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Changes to construction contracts

Special report on changes to construction contracts to come into force on 1 October 2011

The statutory framework that governs all construction contracts is changing on 1 October 2011.

Part II of the Housing Grants, Construction and Regeneration Act 1996 ("HGCRA 1996") regulates the payment and dispute resolution provisions in construction contracts. Part 8 of the Local Democracy, Economic Development and Construction Act 2009 ("LDEDC 2009") introduces a number of key changes to these existing requirements. A commencement order has now been issued confirming that these changes are going to come into force on 1 October 2011.

Who will the changes affect?

All construction contracts (as defined in the HGCRA 1996) entered into on or after 1 October 2011 will have to comply with the new regime. The LDEDC 2009 is not retrospective, and so existing construction contracts operating after 1 October will not be affected. However, the changes do pose some practical issues.

There will inevitably be projects where contracts are completed both pre and post 1 October 2011. In this circumstance, different contracts, sub-contracts and professional appointments on the same project will be governed by two separate statutory provisions.

Similarly, construction contracts called off under existing framework agreements on or after 1 October 2011 will have to comply with the new rules whereas contracts previously called off will not be subject to the changes.

What is changing? The headlines

Payment

- Further restrictions on conditional payments are being introduced by the LDEDC 2009. Clauses stating that a sub-contractor will only become entitled to payment when a certificate is issued under the main contract for its work will be outlawed (often referred to as "pay-when-certified" clauses). However it is intended that PFI construction sub-contracts will not be subject to the restriction on pay-when-certified clauses and a draft exclusion order has been issued to this effect.

- Payment notices will have to be issued even if the sum due is zero. If a payment notice is not issued by the date for doing so, the party due to receive payment can issue a default payment notice.
- Withholding notices are being replaced with pay less notices, although the differences are largely of form rather than substance. One key change is that pay less notices cannot be combined with payment notices as was the case with withholding notices.

Suspension

- Currently, the ability of a party to suspend performance for non-payment is an “all or nothing” right; it cannot pick and choose which obligations to suspend. Under the new rules, a party can instead opt to suspend performance of any rather than all of its obligations.
- The LDED 2009 introduces a new right for the suspending party to receive payment of a reasonable amount for the costs and expenses incurred in exercising its right to suspend. It can also have any time spent remobilising taken into account in an extension of time claim.

Adjudication

- One of the biggest changes being introduced is that construction contracts will no longer have to be in writing. It will therefore be possible to bring adjudications under contracts that are wholly or partly oral.
- There is a new statutory slip rule which allows an adjudicator to correct a clerical or typographical error in a decision after it has been published.
- There is a new provision prohibiting parties from agreeing in advance who will pay the costs of an adjudication. This outlaws so called “Tolent Clauses” which required the party referring a dispute to adjudication to pay the costs of both parties regardless of the outcome.



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The Scheme

- The Scheme for Construction Contracts contains provisions that are imported into construction contracts where they do not contain clauses that satisfy the requirements of the HGCRA 1996. The Scheme is also changing to be compliant with the new rules, although the proposed amendments to the Scheme are still in draft form.

Comment

Whilst the changes being introduced by the LDED 2009 are not as far reaching as they might have been, there are a number of important provisions that will impact upon the drafting and operation of construction contracts after 1 October 2011.

In particular there are subtle differences in the payment regime, and it will be easier for contractors to suspend performance for non-payment. The ability to adjudicate wholly oral contracts is likely to lead to increased adjudication and extensive debate about the terms of such contracts. Employers, contractors and consultants will all need to ensure they are familiar with and prepared for these changes in advance of 1 October 2011 so that minimum inconvenience is caused to existing and new projects when they come into effect.

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