AGGREGATE

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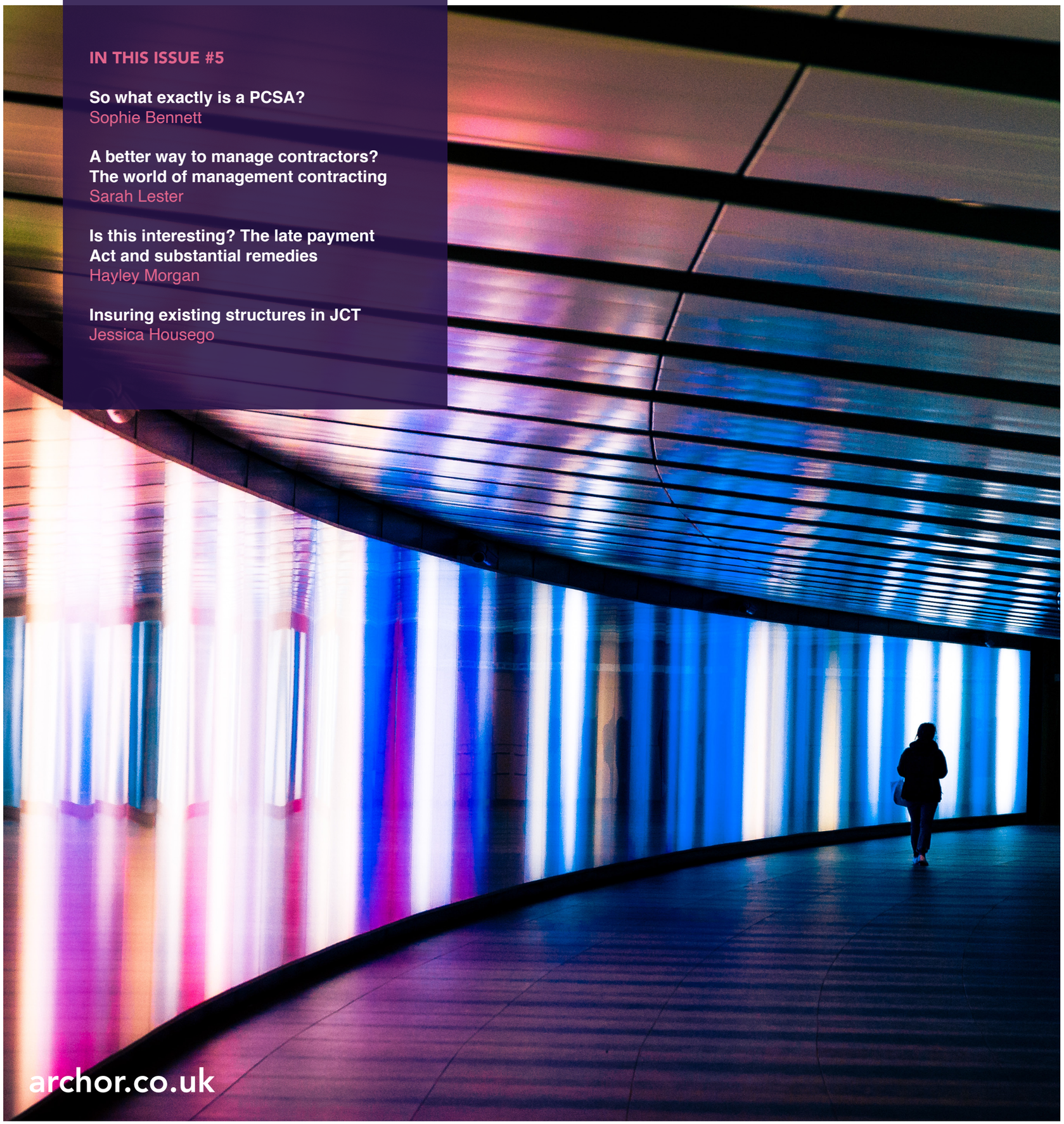

IN THIS ISSUE #5

So what exactly is a PCSA?
Sophie Bennett

A better way to manage contractors? The world of management contracting
Sarah Lester

Is this interesting? The late payment Act and substantial remedies
Hayley Morgan

Insuring existing structures in JCT
Jessica Housego

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Welcome to the latest edition of **Archor's Aggregate** newsletter.

This edition focuses on getting contracts right from the start. We have two articles looking at non-traditional forms of contract. First, Sophie discusses what a PCSA is (a pre-construction services agreement…), something of a follow up to Carolyn's article on LOIs (letters of intent) in our last edition. Then, Sarah considers Management Contracting and asks why it's not as popular as other forms of the JCT suite.

Hayley has an interesting article (pun entirely intended) on statutory interest, considering in particular how to know if you've got a 'substantial remedy' for late payment in your contract (and what to do if you haven't). And finally, Jessica runs through JCT insurance options, including a reminder of the risks of not thinking properly about insurance at the outset (and in particular ticking Option C without understanding what it means!).

We hope you enjoy this edition, wherever you may be reading it – prizes will be available for the best picture of someone enjoying Aggregate on a beach, and for the most exotic reading location! And as ever, if you have any ideas for future articles or other feedback, do please get in touch.

Oli, Editor-in-Chief

So what exactly is a PCSA?

At its simplest, a PCSA is a Pre-Construction Services Agreement.

In many ways, it does exactly what it says on the tin: it's a contract entered into before a formal building contract to provide specified services prior to the full build. They are often used in two-stage tendering for design input and to get advice and costs information from a contractor, usually while full building contract negotiations are ongoing with the same contractor.

But isn't that a letter of intent?
PCSAs and Letters of Intent (LOIs) are similar, but they serve different purposes. PCSAs can take longer to negotiate than LOIs as they essentially carry a 'stand-alone' set of services that can be pared away from the main contract, and sometimes aren't subsumed into the main contract, particularly if a different contractor is then selected for the main build. PCSAs are often used where the employer wants advice on buildability, programming and management, all of which are needed before the build, or even some design works, can go ahead. The terms and conditions of these pre-services are fully negotiated and recorded as a contract, giving both parties the comfort of a sturdy contract and a clear scope of what is required of the contractor.

A LOI, however, is a 'stand-in' for a building contract in the event the full scope of services and/or a building contract is still being negotiated but the employer wants work to be starting on-site as they have their plans, designs and management all ready to go. A good LOI will cover the same liabilities of a building contract before being subsumed into the final contract where all of the services and terms have been fully hashed out. Carolyn wrote about LOIs in the last edition of Aggregate, if you missed it.

This sounds like what I need…what are the benefits?
Well, if you want to get going on the project a little earlier and had been considering an LOI, PCSAs can be useful for commencing a project in advance of a full scope of works or design packages. For example, you might want some groundworks or demolition carried out, but you get the safety of a full contract instead of a risk-riddled LOI. You're also engaging your contractor a lot earlier, which can help build up a working relationship ready for your main phase; although, equally, if you realise that this contractor is not the right fit for you, you can get another one for the main works instead.

There might also be greater cost certainty and a lower risk of delay since your contractor is involved from the start of the project, and has a greater opportunity to have input on pricing on programming. Contractors also find PCSAs attractive as there might not be such a competitive pricing streak in two-staged tendering that single-stage tendering might have, plus they know exactly what they are getting themselves into (and have some input on that) from the outset.

Speaking of being riddled with risk, what do I need to be careful of with PCSAs?
Let's face it, legal fees are usually a big chunk of cost, and, unfortunately, a PCSA adds to this as it often involves more negotiation than an LOI given that it's more akin to a mini-building contract. They usually take more time to negotiate than a standard LOI as well, but you are getting more legal certainty and a surer footing than you could have with an LOI.

Similarly, a contractor engaged under a PCSA may feel as if it will 100% get that main contract as well, due to all the time, money and effort spent on a PCSA, and not price as competitively. The risk allocation under a PCSA often falls solely onto the contractor as well, rather than across a consultant team, so sub-contract inflation may occur as the contractor tries to alleviate some of its risk by passing it down its supply or work chains.

Great. Have you got a draft PCSA I can use?
The JCT has two forms of PCSA that you can use, and the NEC suites have optional clauses that can act as PCSAs (see NEC3 'early contractor involvement' clauses published in 2015, or option X22 for the NEC4 suite). A lot of law firms will also have bespoke PCSAs, or schedules of amendments to the JCT/NEC forms to tweak them perfectly for their clients' needs – we're no exception. Ultimately what's right for your specific project will depend on the circumstances, and it's worth spending a bit of time getting it right – so the standard forms might be right, but shouldn't be used an automatic solution.

Is that it?
Well, yes and no. It's the end of this article, but this is only a very brief overview of PCSAs. If you're an old hand at PCSAs, we've likely taught you nothing new – but if you've never heard of them, or heard of them only to move topic quickly, hopefully we've covered the basics. As ever, we're experts in this kind of thing – so if this has made you think a PCSA might be useful for you, please get in touch to discuss.

Sophie Bennett
Trainee Solicitor

A better way to manage contractors?

The world of management contracting

Although the JCT has published a management contract as a part of its suite for many years, it is fair to say that it is not winning any popularity contests! So, what is the management contract and why is it one of the least used forms of JCT contract?

What is management contracting?
Management contracting works on the basis that the Employer appoints a "Management Contractor" and a team of professional consultants, the "Consultant Team". As with the other forms of JCT contract, part of the Consultant Team includes a contract administrator who has responsibility for administering the management contract on the Employer's behalf.

The Management Contractor is responsible for the overall management of the Project and the site set up and is responsible for directly entering into and administering "Works Contracts" (essentially sub-contracts) for each of the work packages during the construction phase. There are two key stages: (1) the pre-construction stage, whereby the design is developed by the Consultant Team in conjunction with the Management Contractor; and (2) the construction phase, which starts with the Employer issuing a Notice to Proceed to the Management Contractor.

Once the Notice to Proceed has been issued, the Management Contractor has the authority to put the Works Contracts in place as and when required. The Employer does (quite unusually for JCT) retain the right throughout to terminate at will (albeit if they choose to exercise this right, they will be at risk of paying the Management Contractor's direct losses).

This does, however, mean that the Employer maintains a degree of control over the whole process as the Employer can put a stop to the project at any point, and reflects one of the key benefits of the management contract – its flexibility. The Employer can commence the works on site without all elements having been designed allowing the design to develop over time, while retaining control over it, all the while getting on with the elements of the works that can begin.

The management contract generally includes all of the elements that you would expect from a JCT contract, with the key difference between the management contract and other forms being that the Management Contractor is involved at a very early stage and works closely with the Consultant Team to develop the project and decide on how the works will be split down into the various Works Contracts. For this reason, it is important that care is taken over the appointment of the Management Contractor, who is usually an experienced contractor.

Why isn't it used more?
All sounds good so far, so why the reluctance to use it? Well, from the Management Contractor's perspective there are some significant risks as to how extensions of time and claims for loss and expense are managed. In terms of delay, the Management Contractor is potentially required to grant an extension of time to one Works Contractor, due to delays caused by another Works Contractor. This seems sensible, but in situations where the Management Contractor has caused or contributed to any default they will not be entitled to an extension of time.

This means that the Management Contractor could find themselves in a situation where they are obliged to grant an extension of time, without obtaining one themselves. Given that the Management Contractor is paid by way of a fee (and liable for liquidated damages in the event that the project has not achieved practical completion by the stated completion date), this is unlikely to be satisfactory to many contractors.

Further, in relation to claims made by a Works Contractor for a breach by the Management Contractor, the Management Contractor may, at the Employer's option, be required to either settle the claim (and pay any settlement figure) or defend it in proceedings. The Employer is not required to reimburse the Management Contractor for their costs in defending a claim, or any settlement figure in circumstances where the Management Contractor is in breach of contract or has acted negligently. Although again this seems reasonable, the issue for the Management Contractor is that for the Works Contractor to have made a claim against the Management Contractor, it is likely that there has been a breach. This is clearly an problematic position for the Management Contractor.

The future…
Although the construction management contract remains a good option for the right project, it is fair to say that it is not suitable in many situations. If it is the right approach for the project, care must be taken with the appointment of the Construction Manager and the Consultant Team, who will need to be suitably experienced to ensure the smooth running of the project (for all concerned).

So although there are definitely benefits, and some contractors are becoming more prepared to work as Management Contractors, don't expect to suddenly see the contract rivaling the D&B or SBC for popularity among the JCT ranks!

Sarah Lester
Senior Associate

Is this interesting?

Late payment Act substantial remedies

With interest and inflation rates constantly in the news recently, thinking about what contractual terms are 'fair' and 'reasonable' when it comes to interest is timely. Interest is something parties will seek on top of sums owed to them for late payment when in dispute, so it is important you ensure that any agreed terms are reasonable and, as some would say more importantly, what you can do if they aren't.

The Late Payments of Commercial Debts (Interest) Act 1998

The 1998 Act changed the landscape on interest. Prior to its introduction, interest could only be claimed if it was expressly provided for within the terms of the contract. However, following its introduction, implied terms surrounding interest became automatically incorporated into the contract where there isn't already a 'substantial remedy' for late payment.

These implied terms entitle the party owed a sum that is overdue to interest from the due date for payment, until payment is made. The Act also provides a set rate of interest, at 8% above base rate (also known as 'simple interest') which starts accruing from the day after the agreed payment date where such a payment date is specified.

What is a substantial remedy?

The courts have interpreted this widely and the remedy can be high. In Longulf Trading (UK) Ltd v. Niyazi Onen Gida Sanayi AS [2019], an interest at a rate of 15% per annum was held to be enforceable. In Biosol Renewables UK Ltd v. Lovering [2021] a provision providing an interest rate of 1.5% per month was also held to be a 'substantial remedy'. At the other end of the scale, rates as low as 2-3% per annum have been found to be 'substantial'.

What qualifies as a 'substantial remedy' was reviewed in a construction context in Yuanda v. WW Gear Construction Ltd [2010]. The court said that any interest remedy is 'substantial' unless: "It would not be fair or reasonable to allow the remedy to be relied on to oust or vary the right to statutory interest that would otherwise apply having regard to: the benefits of commercial certainty, the strength of the relative bargaining positions of the parties, whether the term was imposed by one party to the detriment of the other, and whether the supplier received an inducement to agree to the term".

In that case, the court was tasked with considering whether an amendment to the JCT form's default 5% above base rate interest allowance to 0.5% was a 'substantial remedy'. It said that absent special considerations – which might include evidence of negotiation of such a sum and reasons why it was justified, neither of which existed on the facts – the rate was clearly not a 'substantial remedy'.

The 2013 Regulations

In 2013, the 1998 Act was revised by two sets of Regulations. These bolstered the protection offered by the 1998 Act in several ways, including to provide implied terms to protect a party owed a sum in the event a payment date is not specified in the contract. As a result, interest accrues from 30 days after the latest of either delivery, invoice or acceptance.

When trying to assess the latest date a sum is deemed owed for interest to be calculated, try to think of the above as:

A – Acceptance: when were the goods or services (if any) accepted?

I – Invoice: what is the date of the last invoice from the party owed?

D – Delivery: when were the goods delivered or services performed on site?

It is important to note that the implied terms incorporated under the Act can be varied by express wording.

The 2013 Regulations also introduced the ability to recover reasonable debt recovery costs where the 1998 Act applies. The original act allowed fixed compensation depending on the level of debt, often in the low hundreds of pounds. But the 2013 Regulations improved this so that if the fixed sum was inadequate, whatever the reasonable costs of pursuing a debt were could be recovered through the Act. This was therefore a substantial improvement for those chasing money – although it should be noted that recovering these costs isn't possible through adjudication, where the courts have found that the Construction Act's prohibition on recovery of adjudication costs unless made in writing after service of the Notice trumps the 1998 Act.

Interest Free Period?

It's not just the rate of interest that you should be looking out for. Parties can delay the date from which interest will accrue on a sum owed, for example by agreeing a later payment date or adopting an acceptance procedure. This in turn effectively creates an 'interest free period'.

However, the Act and Regulations can help. If an agreed payment date is more than 60 days after the date of delivery, invoice or acceptance (whichever is the latest) and this is determined to be, in the circumstances, grossly unfair to the party being paid, then interest will run from the end of that 60 day period.

In relation to delays resulting from an 'acceptance procedure' the rules are a bit simpler. If the acceptance procedure under the contract lasts more than 30 days after delivery of the goods, and that is grossly unfair to the party owed the sum, then the acceptance procedure is deemed to be completed 30 days after the date of delivery. This means that the interest will run from the end of that 30 day period.

If a longer acceptance procedure is agreed in a contract and this is not deemed 'grossly unfair' to the party being paid in their specific circumstances, then interest will run from the end of that longer acceptance procedure.

What do you do if you think a term isn't a 'substantial remedy'?

The Courts, and adjudicators, must satisfy themselves that any interest provision is fair and reasonable. As mentioned above, they assess the circumstances of the parties and provisions against whether the wording "provides sufficient compensation for late payment, is fair and reasonable as against the statutory right and serves to deter late payment."

Therefore, no two matters can be looked at in the same way. It is vital you familiarise yourself with any terms relating to payments, delayed payments and entitlement to interest in order for an agreement to be made which satisfies both parties and is commercially reasonable. Failure to do so will likely mean the statutory interest provisions of the 1998 Act (amended by the Regulations) will come into force – together with giving the right to recover reasonable debt recovery costs.

Hayley Morgan
Paralegal

Insuring existing structures in JCT

Insurance provisions are an important part of a construction contract that provide protection against different types of risk. Each project will present different risks based on the design, surroundings, and nature of the project. However, regardless of the size and scope of the project, it is essential insurance is taken out to protect each party from liabilities.

In most of the JCT suite of contracts, Section 6 deals with the different types of insurance. The section is split into four parts: injury to persons and property; insurance against personal injury and property; insurance of the works; and professional indemnity insurance. This article focuses on insurance of the works, which is a type of insurance designed to protect building works in progress, covering for any loss or damage that happens during construction.

JCT options

There are three different options for insurance of the works in JCT standard forms:

- Option A, in which a joint-names all risks insurance of the works is taken out by the contractor;
- Option B, in which a joint-names all risks insurance of the works is taken out by the employer; and
- Option C, in which the employer takes out a joint names all risks insurance of the works and the policy also insures the existing structure and contents against 'specified perils'.

Options A and B

Options A and B are relatively straightforward. 'All risks' policies do exactly what they say on the tin: cover against all risks that might affect a construction project. They are specialist insurance policies that are joint insured, composite insurance policies designed for building works. They cover sub-contractors, remove any rights for the insurer to recover from the party at fault and have no rights of vitiation – this being that even if the premium is not paid the policy subsists.

Most main contractors will have a company-wide 'all risks' policy that new projects can be notified under to receive cover. Provided notified properly so that the employer's interest is as a joint-named holder (not just with their interest noted – a different and insufficient concept), Option A therefore makes the most sense for most projects.

In contrast, this type of insurance is very difficult for employers to obtain as they obviously typically have no record of building. So Option B is rarely a sensible choice.

Option C

Option C insurance is the only option that involves existing structures and refers to refurbishment and extensions. In fact, under Option C the employer will be required to take out and maintain two joint-names policies: a policy covering the costs of repair arising from damage to the existing structure and contents caused by 'Specified Perils' (such as fire and flood), and an 'all risks' policy covering the works themselves (as described above).

The former type of insurance covers Specified Perils rather than All Risks, but in practice covers fire, flood, storm etc, which are the normal risks. What this policy is intended to do is cover damage to the existing structure caused by, for example, a flood in the works.

The existing structures policy is required under the unamended JCT form to be on a joint names basis. Although the market does typically offer cover for damage to the existing structure, it will not usually offer it on a joint-names basis. The employer, therefore, will not be able to comply with the strict terms of the contract. If there is a claim and the employer does not have the right insurance, it will be in breach of the contract. The contractor would therefore have a defence to any claim on the basis had the employer complied with the terms of the contract, there would be no claim against the contractor, due to the policy having no rights of subrogation.
One way around this would be amending the standard form JCT to reflect, in particular, the scope of cover that the employer is able to procure.

Most typically this will remove the contractor as the joint insured in relation to the existing structures and will be relying instead on the scope of its public liability cover. Additionally, the employer should take out whichever policy it is able to and ensure the amendments to the contract effectively cover this.

In the JCT 2016 suit of contracts, the parties can replace paragraph C.1 with a "C.1 Replacement Schedule". This essentially allows the parties to agree an alternative arrangement for the insurance of the existing structures where a joint names policy cannot be obtained by the employer. This is a sensible way forward for parties that properly engage with the insurance provisions at the outset.

Conclusion

Regardless of the project, all parties need to ensure they have robust insurance provisions in their contracts, and conversations about these provisions should be started early to avoid delays to the works. Once it has been agreed which insurance options will be used, parties should be careful to ensure they procure the right policy – otherwise they will be in breach of contract and will face problems should a potential insurance claim ever arise.

And always remember – whatever issue you are facing with your Option C insurance, the answer probably lies in amending the contract!

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Trainee Solicitor

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