Explanatory Memorandum to the Scheme for Construction Contracts (England and Wales) Regulations 1998 (Amendment) (Wales) Regulations 2011 and the Construction Contracts (Wales) Exclusion Order 2011

This Explanatory Memorandum has been prepared by the Construction Unit of the Environment and Sustainability Directorate and is laid before the National Assembly for Wales in conjunction with the above subordinate legislation and in accordance with Standing Order 27.1.

Minister's Declaration

In my view, this Explanatory Memorandum gives a fair and reasonable view of the expected impact of the Scheme for Construction Contracts (England and Wales) Regulations 1998 (Amendment) (Wales) Regulations 2011 and the Construction Contracts (Wales) Exclusion Order 2011

John Griffiths AM

Minister for Environment and Sustainable Development.

17 June 2011

1. Description

1.1 These statutory instruments are intended to facilitate cash flow through the construction supply-chain and ensure disputes are dealt with promptly through adjudication.

2. Matters of special interest to the relevant Committee

2.1 None.

3. Legislative background

3.1 The Construction Act passed in 1996 set out a statutory framework to address issues relating to co-ordination failure between contractors. Following extensive consultation with industry stakeholders in 2005 and 2007 measures to amend the Construction Act were developed which streamlined the legal requirements to prevent areas which historically caused dispute whilst minimising burdens on both sets of contractors. These amendments were passed in primary legislation in 2009 but require changes to accompanying secondary legislation to become active.

3.2 These Statutory Instruments follow the affirmative resolution procedure.

4. Purpose and intended effect of the legislation

4.1 Coordination failures between construction contractors and sub-contractors cause commercial disputes with a financial cost of around £35m a year. Disputes also impact negatively on both project delivery and firms in the supply-chain. The current legislation, Part 2 of the Housing Grants, Construction and Regeneration Act 1996 (the Construction Act) sets out certain requirements for construction contracts which mitigate the costs of such disputes. However, a number of weaknesses have been identified with the legislation and following extensive consultation with industry stakeholders, measures were identified to 'fix' these weaknesses to yield further costs savings to business. The relevant measures were introduced at Part 8 of the Local Democracy, Economic Development and Construction Act 2009 ('the 2009 Act').

5. Application

5.1 These statutory instruments will apply in relation to construction contracts which relate to the carrying out of construction operations in Wales. The same changes are being made to construction contracts in England and Scotland all coming into effect on 1 October 2011.

6. Consultation

6.1 Details of the consultation undertaken are included in the Regulatory Impact Assessment.

6.6 Copies of the responses to the consultation can be found on the Welsh Government's web from 24 June 2011.

REGULATORY IMPACT ASSESSMENT

A regulatory impact assessment is presented in accordance with Standing Order 27.1 of the National Assembly for Wales. This assessment is based on the impact assessment undertaken by the Department for Business, Skills and Innovation (BIS) which in turn was informed by that undertaken in support of the amendments to Part 2 of the Housing Grants, Construction and Regeneration Act 1996 which formed part of the Local Democracy, Economic Development and Construction Act 2009 http://www.communities.gov.uk/documents/communities/pdf/1088220.pdf This is because the changes to the secondary legislation are required for the changes to the primary legislation to come into effect. The changes to the Scheme for Construction Contracts secondary legislation are consequential to the changes made in the 2009 Act.

The 2009 assessment produced by the Department for Communities and Local Government suggests that the secondary legislation proposed will yield cost savings to businesses in the UK, including those in Wales. A separate analysis for the construction industry in Wales has not been carried out because:

- the relatively modest scale of savings identified for the UK indicates it would be disproportionate to undertake a detailed separate impact assessment for Wales;

- The issues the proposed legislation is designed to address apply just as much to the construction sector in Wales as in the UK, suggesting that the work completed by BIS is relevant to the construction industry in Wales.

In light of the above, it is sensible to accept the BIS impact assessment as representative of the situation in Wales and pro-rate the costs and benefits for Wales. Construction accounts for approximately 6% of GVA in the UK and in Wales. Wales produces 3.7% of GB GVA. Therefore, the costs and benefits BIS identifies for the UK are pro-rated using a factor of 3.7%. The table below summarises the likely position for Wales that would result from the proposed legislation. The BIS impact assessment is included as an appendix and should be referred to for context on the cost and benefit calculations included in the summary table below. Note there are not any costs and benefits associated with the do nothing option (see Appendix 1 for GB wide assessment).

Background to the need for intervention

Coordination failures between construction contractors and sub-contractors cause commercial disputes with a financial cost of around £35m a year. Disputes also impact negatively on both project delivery and firms in the supply-chain. The current legislation, Part 2 of the Housing Grants, Construction and Regeneration Act 1996 (the Construction Act) sets out certain requirements for construction contracts which mitigate the costs of such disputes. However, a number of weaknesses have been identified with the legislation and following extensive consultation with industry stakeholders jointly undertaken in conjunction the Department for Business, Innovation and Skills, measures were identified to 'fix' these weaknesses to yield further costs savings to business. The relevant measures were introduced at Part 8 of the Local Democracy, Economic Development and Construction Act 2009 ('the 2009 Act').

The intention of this secondary legislation building on the measures introduced in the 2009 Act is to improve and deregulate the existing regulatory framework to minimise costs of adjudication and regulatory burdens to contractors and sub-contractors. The recommended amendments to the secondary legislation seek to:

• Increase transparency and clarity in the exchange of information relating to payments to enable the better management of cash flow and more effective dispute resolution;

• Encourage the parties to resolve disputes by adjudication, where it is appropriate and timely; and

• Strengthen the right to suspend performance under the contract.

Options

Option 1 - Do nothing:

The de-regulatory amendments and cost savings made to the primary legislation by the 2009 Act will not be realised unless consequential changes are made to the underpinning secondary legislation. The cost of maintaining the status quo is to continue with the defective legislation threatening the viability of individual businesses and the long-term health of the industry.

Option 2 - Amend the Secondary legislation underpinning the Construction Act to reflect the changes introduced to the legislation by the 2009 Act; and introduce a new Construction Contracts Exclusion Order. This is the preferred option as it will deliver a saving to business of approximately £265mn

Summary of Costs and Benefits (Wales)

Price Base Year 2010	PV Base Year 2010	Time Period Years 10	Net Benefit (Present Value (PV)) (£m)		
			Low: £7mn	High: £12mn	Best Estimate: £10mn

COSTS (£m)	Total Transition (Constant Price)	Years	Average Annual (excl. Transition) (Constant Price)	Total Cost (Present Value)
Low	£130,000	1	£22,000	£318,000
High	£511,000		£33,000	£792,000
Best Estimate	£255,000		£27,000	£492,000

Description and scale of key monetised costs by 'main affected groups'

The one-off costs of targeted regulation include the costs of re-writing standard forms of contracts and the requirement that industry read the guidance prepared that explains the changes. The range relates to the amount of time required to read and understand the guidance issued from 30mins to 2hrs with a best estimate of 1hr. Costs and also benefits relate to the greater clarity and certainty we are introducing into the payment framework.

Other key non-monetised costs by 'main affected groups'

Time taken to familiarise industry with new framework.

BENEFITS (£m)	Total Transition (Constant Price)	Years	Average Annual (excl. Transition) (Constant Price)	Total Benefit (Present Value)
Low	Optional		£932,000	£8,029,000
High	Optional		£1,402,000	£12,062,000
Best Estimate			£1,166,000	£10,057,000

Description and scale of key monetised benefits by 'main affected groups'

One example of the annual benefits from the legislative changes is the removal of the requirements to issue duplicate payment notices. In the case where the contract provides for 3rd party certification of the work (by for example an architect or engineer), a separate payment notice issued by the payer will no longer be required. This measure will save the industry in the region of £6m per annum.

Other key non-monetised benefits by 'main affected groups'

Many commentators say there is considerable benefit to be gained from effective cash flow management in construction. Work carried out for OGC identified improvements in payment practices which created clear entitlements (which the amended primary legislation does) could save 1-1.5% on the average project or £1bn to £1.5bn pa in Great Britain.

Source: BIS impact assessment. Text in the above was written by BIS. Numbers were pro-rated by EcAD.

Overview

Size of the industry

1. The legislation applies to contracts for construction work including mechanical, electrical, civil engineering and ground works. Construction accounts for over 8% of GVA and in Great Britain there are nearly 300,000 construction enterprises of which over 90% are small or micro businesses employing approximately 1.5m people[1].

2. Coordination failures between construction contractors and sub-contractors cause commercial disputes with a financial cost of around £35m a year. Disputes also impact negatively on both project delivery and firms in the supply-chain. Existing legislation (Part 2 of the Housing Grants, Construction and Regeneration Act 1996 (the Construction Act)) sets out certain requirements for construction contracts which mitigate the cost of such disputes. However, a number of weaknesses have been identified with the legislation and following extensive consultation with industry stakeholders, measures were identified to address these weaknesses to yield further cost savings to business. The relevant measures were introduced at Part 8 of the Local Democracy, Economic Development and Construction Act 2009 ('the 2009 Act').

3. The market failures at hand are the principal-agent relationship between contractors and sub-contractors, the conflict of interests between them, and the tendency of contractors to exhibit moral hazard. The economic activity within the construction sector involves numerous principal-agent relationships between a main contractor and sub-contractor, in which both have incentives to behave according to their own self interest. For example, the main contractor may want a contract for the lowest price, but a sub-contractor will want to achieve the highest price to maximise his profits. Having agreed a contract price, construction contractors often dispute the value of post contract variations. The specific failures addressed by the proposed amendments include:

    - Exploitation of 'loop-holes' that prevent the flow of money through the supply-chain; and.
    - lack of clarity relating to payment resulting in adverse effects on sub-contractors ability to manage cash flow

4. Disputes under construction contracts threaten and compromise the affordability and timely delivery of construction projects and the viability of individual businesses. This undermines the long-term health of the construction industry.

5. The 2009 Act's provisions will:

- improve access to adjudication and reduce the costs of the process; and
- improve the exchange of information relating to payment to enable parties to construction contracts to better manage cash flow, introducing greater clarity and transparency and removing administrative burdens.

6. For the measures introduced in the 2009 Act to be effective, consequential changes need to be made to the secondary legislation underpinning the Construction Act i.e. the Scheme for Construction Contracts (England and Wales) Regulations 1998.

[1] Finalised 2008 ABI Data

How the Legislation works

7. This impact assessment is concerned with 3 pieces of legislation which work together to create a statutory framework for construction contracts. The framework is as follows:

- The Construction Act requires construction contracts to do certain things. It does not generally specify how, leaving that for the parties to agree freely in contract.
- The Exclusion Order can limit the scope of the application of the Act where the Secretary of State deems fit. The Secretary of State has the power to exclude all or part of a specific type of contract from the application of the Act.
- Where a contract has failed to give proper effect to a requirement of the Construction Act, the relevant part of the Scheme for Construction Contracts (England and Wales) Regulations 1998 ("the Scheme") is implied into the contract. This ensures that parties to a construction contract continue to benefit from the protections and rights the Act provides.

BACKGROUND

8. Since coming into force on 1 May 1998, a number of concerns have been raised about the effectiveness of the Construction Act. In 2003/04, the then Cabinet Office, Better Regulation Executive carried out a review of the construction sector. One of the review's conclusions was that there was a need to review the "Construction Act" to identify how it could be improved. The Chancellor announced this review in his Budget Statement in 2004.

9. Extensive and prolonged consultation with the industry, in 2005, 2007 and 2008, confirmed that, while delivering a number of important benefits, the Act was defective in certain key respects which could only be dealt with through amendments to the primary legislation. These issues are addressed in the Local Democracy, Economic Development and Construction Act 2009 ('the 2009 Act').

10. Before the Act can come into force consequential changes must be made to the secondary legislation i.e. the Scheme for Construction Contracts (England and Wales) Regulations 1998.

Part 2 of the Housing Grants, Construction and Regeneration Act 1996 ("the Construction Act")

11. The Construction Act sets out a statutory framework for key aspects of construction contracts (for example on payment communication and dispute resolution). Generally, the Act requires these to be implemented through the construction contract.

12. These include:

- Providing a statutory right for parties to a construction contract to refer disputes to adjudication[2]
- Providing a right to interim, periodic or stage payments, making clear when payments become due, their amount and a final date for payment
- Preventing the payer from withholding money from the 'sum due' after the final date for payment unless he has given a withholding notice
- Providing a statutory right for the payee to suspend performance where a 'sum due' is not paid, or properly withheld, by the final date for payment; and

[2] Adjudication is a statutory right under the existing 1996 Construction Act. It is one of the remedies. The amendments in the 2009 Act deals with weaknesses and inefficiencies in the existing statutory adjudication process.

- Prohibiting the pay when paid clauses which delay payment until it is received by the payer

The Scheme for Construction Contracts (England and Wales) Regulations 1998

13. Where the contract omits to deal with an issue, or does so in a way which does not comply with the Construction Act, a 'fall back' is required so that the contract continues to comply. That is the function fulfilled by the Scheme for Construction Contracts (England and Wales) Regulations 1998 (SI 1998/649).

14. Where a contract is defective in a specific regard, the relevant part of the Scheme is "pasted" in. This means that the defect is rectified but the remainder of the contract terms continue as agreed between the parties.

15. The 2009 amendments to the primary legislation which the Scheme will give effect are also included in the Department's simplification plan. The costs and benefits from the primary legislation will not take hold until the secondary legislation is amended in line with the changes. The consequential amendments to the Scheme were subject to consultation in March 2010.

16. The industry and its contract writing bodies are currently engaged in an intensive round of redrafting to ensure that the industry's standard forms of contract reflect the changes introduced by the 2009 Act so that they are ready for autumn 2011.

The Construction Contract (England and Wales) Exclusion Order 1998 (SI/649)

17. The extensive consultation process and subsequent more detailed discussions with the Public Private Partnerships (PPP) industry Forum have identified a particular issue with the specific operation of PFI contracts and one of the changes introduced by the 2009 Act. To enable this to be dealt with – and to allow future flexibility – the 2009 Act amended the Secretary of State's existing exclusion order making powers (and provided powers to Welsh and Scottish Ministers) so that it could be applied proportionately. The power in the 1996 Act was broad and unspecific (i.e. a specific type of contract is either covered by the Act or it is not). The amended power in the 2009 Act allows the Secretary of State, Welsh and Scottish Ministers to exclude specific contract types from all or part of the Construction Act.

Background to this issue

18. The Construction Act prevents the use of "pay when paid" clauses in construction contracts as this was a commonly used contractual mechanism to delay payment to the supply-chain. Some firms in the industry have avoided the effect of this by making payment dependent on the issue of a certificate (e.g. a valuation of the work by the client's agent) under the superior contract. The 2009 Act closes this loophole by preventing any contract term which makes payment conditional on the performance of an obligation under a superior contract.

19. In traditional construction contracts, this amendment to the 1996 Act places an annual cost on the industry of £325,000[3] as it requires the issue of a notice by the contractor to a sub-contractor setting out what will be paid and when where a contractor is currently able to rely on a notice issued under his contract with the client. Requiring the issue of such a notice is however of significant benefit to small and micro firms in construction supply chains in terms of the greater clarity and certainty of cash flow which it will deliver by requiring that they are directly notified what they would be paid and when it would be paid.

[3] Figure comes from *Improving payment practices in the construction industry: June 2007*

Basis for the exercise of the Exclusion Order making process

20. Different circumstances exist in contracts between PFI Special Purpose Companies (SPC) and the Construction sub-contractor than those which prevail in traditional construction sub-contracts. The SPC's contract with the public sector authority and the SPC's contract with its construction contractor is a standard one developed by Government. While payment under these contracts can depend on the issue of a certificate under the SPC's contract with the public sector authority, issues around clarity and certainty are effectively dealt with in that standard form of contract. Furthermore, a different incentive structure exists in pfi contracts than that which applies in more traditional forms of contracting. The Construction Contractor is in almost all cases part of the SPC – along with the FM contractor and the organisation providing finance. It is therefore to the direct benefit of the construction contractor to limit the amount of capital in the SPC. Removing the need to provide a contingency for funding a payment from the SPC to the construction contractor reduces the amount of capital required by the SPC and therefore the cost of capitalising it to the construction contractor.

21. The Construction Contracts (England and Wales) Exclusion Order 1998 already excludes PFI head contracts (i.e. the contract between the public authority and the SPC) from the entirety of the 1996 Act. The new Exclusion Order will extend that so that it also excludes the pfi construction contract from the application of the clause which prevents a party to a construction contract making a payment dependent on the performance of obligations under a superior contract.

Problem under consideration

22. The conflict of interests that occurs between contractors and sub-contractors often leads to disputes. A DTI survey estimated that there were 1,750 adjudications in 2007 in England and Wales at an average financial cost of £20,000 per adjudication[4]. Thus the total financial cost[5] of adjudication in England and Wales can be estimated at £35m per year.

23. Contracts between contractors and sub-contractors can mitigate such disputes and costs, but conflicting interests also mean that both parties will to manipulate the contracts to suit their views. The main contractor can be in a dominant position in any contractual arrangement which can work against the sub-contractor.

Rationale for Government Intervention

24. The central problem at hand is the **principal-agent relationship** between contractors and sub-contractors, the **conflict of interests** between them, and tendency of the sub-contractor to exhibit **moral hazard**. The economic activity within the construction sector involves the interaction between many sets of contractors over long periods of time. This typically involves numerous principal-agent relationships between a main contractor and sub-contractor, in which both have incentives to behave according to their own self interest. For example, the main contractor may want a contract delivered at the lowest price, but a sub-contractor may have an incentive to increase price and his profit. Both might seek to do this through contract variation post award.

25. Contractual clauses that might prevent or mitigate such disputes are not agreed because of conflicting interests between parties. Improved clarity in contractual arrangements between contractors and sub-contractors can minimise such coordination failures and the burdens and costs that result.

[4] *Improving payment practices in the construction industry: June 2007*

[5] Total economic cost would need to include additional costs such as the opportunity cost of time invested by both parties and the cost of appeal procedures.

26. The Construction Act passed in 1996 set out a statutory framework to address issues relating to co-ordination failure between contractors. Following extensive consultation with industry stakeholders in 2005 and 2007 measures to amend the Construction Act were developed which streamlined the legal requirements to prevent areas which historically caused dispute whilst minimising burdens on both sets of contractors. These amendments were passed in primary legislation in 2009 but require changes to accompanying secondary legislation to become active. The specific amendments to the legislation are described in table 1 below.

Table 1: Changes to the Construction Act contained within 2009 amendments

Measure (s) included in the 2009 Act	**Why change is necessary**
Removing restriction on who can serve a payment notice	The current statutory framework can create, in certain circumstances requirements to serve a duplicate notice. This measure removes that duplication allowing anyone who is named in the contract to issue the payment notice (currently only the payer can)
Clarity of the content of payment and withholding notices	The current statutory framework can fail to provide a clear explanation of the amount due. The measure provides the payee with details of what they will be paid and how that amount (even if that amount is Zero) has been calculated subject to any subsequent amendment.
A 'fall back' provision which allows the payee to submit a payment notice in default of the payer's notice after the payment due date.	Provides a default mechanism (i.e. it allows the payee to issue the notice if the payer doesn't) thereby allowing the speedy '"crystallisation" of a debt.
Prohibiting payment by reference to other contracts	The Construction Act prevented the use of "pay when paid" clauses in construction contracts. Some firms in the industry have avoided the effect of this by making payment dependent on the issue of a certificate (e.g. a valuation of the work by the client's agent) under the superior contract. We have therefore closed this loophole by preventing any contract term which makes payment conditional on the performance of an obligation under a superior contract. Although, this will place an annual cost on the industry of £325,000 as it will require the issue of a payment notice by the contractor to a sub-contractor setting out what will be paid and when where a contractor is currently able to rely on a notice issued under his contract with the client. It is however of significant benefit to small and micro firms in construction supply chains in terms of the greater clarity and certainty of cash flow which it will deliver.
A statutory framework for the costs of the adjudication	The current legislation is silent on adjudication costs which allows parties to include contractual terms to create a disincentive to use adjudication e.g. by requiring the sub-contractor to pay all the costs of the adjudication irrespective of the decision.

Requirement for contracts to be 'in writing'	A large number of construction contracts contain orally agreed terms or variations. Extending the application of the Construction Act to oral and partly oral construction contracts makes adjudication more widely available. In addition, it had become common practice to challenge an adjudicator's jurisdiction on the basis that not all the contract was in writing as a way of frustrating the process and increasing cost. This removes the problem.
Suspension of performance for non-payment	This proposal makes more equitable the statutory right for the payee to receive compensation for losses caused by the suspension. The payee will also have a sufficient length of time to remobilise on site. This makes it easier for the payee to suspend (or threaten to suspend) performance Threat of having to pay the additional costs of suspension incurred by the payer is intended to incentivise the payer to administer payment in a fair way.

Policy Objective

27. To amend the existing regulatory framework and remove burdens in order to:

- Increase transparency and clarity in the exchange of information relating to payments to enable the better management of cash flow and more effective dispute resolution;
- Encourage the parties to resolve disputes by adjudication, where it is appropriate, rather than by resorting to more costly and time consuming solutions such as litigation; and
- Strengthen the right to suspend performance under the contract.

Description of options considered

Option 1 – Do nothing

28. The market failures at hand are the principal-agent relationship between contractors and sub-contractors, the conflict of interests between them, and the tendency of contractors to exhibit moral hazard. The economic activity within the construction sector involves numerous principal-agent relationships between a main contractor and sub-contractor, in which both have incentives to behave according to their own self interest. For example, the main contractor may want a contract delivered at the lowest cost, but a sub-contractor may have an incentive to increase cost so they undertake more paid work. The specific failures addressed by the proposed amendments include:

- Exploitation of 'loop-holes' stopping the flow of money through the supply-chain; and.
- lack of clarity relating to payment resulting in adverse effects on sub-contractors cash flow

29. These failures were confirmed by evidence gathered from *Improving payment practices in the construction industry* consultations in addition to representations from various sectors of the construction industry.

30. The costs therefore of maintaining the status quo is to fail to deliver the de-regulatory and simplification benefits accredited to these measures under the construction contracts which may eventually threaten the viability of individual businesses and undermine the long-term health of the construction industry.

Option 2- Amend the Scheme for Construction Contracts (England and Wales) Regulations 1998 and introduce a Construction Contracts (Wales) Exclusion Order 2011

31. The changes to the primary legislation were necessary to improve the operation of the Construction Act. However, none of these benefits can be realised without making the necessary amendments to the secondary legislation which underpins the Construction Act i.e. the Scheme for Construction Contracts (England and Wales) Regulations 1998. We are also introducing a new Construction Contracts (Wales) Exclusion Order to exempt certain contracts from a specific aspect of the Act. These amendments will bring significant benefits to small and micro firms in the construction supply-chains in terms of greater clarity and certainty of cash flow which it will deliver.

32. The changes will produce substantial benefits for the industry each year. The detail of how the costs and benefits are calculated for each amendment is presented below.

33. This Impact Assessment contains substantially the same costs and benefits calculations supporting the Local Democracy Economic Development and Construction Bill which received Royal Assent in November 2009 ('the 2009 Act') http://www.communities.gov.uk/documents/communities/pdf/1088220.pdf. This is because the consequential changes to secondary legislation are required for the changes in the primary legislation to come into effect. Some costs and benefits have been updated where appropriate in line with further data and evidence. We are presenting, in table 2 below, the costs for primary and secondary because the costs and benefits from both sets of legislation will not come into effect without the amendments to the secondary.

34. The various contract writing bodies will need to alter their standard forms of contract. As an example, the Joint Contracts Tribunal (JCT) has some 50 contracts to attend to and these would potentially need to be revised and updated as the transition was made from one statutory framework to another. The extent and nature of the regulation (and whether Counsels opinion would need to be sought) would determine how long the transition would take. The shortest time has been roughly estimated at about 5 months stretching out to more than 12 months if the regulations were particularly complex or he changes radical. It is estimated that it costs on average £833 to update each contract template leading to a total cost of about £42k.

35. The new regulations will require industry to familiarise itself with the new requirements and protocols through guidance that has been prepared explaining the changes. Discussions with industry stakeholders confirm that this should take no more than one hour[6]. Using Office of National Statistics data, the average hourly rate for a construction manager is approximately £23 per hour[7]. If we assume that one person from each of the 300,000 enterprises reads through the Guidance, the cost to industry equates to approximately £6.9m. In order to take into account the fact that it may take some companies more or less time than the 1hr estimated, we provide a range based on all companies taking just 30 minutes in a best case, or a relative worst case that

[6] Informal consultation with several private sector industry stakeholders: May 2011

[7] Data comes from the Office of National Statistics Annual Survey of Hours and Earnings (ASHE) 2010 (£19.11p/h), uprated by 21% to take account of non-wage labour costs, as per general BIS practice.

it could take 2hrs per enterprise. The range of familiarisation costs in this instance is £3.5m - £13.8m. Our best estimate though is £6.9m as discussed above as this is based on information received through informal consultation with industry experts.

Wider Impacts

Small firms

As part of earlier consultations (BERR) (now BIS) invited stakeholders of all sizes to voice their concerns/views either through their federations, trade associations or as individuals. There has been strong support from representatives of small firms for the Construction measures. An example of this is a quote from the Federation of Master Builders (FMB) who said:

"*The FMB strongly supports efforts by BERR to improve payment practise in the construction industry and commend the years of hard work and commitment of the department, without which these proposals would have been lost, to the detriment of the whole industry.*

FMB strongly supports the proposals and is of the view that they will bring about genuine improvements to payment practices in the industry"

Given this general industry context, engagement of small firms, at all points in the supply chain, has been fundamental to the development of these proposals.

There have been a numerous stakeholder events during the Construction Act review. Those attending have included construction trade associations whose main membership consists of small firms and other industry stakeholders. The National Specialist Contractors Council and the Specialist Engineering Contractors Group in particular have been very helpful in ensuring that representatives from SMEs attended these events (and in encouraging firms from within their membership to respond to the March 2005 consultation exercise). The purpose of these events was to encourage those who would be affected by the measures to voice their concerns and come up with suggestions for amending the Construction Act.

The cost of monitoring cash flow, negotiating credit as well as the financing costs and administration, information and legal cost involved in disputes can bear disproportionately on smaller businesses. Not only does this constrain development by increasing relative costs and reducing the ability of small businesses to compete but it can also divert resources from training, innovation and management.

The benefits of the proposed amendments to small and micro businesses are:

- introducing greater transparency and clarity into the payment framework to facilitate better management of cash flow – "crystallizing the debt"
- increasing access to adjudication – the simple mechanism for resolving disputes
- improving communication between payer and payee on what will be paid and when
- encouraging prompt administration and communication of payment and improving the efficiency and productivity in the industry; and
- enabling the parties to continue to work together effectively to deliver high quality construction projects on time and on budget.

Statutory duties (GOWA 2006) of Welsh Ministers and their sectoral interests

Sectors

Local government (queries to LGF Mailbox)

There are not considered to be any specific impacts on local government, local government as a procurer of construction contracts is however likely to benefit from reduced risk of dispute related costs and delays to contracts arising out of the measures in this order.

Voluntary Sector (contact the Voluntary Sector Unit)

There are not considered to be specific impacts on the voluntary sector. Where it procures construction contracts there are likely to be similar benefits to those that could accrue to local government.

Duties

Equality of Opportunity

After initial consideration as to the potential impact of this policy/regulation on race, disability and gender equality it has been decided that there will not be a major impact upon minority groups in terms of numbers affected or the seriousness of the likely impact, or both.

The amendments to the Construction Act will have the following benefits:-

- Improving the operation of the existing legislation by introducing greater clarity and transparency and reducing disincentives to use adjudication where appropriate;
- Help to maintain a level playing field in a competitive market with a large proportion of small firms; and
- Underpin existing best practice in the industry.

The amendments will also make the system fairer – providing the often smaller parties to construction contracts (the sub-contractors) with greater certainty about what they will be paid and when. Where the parties disagree as to the amount to be paid, the amendments will make it easier to refer the dispute to adjudication - a quick (28-day) dispute resolution regime. They will better enable contractors to plan cash flow, address poor performance, and potentially improve liquidity and reduce the costs of servicing debt. They are intended to benefit small businesses in particular.

The Welsh language (contact Welsh Language & Media Policy Unit)

There not considered to be any Welsh Language issues arising out of this order

Sustainable development (contact the Strategic Delivery and Sponsorship Branch)

This order will support economic aspects of the Welsh Government's duty to promote sustainable development.

Competition Assessment

The construction industry is extremely competitive. There is no dominant firm in the construction sector. Many firms report very low margins. Competition is healthy to the point of sometimes being extremely fierce affecting profitability.

Similarly, there is no small key group of dominant firms in any sub-sector other than perhaps some very small specialists. The legislation does not set up barriers to entry to any sectors of the construction industry and is unlikely to affect the size of firms or number, though it may reduce the churn brought about by the combination of insolvencies and new firms being established.

The Competition Assessment filter indicated no risk of a significant detrimental effect on competition.

The competition filter test	
Question	**Answer yes or no**
Q1: In the market(s) affected by the new regulation, does any firm have more than 10% market share?	yes
Q2: In the market(s) affected by the new regulation, does any firm have more than 20% market share?	no
Q3: In the market(s) affected by the new regulation, do the largest three firms together have at least 50% market share?	no
Q4: Would the costs of the regulation affect some firms substantially more than others?	no
Q5: Is the regulation likely to affect the market structure, changing the number or size of businesses/organisation?	no
Q6: Would the regulation lead to higher set-up costs for new or potential suppliers that existing suppliers do not have to meet?	no
Q7: Would the regulation lead to higher ongoing costs for new or potential suppliers that existing suppliers do not have to meet?	no
Q8: Is the sector characterised by rapid technological change?	no
Q9: Would the regulation restrict the ability of suppliers to choose the price, quality, range or location of their products?	no

Consultation

The England consultation followed on from the joint Department for Business Innovation and Skills (then DTI)/Welsh Assembly Government joint consultations of 2005 and 2007 on proposals drawn from Sir Michael Latham's report on the operation of Part 2 of the Housing Grants, Construction and Regeneration Act 1996 ("the 1996 Act").
The purpose of the Welsh consultation was to seek views on the consequential amendments necessary to the Scheme for Construction Contracts (England and Wales) Regulations 1998 following the changes introduced at Part 8 of the Local Democracy, Economic Development and Construction Act 2009 to amend the 1996 Act; and on proposals put forward by the Construction Umbrella Bodies Adjudication Task Group (CUBATG) to improve the effectiveness of the Scheme.
The consultation which took place in Wales relates to construction contracts in Wales. A parallel consultation was undertaken on the same proposals in England by the Department for Business, Innovation and Skills, (BIS) and in Scotland by the Scottish Executive.

List of consultees

Construction Industry Council
Specialist Engineering Contractors' Group
Public Sector Construction Clients' Forum
Strategic Forum for Construction
National Specialist Contractors Council
Construction Confederation
Construction Skills
Federation of Master Builders
UK Contractor's Group
CBI Construction Council/CBI Wales
Civil Engineering Contractor's Association
National Federation of Builders
Construction Products Association
Constructing Excellence Wales
Technology and Construction Solicitors' Association
Considerate Contractors Scheme
Consortium of Local Authorities in Wales
Chartered Institute of Arbitrators (Wales Branch)
Community Housing Cymru
Royal Institution of Chartered Surveyors (Wales)
Royal Society of Architects Wales

The organisations consulted have been taken from a standard list of organisations to be consulted in Wales for any proposed changes to legislation covering the construction industry.

The consultation commenced on 21 March and ended on 18 June 2011.

A summary of the outcome of the consultation will be made available from 24 June 2011 on the Welsh Government website under consultations.

Enforcement, Monitoring and sanctions

It is not proposed to change the enforcement mechanisms introduced through the original legislation. The main enforcement mechanism for the legislation other than the courts or arbitration is the adjudication process, which the legislation provides. The decision of the adjudicator is binding on the parties and enforceable through summary judgement in court.

The only sanction being introduced is where an application for payment becomes due if the payer fails to issue a payment notice. No other sanctions are proposed.

Summary and recommendation

This package of measures strikes a fine balance between:

- the need to improve the effectiveness of the Construction Act by:
- Improving the transparency and clarity in the exchange of information relating to payments to enable the parties to construction contracts to better manage cash flow; and
- Encouraging the parties to resolve disputes by adjudication, where it is appropriate, rather than resorting to more costly and time consuming solutions such as litigation

- The important principle of not unduly upsetting the compromise between all sectors of the construction industry which underpinned the introduction of the original legislation in 1996.

36. It is recommended that the proposed regulatory changes be proceeded with.

Post Implementation Review

The Department for Business, Innovation and Skills (BIS) has committed to undertake a review of the effectiveness of the changes to the Construction Act in due course. The objective of the review would be to ensure that the changes to the legislation were effective in improving certainty and clarity. The Welsh Government will work with BIS on that review. The baseline would be the number of disputes adjudicated. The review would consider the number of disputes being referred to the courts for final judgements and payment days as well as a "satisfaction" survey. It would be expected to see an increase in the number of disputes adjudicated and a decrease in the number of adjudications being referred to the courts. Adjudication amendments should see a reduction in payment days. It is also expected to see the costs of adjudication come down. BIS will continue to work with the Construction Umbrella Bodies Adjudication Task Group (CUBATG) to gauge whether the adjudication amendments have had the necessary impact and would continue to monitor the survey work on adjudication being by industry and academia e.g. the Adjudication Reporting Centre at Glasgow Caledonian University.

Appendix 1 BIS RIA (GB)

Summary: Analysis and Evidence

Policy Option 1 Do Nothing

Description:

Price Base Year 2010	PV Base Year	Time Period Years	Net Benefit (Present Value (PV)) (£m)0		
			Low: 0	High: 0	Best Estimate: 0

COSTS (£m)	Total Transition (Constant Price)	Years	Average Annual (excl. Transition) (Constant Price)	Total Cost (Present Value)
Low	0		0	**0**
High	0		0	**0**
Best Estimate	0		0	**0**

Description and scale of key monetised costs by 'main affected groups'

No monetised costs.

Other key non-monetised costs by 'main affected groups'

The costs of maintaining the status quo are continued escalation of disputes under construction contracts that may eventually threaten the viability of individual businesses and undermine the long-term health of the construction industry. In addition, the benefits which are expected to arise from the amended primary legislation will not be realised.

BENEFITS (£m)	Total Transition (Constant Price)	Years	Average Annual (excl. Transition) (Constant Price)	Total Benefit (Present Value)
Low	0		0	**0**
High	0		0	**0**
Best Estimate	0		0	**0**

Description and scale of key monetised benefits by 'main affected groups'

No monetised benefits from no change to status quo

Other key non-monetised benefits by 'main affected groups'

Key assumptions/sensitivities/risks **Discount rate (%)** N/A

Direct impact on business (Equivalent Annual) £m):				
Costs: £0	**Benefits:** £0	**Net: £0**		

Summary: Analysis and Evidence Policy Option 2 (Preferred Option)

Description:

Price Base Year 2010	PV Base Year 2010	Time Period Years 10	Net Benefit (Present Value (PV)) (£m)		
			Low: £196**mn**	High: **£317mn**	Best Estimate: £259mn

COSTS (£m)	Total Transition (Constant Price)	Years	Average Annual (excl. Transition) (Constant Price)	Total Cost (Present Value)
Low	£3.5m	1	£0.588mn	**£8.6mn**
High	£13.8m		£0.88mn	**£21.4mn**
Best Estimate	£6.9m		**£0.735**	**£13.3mn**

Description and scale of key monetised costs by 'main affected groups'

The one-off costs of targeted regulation include the costs of re-writing standard forms of contracts and the requirement that industry read the guidance prepared that explains the changes. The range relates to the amount of time required to read and understand the guidance issued from 30mins to 2hrs with a best estimate of 1hr. Costs and also benefits relate to the greater clarity and certainty we are introducing into the payment framework.

Other key non-monetised costs by 'main affected groups'

Time taken to familiarise industry with new framework.

BENEFITS (£m)	Total Transition (Constant Price)	Years	Average Annual (excl. Transition) (Constant Price)	Total Benefit (Present Value)
Low	Optional		£25.2mn	**£217.4mn**
High	Optional		£37.9mn	**£326mn**
Best Estimate			**£31.5mn**	**£271.8mn**

Description and scale of key monetised benefits by 'main affected groups'

One example of the annual benefits from the legislative changes is the removal of the requirements to issue duplicate payment notices. In the case where the contract provides for 3rd party certification of the work (by for example an architect or engineer), a separate payment notice issued by the payer will no longer be required. This measure will save the industry in the region of £6m per annum.

Other key non-monetised benefits by 'main affected groups'

Many commentators say there is considerable benefit to be gained from effective cash flow management in construction. Work carried out for OGC identified improvements in payment practices which created clear entitlements (which the amended primary legislation does) could save 1-1.5% on the average project or £1bn to £1.5bn pa.

Key assumptions/sensitivities/risks **Discount rate (%)** 3.5%

Sensitivity analysis has been applied to key assumptions:

Sensitivity analysis has been used for the cost of issuing the payment certificate. The cost of issuing the certificate can vary among contractors. The average cost of £25 came from the Improving payment practices in the construction industry (June 2007) consultation. We have therefore assumed a range of +/- 10%, i.e. a total of 20% sensitivity to address this in the table of costs and benefits at paragraph 35 on page 13.

- proportion of adjudication cost spent determining the amount of the dispute when it is not clear: The time can vary because of the complexity of the issues relating to time and amount of payment. In some instances it might be quite simple in others it might be more complicated. We have therefore assumed a range of +/- 10%
i.e. a total of 20% sensitivity to address this in the table of costs and benefits analysis at at paragraph 35 on page 13.

Direct impact on business (Equivalent Annual) £m:			In scope of OIOO?	Measure qualifies as
Costs: £1.5mn	**Benefits:** £31.5mn	**Net: £30**m	Yes	OUT

Evidence Base (for summary sheets) – Notes

References

	Reference material
1	*Improving Payment practices in the construction industry: Consultation on proposals to amend Part II of the Housing Grants Construction and Regeneration Act 1996 and Scheme for Construction Contracts (England and Wales) Regulations 1998 : March 2005*
2	*Improving Payment practices in the construction industry: Analysis of responses to the Consultation on proposals to amend Part II of the Housing Grants, Construction and Regeneration Act 1996 and the Scheme for Construction Contracts (England and Wales) Regulations 1998: January 2006*
3	*Improving Payment practices in the construction industry: 2nd Consultation on proposals to amend Part II of the Housing Grants, Construction and Regeneration Act 1996 and the Scheme for Construction Contracts (England and Wales) Regulations 1998 – June 2007*
4	*Improving Payment practices in the construction industry stakeholder event to discuss the second consultation on proposals to amend Part II of the Housing Grants, Construction and Regeneration Act 1996 and the Scheme for Construction Contracts (England and Wales) Regulations 1998 – July 2007*
5	*Improving Payment practices in the construction industry: Analysis of responses to the 2nd Consultation on proposals to amend Part II of the Housing Grants, Construction and Regeneration Act 1996 and the Scheme for Construction Contracts (England and Wales) Regulations 1998*
6	2008 Impact Assessment - Amendments to part 2 of the Housing Grants, Construction and Regeneration Act 1996 http://www.communities.gov.uk/documents/communities/pdf/1088220.pdf
7	The Local Democracy, Economic Development and Construction (LDEDC) Act 2009
8	Consultation on Amendments to the Scheme for Construction Contracts (England and Wales) Regulations 1998: March 2010

Annual profile of monetised costs and benefits* - (£m) Discounted prices *EcAD to revise*

	Y_0	Y_1	Y_2	Y_3	Y_4	Y_5	Y_6	Y_7	Y_8	Y_9
Transition costs	0.042	0	0	0	0	0	0	0	0	0
Annual recurring cost	0.7	0.7	0.7	0.7	0.6	0.6	0.6	0.6	0.6	0.5
Total annual costs	0.7	0.7	0.7	0.7	0.6	0.6	0.6	0.6	0.6	0.5
Transition benefits	0	0	0	0	0	0	0	0	0	0
Annual recurring benefits	31.6	30.5	29.5	28.5	27.5	26.6	25.7	24.8	24.0	23.2
Total annual benefits	31.6	30.5	29.5	28.5	27.5	26.6	25.7	24.8	24.0	23.2

* For non-monetised benefits please see summary pages and main evidence base section

Ongoing Costs and Benefits of the individual changes to the primary and secondary legislation[8]

Measures included in the 2009 Act	Details of Legislative change	Cost (£) (10 year NPV)	Benefit (£) (10 year NPV)	Calculation
1. Removing restriction on who can serve a payment notice	Change to Primary. No change required to secondary legislation.	0	£63mn (Range £50.6mn - £75.9mn)	**Costs:** No costs, as removes duplicative certificates. **Benefits:** 432,000[9] main contract payments per year of which 60%[10] involve duplicate

[8] All figures have been rounded to the next 0.5 million.

[9] Monthly Inquiry of Contracts and New Orders, BERR, 2005

[10] Improving Payment Practices in the Construction Industry: consultation on proposals to amend Part II of the Housing Grants Construction and Regeneration Act 1996 and Scheme for Construction Contracts (Scotland) Regulations 1998, Scottish Executive, 2005

				certification procedures. Average cost of issuing a certificate is £25[11] 2005 costs and benefits inflated to 2010, discounted over 10 years.[12] **A 20% sensitivity analysis has been used for the cost of issuing the payment certificate. The cost of issuing the certificate can vary among contractors. The average cost of £25 came from the Improving payment practices in the construction industry (June 2007) consultation. We have therefore assumed a range of +/- 10%, i.e. a total of 20% sensitivity to address this.**
2. Clarity of the content of payment and withholding notices	Change to Primary. Minor consequential changes to Secondary	£3.1mn (Range £2.5mn - £3.8mn)	£57mn (Range £43mn - £64.5mn)	This helps clarify the scope of the debt/payments owed/or not owed by both parties. **Costs:** 388,900[13] payments per year under contracts without certificates. Estimate of proportion of payments subject to abatement after deadline is one monthly payment every 2½ years[14] Average cost of issuing a withholding notice is £25[15]. **A 20% sensitivity analysis has been used for the cost of issuing the payment certificate. The cost of issuing the certificate can vary among contractors. The average cost of £25 came from the Improving payment practices in the construction industry (June 2007) consultation. We have therefore assumed a range of +/- 10%, i.e. a total of 20% sensitivity to address this** **Benefits:** Makes adjudication process simpler reducing costs: Total estimated adjudications (1,750) multiplied by proportion of adjudication cost spent determining the time and amount of the dispute when it is not clear (50%[16]) **multiplied** by the Average cost of the dispute (£20,000). NOTE: The total benefit from clarity is £170mn. This benefit is equally split between 2, 3 and 4, which all work to clarify the terms of the adjudication.

[11] Figure comes from responses to Improving payment practices in the construction industry June 2007

[12] Excel spreadsheet attached explaining the inflation rate rates used

[13] Monthly Inquiry of Contracts and New Orders, BERR, 2005

[14] Improving Payment Practices in the Construction Industry: consultation on proposals to amend Part II of the Housing Grants Construction and Regeneration Act 1996 and Scheme for Construction Contracts (Scotland) Regulations 1998, Scottish Executive, 2005

[15] Ibid

[16] Based on consultations with private sector adjudicators on May 2011

				2005 costs and benefits inflated to 2010 and discounted over 10 years. **NB:However, the annual average cost of adjudication of £20,000 and the number of annual adjudications of 1,750 both came from data in the June 2007 Improving payment practices in the construction industry consultation**. Proportion of adjudication cost spent determining the amount of the dispute when it is not clear. The time can vary because of the complexity of the issues relating to time and amount of payment. In some instances it might be quite simple in others more complicated. We have therefore assumed a range of +/- 10% i.e. a total of 20% sensitivity to address this.
3. A 'fall back' provision which allows the payee to submit a payment notice in default of the payer's notice after the payment due date.	Change to Primary. No change required to secondary legislation	0	£57mn (Range £45.5mn - £68.3mn)	**Costs:** None because payees would already have a payment notice as business as usual **Benefits:** Makes adjudication process simpler reducing costs: Total estimated adjudications (1750) multiplied by the proportion of adjudication cost spent determining the **time** and **amount** of the dispute when it is not clear (50%[17]) multiplied by the Average cost of the dispute (£20,000) NOTE: The total benefit from clarity is £170mn. This benefit is equally split between 2, 3 and 4, which all work to clarify the terms of the adjudication. 2005 costs and benefits inflated to 2010, discounted over 10 years. **NB:However, the annual average cost of adjudication of £20,000 and the number of annual adjudications of 1,750 both came from data in the June 2007 Improving payment practices in the construction industry consultation** Proportion of adjudication cost spent determining the amount of the dispute when it is not clear. The time can vary because of the complexity of the issues relating to time and amount of payment. In some instances it might be quite simple in others more complicated. We have therefore assumed a range of +/- 10% i.e. a total of 20% sensitivity to address this.

4. Prohibiting payment by reference to other contracts (Main	Change to Primary. No change required to secondary	£3.1mn (Range £2.5mn - £3.8mn)	£57mn (Range £45.5mn - £68.3mn)	**Costs:** DTI statistics from 2007 consultation, page 39. 13,000[18] payments under civil engineering payments include pay-when-certified

[17] Survey of private sector adjudicators – May 2011

[18] Monthly Inquiry of Contracts and New Orders, BERR, 2005

contractors have to issue their own certificate of work)	legislation			clauses. Removal means that a payment or withholding notice will now be required at average cost of £25. 13,000x£25 **A 20% sensitivity analysis has been used for the cost of issuing the payment certificate. The cost of issuing the certificate can vary among contractors. The average cost of £25 came from the Improving payment practices in the construction industry (June 2007) consultation. We have therefore assumed a range of +/- 10%, i.e. a total of 20% sensitivity to address this.** **Benefits:** Makes adjudication process simpler reducing costs: Total estimated adjudications (1750) multiplied by the proportion of adjudication cost spent determining the **time** and **amount** of the dispute when it is not clear (50%[19]) multiplied by the Average cost of the dispute (£20,000) NOTE: The total benefit from clarity is £170mn. This benefit is equally split between 2, 3 and 4, which all work to clarify the terms of the adjudication. 2005 costs and benefits inflated to 2010, discounted over 10 years. **NB:However, the annual average cost of adjudication of £20,000 and the number of annual adjudications of 1,750 both came from data in the June 2007 Improving payment practices in the construction industry consultation** Proportion of adjudication cost spent determining the amount of the dispute when it is not clear. The time can vary because of the complexity of the issues relating to time and amount of payment. In some instances it might be quite simple in others more complicated. We have therefore assumed a range of +/- 10% i.e. a total of 20% sensitivity to address this.
5. Change to Exclusion Order. This enacts the same provision as (4) but in PFI contracts	Change to Primary. Change required to secondary legislation	0	£0.211mn (Range £0.17mn - £0.25mn)	**Costs:** No costs. **Benefits:** 36[20] PFI contracts in 2011/12 multiplied by 12 monthly payments per year, multiplied by cost of certification between SPC and Main contractor = £50[21] (as part of the SOPC SPC contracts are more sophisticated hence assumed double that of average contract)

[19] Survey of private sector adjudicators May 2011

[20] HMT statistics on PFI, March 2011

[21] Improving Payment Practices in the Construction Industry: Second consultation on proposals to amend Part II of the Housing Grants Construction and Regeneration Act 1996 and Scheme for Construction Contracts (England and Wales) Regulations 1998, DTI, June 2007

				2005 costs and benefits inflated to 2010, discounted over 10 years. **A 20% sensitivity analysis has been used for the cost of issuing the payment certificate. The cost of issuing the certificate can vary among contractors. The average cost of £25 came from the Improving payment practices in the construction industry (June 2007) consultation. We have therefore assumed a range of +/- 10%, i.e. a total of 20% sensitivity to address this** .
6. A statutory framework for the costs of the adjudication (Inequitable share of adjudication costs discourages adjudication)	Change to Primary. Minor consequential changes to Secondary	0	Unquantified	**Costs:** None as no additional requirements. **Benefits:** These benefits are extremely difficult to quantify. The change gives parties the flexibility to seek less costly arrangements for the adjudication than those contained in the initial agreements entered in advance of a dispute. Such agreements can act as a disincentive to the use of adjudication. Illustrative example; If 10% of adjudications came to more flexible arrangements, saving 10% then total benefit = £396,000 (2010 prices). We do not have robust evidence for these assumptions, hence they not included.
7. Requirement for contracts to be 'in writing'	Change to Primary. Minor consequential changes to Secondary	0	£20mn (Range £16.4 -24.6mn)	The effect of the change means that the legislation can be applied to oral and partly oral contracts. Inclusion of oral clauses in contracts will reduce challenges to disputes. **Costs:** No cost to parties. Change to scope of contracts. **Benefits:** Total estimated adjudications (1750) multiplied by proportion of adjudication that are challenged (40%[22]) multiplied by expected saving of a challenge (15%[23]) multiplied by average cost of challenge (£20,000). 20% sensitivity considered on saving of a challenge 2005 costs and benefits inflated to 2010, discounted over 10 years. **NB:However, the annual average cost of adjudication of £20,000 and the number of annual adjudications of 1,750 both came from data in the June 2007 Improving payment practices in the construction industry consultation**

[22] Ibid
[23] Ibid

8. Suspension of performance for non-payment	Change to Primary. No change required to secondary legislation	0	£17mn (Range £13.6mn - £20.5mn)	**Costs:** None as no additional requirements. **Benefits:** Total estimated adjudications (1750) multiplied by proportion of adjudications saved by threat of walking out (5%[24]) multiplied by expected saving of a challenge (15%[25]) multiplied by average cost of challenge (£20,000). 2005 costs and benefits inflated to 2010, discounted over 10 years. **NB:However, the annual average cost of adjudication of £20,000 and the number of annual adjudications of 1,750 both came from data in the June 2007 Improving payment practices in the construction industry consultation** 20% sensitivity considered on proportion of adjudications saved by threat of walking out
Targeted total		**£6mn** (Range £5.1 - £7.6mn)	**£271mn** (Range £217.4 - £326.1mn)	***Net benefit £*265mn** (Range £212.4 -£318.5mn)

[24] 2008 analysis of the consultation responses to Improving Payment Practices in the Construction Industry: Second consultation on proposals to amend Part II of the Housing Grants Construction and Regeneration Act 1996 and Scheme for Construction Contracts (England and Wales) Regulations 1998, DTI, June 2007

[25] Improving Payment Practices in the Construction Industry: Second consultation on proposals to amend Part II of the Housing Grants, Construction and Regeneration Act 1996 and Scheme for Construction Contracts (England and Wales) Regulations 1998, DTI, June 2007