, by the party exercising the right or by a third party, to complete any work directly or indirectly affected by the exercise of the right.

Where the contractual time limit is set by reference to a date rather than a period, the date shall be adjusted accordingly.

It is not just the works, which are suspended. Section 112 (4) provides for the contract completion date to be extended in exact proportion to time lost during a valid suspension of the works. For example if a contract was suspended for 10 days due to a late payment and the contract was originally intended to be complete on 10 March, then the new completion date would be the 20 March. The contract has been extended by the 10 days suspension.

The Act provides no automatic right for claiming additional costs resulting from a suspension of the works under section 112. Some standard forms in the UK have dealt with this matter and facilitate the recovery of loss and expense. It is also possible for a party who validly suspended the works to seek the recovery of any damages, resulting from the breach of contract by the defaulting party.

Section 113 Prohibition of conditional payment provisions

Conditional payment provisions, which are commonly referred to as back-to-back payments, have been almost entirely quashed by this section³⁶. It was quite common in the UK for main contractors to stipulate that the sub contractor would only be paid after the main contractor had received his money. Thus, a standard defence used by the main contractor’s quantity surveyor would be that they had not had their money yet.

113 (1) A provision making payment under a construction contract conditional on the payer receiving payment from a third person is ineffective, unless that third person, or any other person payment by whom is under the contract (directly or indirectly) a condition of payment by that third person, is insolvent.

This clause is badly drafted and grammatically incorrect. It is very difficult to read and understand. It is commonly understood to mean that a clause making payment conditional upon payment being first made by a third party will only be valid if that third party becomes insolvent.

The only exception to the rule that back to back payments are invalid is whereby a payment is conditional on payment being first received by a third party who has subsequently become insolvent. Whilst it appears inequitable that a contractor may lose his right to payment as a result of the insolvency of a third party, with whom they have no contractual relationship, the Act has at least gone a long way towards the removal of the back-to-back payment.

³⁶ **Durabella Ltd v Jarvis.J & Sons Ltd** 1998 ORB 33 –This concerned a pre-HGCRA contract with a pay when paid provision. In the circumstances the court held that insufficient evidence had been adduced to establish non-payment by the client. Since the contractor had been paid he was therefore order to pay up.

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Payment : Entitlement to stage payments.

- 109(1) A party to a construction contract is entitled to payment by instalments, stage payments or other periodic payments for any work under the contract unless-
- (a) it is specified in the contract that the duration of the work is to be less than 45 days, or
 - (b) it is agreed between the parties that the duration of the work is estimated to be less than 45 days.
- 109(2) The parties are free to agree the amounts of the payments and the intervals at which, or circumstances in which, they become due.
- 109(3) In the absence of such agreement, the relevant provisions of the Scheme for Construction Contracts apply.
- 109(4) References in the following sections to a payment under the contract include a payment by virtue of this section

Dates for payment.

- 110(1) Every construction contract shall-
- (a) provide an adequate mechanism for determining what payments become due under the contract, and when, and
 - (b) provide for a final date for payment in relation to any sum which becomes due.
- The parties are free to agree how long the period is to be between the date on which a sum becomes due and the final date for payment.
- 110(2) Every construction contract shall provide for the giving of notice by a party 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.
- 110 (3) If or to the extent that a contract does not contain such provision as is mentioned in subsection (1) or (2), the relevant provisions of the Scheme for Construction Contracts apply

Notice of intention to withhold payment.

- 111(1) A party to a construction contract may not withhold payment after the final date for payment of a sum due under the contract unless he has given an effective notice of intention to withhold payment.
- The notice mentioned in section 110(2) may suffice as a notice of intention to withhold payment if it complies with the requirements of this section.
- 111(2) To be effective such a notice 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.
- 111(3) The parties are free to agree what that prescribed period is to be.
- In the absence of such agreement, the period shall be that provided by the Scheme for Construction Contracts.
- 111(4) Where an effective notice of intention to withhold payment is given, but on the matter being referred to adjudication it is decided that the whole or part of the amount should be paid, the decision shall be construed as requiring payment not later than-
- (a) seven days from the date of the decision, or
 - (b) the date which apart from the notice would have been the final date for payment, whichever is the later.

Right to suspend performance for non-payment.

- 112(1) Where a sum due under a construction contract is not paid in full by the final date for payment and no effective notice to withhold payment has been given, the person to whom the sum is due has the right (without prejudice to any other right or remedy) to suspend performance of his obligations under the contract to the party by whom payment ought to have been made ("the party in default").
- 112(2) The right may not be exercised without first giving to the party in default at least seven days' notice of intention to suspend performance, stating the ground or grounds on which it is intended to suspend performance.
- 112(3) The right to suspend performance ceases when the party in default makes payment in full of the amount due
- 112(4) Any period during which performance is suspended in pursuance of the right conferred by this section shall be disregarded in computing for the purposes of any contractual time limit the time taken, by the party exercising the right or by a third party, to complete any work directly or indirectly affected by the exercise of the right.
- Where the contractual time limit is set by reference to a date rather than a period, the date shall be adjusted accordingly.

Prohibition of conditional payment provisions.

- 113(1) A provision making payment under a construction contract conditional on the payer receiving payment from a third person is ineffective, unless that third person, or any other person payment by whom is under the contract (directly or indirectly) a condition of payment by that third person, is insolvent.
- 113(2) For the purposes of this section a company becomes insolvent-
- (a) on the making of an administration order against it under Part II of the Insolvency Act 1986,
 - (b) on the appointment of an administrative receiver or a receiver or manager of its property under Chapter I of Part III of that Act, or the appointment of a receiver under Chapter II of that Part,
 - (c) on the passing of a resolution for voluntary winding-up without a declaration of solvency under s89 of that Act, or
 - (d) on the making of a winding-up order under Part IV or V of that Act.

³⁷ Copyright the Crown

PAYMENT PROVISIONS OF THE HGCRA 1996

- 113(3) For the purposes of this section a partnership becomes insolvent-
- (a) on the making of a winding-up order against it under any provision of the Insolvency Act 1986 as applied by an order under section 420 of that Act, or
 - (b) when sequestration is awarded on the estate of the partnership under section 12 of the Bankruptcy (Scotland) Act 1985 or the partnership grants a trust deed for its creditors.
- 113(4) For the purposes of this section an individual becomes insolvent-
- (a) on the making of a bankruptcy order against him under Part IX of the Insolvency Act 1986, or
 - (b) on the sequestration of his estate under the Bankruptcy (Scotland) Act 1985 or when he grants a trust deed for his creditors.
- 113(5) A company, partnership or individual shall also be treated as insolvent on the occurrence of any event corresponding to those specified in subsection (2), (3) or (4) under the law of Northern Ireland or of a country outside the United Kingdom.
- 113(6) Where a provision is rendered ineffective by subsection (1), the parties are free to agree other terms for payment. In the absence of such agreement, the relevant provisions of the Scheme for Construction Contracts apply

The Scheme for Construction Contracts.

- 114(1) The Minister shall by regulations make a scheme ("the Scheme for Construction Contracts") containing provision about the matters referred to in the preceding provisions of this Part
- 114(2) Before making any regulations under this section the Minister shall consult such persons as he thinks fit.
- 114(3) In this section "the Minister" means-
- (a) for England and Wales, the Secretary of State, and
 - (b) for Scotland, the Lord Advocate.
- 114(4) Where any provisions of the Scheme for Construction Contracts apply by virtue of this Part in default of contractual provision agreed by the parties, they have effect as implied terms of the contract concerned.
- 114(5) Regulations under this section shall not be made unless a draft of them has been approved by resolution of each House of Parliament.

Service of notices, &c.

- 115(1) The parties are free to agree on the manner of service of any notice or other document required or authorised to be served in pursuance of the construction contract or for any of the purposes of this Part
- 115(2) If or to the extent that there is no such agreement the following provisions apply.
- 115(3) A notice or other document may be served on a person by any effective means
- 115(4) If a notice or other document is addressed, pre-paid and delivered by post-
- (a) to the addressee's last known principal residence or, if he is or has been carrying on a trade, profession or business, his last known principal business address, or
 - (b) where the addressee is a body corporate, to the body's registered or principal office,
- it shall be treated as effectively served. (5) This section does not apply to the service of documents for the purposes of legal proceedings, for which provision is made by rules of court.
- 115(6) References in this Part to a notice or other document include any form of communication in writing and references to service shall be construed accordingly.

Reckoning periods of time.

- 116(1) For the purposes of this Part periods of time shall be reckoned as follows.
- 116(2) Where an act is required to be done within a specified period after or from a specified date, the period begins immediately after that date.
- 116(3) Where the period would include Christmas Day, Good Friday or a day which under the Banking and Financial Dealings Act 1971 is a bank holiday in England and Wales or, as the case may be, in Scotland, that day shall be excluded.

Crown application. 117 (1)–(3) omitted

THE SCHEME FOR CONSTRUCTION CONTRACTS - PART II - PAYMENT

Entitlement to and amount of stage payments

1. Where the parties to a relevant construction contract fail to agree -
- (a) the amount of any instalment or stage or periodic payment for any work under the contract, or
 - (b) the intervals at which, or circumstances in which, such payments become due under that contract, or
 - (c) both of the matters mentioned in sub-paragraphs (a) and (b) above,
- the relevant provisions of paragraphs 2 to 4 below shall apply.
- 2(1) The amount of any payment by way of instalments or stage or periodic payments in respect of a relevant period shall be the difference between the amount determined in accordance with sub-paragraph (2) and the amount determined in accordance with sub-paragraph (3).
- 2(2) The aggregate of the following amounts -
- (a) an amount equal to the value of any work performed in accordance with the relevant construction contract during the period from the commencement of the contract to the end of the relevant period (excluding any amount calculated in accordance with sub-paragraph (b)),
 - (b) where the contract provides for payment for materials, an amount equal to the value of any materials manufactured on site or brought onto site for the purposes of the works during the period from the commencement of the contract to the end of the relevant period, and
 - (c) any other amount or sum which the contract specifies shall be payable during or in respect of the period from the commencement of the contract to the end of the relevant period.

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- 2(3) The aggregate of any sums which have been paid or are due for payment by way of instalments, stage or periodic payments during the period from the commencement of the contract to the end of the relevant period.
- 2(4) An amount calculated in accordance with this paragraph shall not exceed the difference between -
- (a) the contract price, and
 - (b) the aggregate of the instalments or stage or periodic payments which have become due.

Dates for payment

3. Where the parties to a construction contract fail to provide an adequate mechanism for determining either what payments become due under the contract, or when they become due for payment, or both, the relevant provisions of paragraphs 4 to 7 shall apply.
4. Any payment of a kind mentioned in paragraph 2 above shall become due on whichever of the following dates occurs later -
- (a) the expiry of 7 days following the relevant period mentioned in paragraph 2(1) above, or
 - (b) the making of a claim by the payee.
5. The final payment payable under a relevant construction contract, namely the payment of an amount equal to the difference (if any) between -
- (a) the contract price, and
 - (b) the aggregate of any instalment or stage or periodic payments which have become due under the contract, shall become due on the expiry of -
 - (a) 30 days following completion of the work, or
 - (b) the making of a claim by the payee, whichever is the later.
6. Payment of the contract price under a construction contract (not being a relevant construction contract) shall become due on
- (a) the expiry of 30 days following the completion of the work, or
 - (b) the making of a claim by the payee, whichever is the later.
7. Any other payment under a construction contract shall become due
- (a) on the expiry of 7 days following the completion of the work to which the payment relates, or
 - (b) the making of a claim by the payee, whichever is the later.

Final date for payment

- 8(1) Where the parties to a construction contract fail to provide a final date for payment in relation to any sum which becomes due under a construction contract, the provisions of this paragraph shall apply.
- 8(2) The final date for the making of any payment of a kind mentioned in paragraphs 2, 5, 6 or 7, shall be 17 days from the date that payment becomes due.

Notice specifying amount of payment

9. A party to a construction contract shall, not later than 5 days after the date on which any payment -
- (a) becomes due from him, or (b) would have become due, if -
 - (i) the other party had carried out his obligations under the contract, and
 - (ii) no set-off or abatement was permitted by reference to any sum claimed to be due under one or more other contracts,
- give notice to the other party to the contract specifying the amount (if any) of the payment he has made or proposes to make, specifying to what the payment relates and the basis on which that amount is calculated.

Notice of intention to withhold payment

- 10 Any notice of intention to withhold payment mentioned in section 111 of the Act shall be given not later than the prescribed period, which is to say not later than 7 days before the final date for payment determined either in accordance with the construction contract, or where no such provision is made in the contract, in accordance with paragraph 8 above.

Prohibition of conditional payment provisions

11. Where a provision making payment under a construction contract conditional on the payer receiving payment from a third person is ineffective as mentioned in section 113 of the Act, and the parties have not agreed other terms for payment, the relevant provisions of -
- (a) paras 2, 4, 5, 7, 8, 9 and 10 shall apply in the case of a relevant construction contract, and
 - (b) paras 6, 7, 8, 9 and 10 shall apply in the case of any other construction contract.

Interpretation

12. In this Part of the Scheme for Construction Contracts -
- "claim by the payee"** means a written notice given by the party carrying out work under a construction contract to the other party specifying the amount of any payment or payments which he considers to be due and the basis on which it is, or they are calculated;
- "contract price"** means the entire sum payable under the construction contract in respect of the work;
- "relevant construction contract"** means any construction contract other than one -
- (a) which specifies that the duration of the work is to be less than 45 days, or
 - (b) in respect of which the parties agree that the duration of the work is estimated to be less than 45 days;
- "relevant period"** means a period which is specified in, or is calculated by reference to the construction contract or where no such period is so specified or is so calculable, a period of 28 days;
- "value of work"** means an amount determined in accordance with the construction contract under which the work is performed or where the contract contains no such provision, the cost of any work performed in accordance with that contract together with an amount equal to any overhead or profit included in the contract price;
- "work"** means any of the work or services mentioned in section 104 of the Act.