

On 20 March 2020, the Cabinet Office published Procurement Policy Note PPN 02/20 – Supplier Relief Due to COVID-19 (PPN 02/20), which makes recommendations to contracting authorities in relation to providing financial and other support to suppliers with a view to ensuring service continuity and the protection of infrastructure, supply chains and jobs both during and after the coronavirus disease 2019 (COVID-19) pandemic.

On 6 April, the Cabinet Office published an additional guidance note and frequently asked questions (Guidance) in relation to construction contracts, which provides direction to contracting authorities on how to implement the PPN 02/20 under existing works contracts.

In this article, we consider the effect of the Guidance and its application in practice for both contracting authorities and suppliers.

Purpose and Legal Status of the Guidance

The PPN 02/20 is perhaps best viewed as an emergency financial support scheme devised by central government to encourage contracting authorities to assist suppliers during the COVID-19 crisis. This is an alternative to the central government Coronavirus Job Retention Scheme (CJRS), but, unlike the CJRS, it is funded by contracting authorities rather than central government.

The PPN 02/20 and associated guidance is not legally binding; it is merely a reflection of expected practice on the part of contracting authorities. However, authorities would be well advised to ensure they have regard to the PPN 02/20 and Guidance in any relevant decision-making processes. A failure to do so may render any relevant decision taken susceptible to judicial review.

From a supplier's perspective, when making a request for assistance, it may be prudent to remind the contracting authority of its obligation to have regard to the Guidance.

We now consider some of the key points made in the Guidance.

1. Contracting Authorities Should Continue to Pay Their Suppliers Where They Have a Construction Project That Is Paused Due to COVID-19

Contracting authorities should continue to pay any suppliers deemed "at risk" due to COVID-19 until at least the end of June 2020. Contracting authorities are not expected to undertake a detailed assessment of suppliers' financial viability and the PPN 02/20 indicates that the "at risk" threshold is low. Authorities should apply this concept as broadly as possible to ensure service continuity.

This is to ensure these suppliers are supported during this period, particularly where works have ceased due to the impact of COVID-19, which may result in the collapse of the supplier, or where it would enable business continuity in the long term to pay suppliers in the short term.

Where applicable, contracting authorities can provide payment relief to suppliers in a number of ways, including payments against revised/extended milestones or timescales, interim payments, forward ordering and pre-payments.

Contracting authorities should:

- a. Assess and document the level of risk associated with advance or pre-payments, and seek legal advice if necessary
- b. Ensure invoices identify which elements relate to services suppliers are continuing to supply and which elements relate to the impact of COVID-19
- c. Not make payments to suppliers where there is no contractual volume commitment to supply, and suppliers who are underperforming or are subject to an existing improvement plan

Comment

It is clear that the provisions of the PPN 02/20 or Guidance do not alleviate the contracting authorities' obligations under the Public Contracts Regulations 2015 (PCR), other procurement legislation or public law obligations. Any changes effected to the contract must comply with the modification provisions under PCR, reg 72.

Cases should be assessed on a case-by-case basis in the context of the financial risk and the potential legal options and/or obligations of the contracting authority.

2. Contracting Authorities Should Amend Contract Terms to Reflect That a Supplier Has Been Given Relief

Legal advice should be sought in relation to how the form of relief agreed by the parties will affect the parties' obligations under the contract. The parties should work together to amend or vary the contract in place between them and limit any changes to the specific circumstances of the situation.

The Cabinet Office has published Model Terms, providing examples of how JCT and NEC contracts may be varied to provide relief to suppliers.

Comment

Legal advice is necessary, as contract variations must comply with the modification provisions under the PCR, reg.72 (or equivalent provisions under alternative procurement legislation). Careful consideration needs to be given as to whether one of the permitted grounds under PCR, reg.72 might be relied upon to justify the modification – for example, under the small changes provisions under PCR, regs 72(1)(f) and (5).

Where the modification involves conferring an advantage upon a supplier, state aid obligations will also need to be considered.

3. How Contracting Authorities Should Ensure That a Supplier Receiving Relief Under PPN 02/20 Does Not Also Receive Equivalent Relief From the CJRS or Other COVID-19 Support Schemes From the Government

The Guidance notes that suppliers cannot be paid under delivery of a contract and claim for some or all employees working on the contract under the CJRS. Any relief provided by contracting authorities should, therefore, be contingent on suppliers ensuring that the workforce working on the contract is not furloughed under the CJRS during the relief period.

Suppliers must agree to operate on an "open book" basis and provide any data (including from ledgers, cash flow forecasts, profit and loss accounts and balance sheets) to the contracting authority on request to show that payments made to the supplier have been used in the manner intended.

Workers that are paid under a public sector contract risk exclusion from future public contracts on professional misconduct grounds where they are found to have acted fraudulently, such as by claiming under the CJRS or other COVID-19 support schemes.

Comment

From a practical perspective, there may be some difficulty for contracting authorities to carry out their "open book" review of supplier accounts, particularly while the UK is in lockdown.

There may be delays and difficulties in delivering documents in hard copy to contracting authorities, and there may be data protection considerations relating to the electronic transfer of documents and commercially sensitive information.

Suppliers may also have difficulty providing the evidence required by contracting authorities, for example, in proving how many employees are furloughed. It was noted in the Frequently Asked Questions (FAQs) – Procurement Policy Note 02/21 that where staff work a proportion of their time on public sector contracts and a proportion on private sector contracts, public sector contracts will take precedence if the contract is delivering key or critical services, goods or works. Only employees not involved in delivering the contract in full may be furloughed under the CJRS. Whether or not an employee has been correctly furloughed during a relief period may be hard to verify.

Practical Tips

- a. Parties should agree how frequently to undertake a review of payments and how the review should be carried out
- b. Before any action is taken to furlough staff on public sector contracts, suppliers should discuss this with contracting authorities
- c. Where suppliers are found to have taken undue advantage and have not acted with transparency or integrity, contracting authorities should take action to recover payments made

4. Contracting Authorities Should Consider Early Release of Retentions

Retentions can be large amounts of money and may cause cash flow problems for suppliers. Although the premature release of retentions by a contracting authority may result in the authority taking a significant risk that ordinarily would be considered inappropriate and outside of its control, the Guidance recommends such a release should be considered on a case-by-case basis.

A contracting authority should assess the progress of works in order to make an informed decision. For example, where works are substantially complete and only a small proportion of work remains (which currently cannot be carried out due to COVID-19), a contracting authority may consider the release of a retention, withholding an appropriate amount to protect itself against the work that remains outstanding.

Alternatively, a contracting authority could consider releasing a percentage of a retention sum if it is satisfied that certain milestones have been met.

Suppliers in receipt of continuity and retention payments made under the PPN 02/20 will not be required to pay back this money, even where they have not been able to deliver services and goods required under the contract. However, delivery under the contract may be required at a later date. Where delivery will not be made in the future, contracting authorities may consider a future clawback of monies paid.

Comment

Retentions under construction contracts are collected as part of interim/milestone payments and are usually partially released on practical completion of a given project with the remaining amount (subject to deductions) paid out at the end of the defects liability period or on the issuance of the certificate of making good. The retention is, therefore, to cover the contracting authority against defects rectification. Again, the financial risk and legal implications of such action must be considered carefully by the contracting authority.

Any change to the contract will need to comply with PCR, reg.72 (or equivalent) and state aid rules.

5. Options for Relief in Construction Contracts

The Guidance provides a useful summary of the various forms of relief an authority may agree with a supplier in order to deal with business disruption caused by COVID-19. Each option for relief is listed together with points for consideration by the authority and practical notes on the implementation of each relief. We have summarised each of the options for supplier relief in the table below, and have provided some practical tips on how each option for relief would work in practice.

The Guidance also provides a Model Deed of Variation for the NEC3 Engineering and Construction Contract (April 2013 Edition), as well as for the JCT Design and Build Contract 2016 (Model Deeds). The Model Deeds provide standard clauses for the optional reliefs listed in the Guidance (discussed below). Note that these Model Deeds are provided as templates only and are subject to amendments where the standard forms have been amended. The user note suggests that contracting authorities should consider any interim proposals from contractors and agree the appropriate way forward on a case-by-case basis. Contracting authorities may also deviate from the standard clauses and seek legal advice to amend the Model Deeds, as most JCT and NEC forms of contract in use would have been heavily amended.

At a glance, a contracting authority will probably prefer relief options 1 and 3, rather than relief options 2 and 4, as paying a contractor quicker and more regularly will be less risky than certifying payments when work has not been carried out or making substantial advance payments. The Guidance is silent on whether payment options under the Model Deeds can be amended, but a contracting authority is advised to follow closely the standard payment option terms and only amend where existing standard forms have already been substantially amended.

Options for Relief in Construction Contracts

Option 1 – Accelerated Payment of Invoices

Consider accelerating the payment of invoices submitted by all “at risk” suppliers, and where any invoices are disputed, consider paying them now and reconciling them later.

Option 2 – Certification of Interim Valuations Where Work Has Not Been Undertaken, Based on Previous Valuations

- a. Certify interim valuations based on the average of the previous three months’ valuations (less supplier profit)
- b. Discount any disproportionately high values for project-specific reasons and discount these values in assessing the value of interim payments to be made
- c. Consider the value and the stage of works already provided
- d. Suppliers may not make contractual claims for costs incurred as a result of COVID-19 if this relief is given

Option 3 – Amendment to Existing Payment Mechanism to Make More Regular Payments or Re-order Existing Payment Schedule

- a. Consider whether current milestones can be re-ordered/modified
- b. Consider the ability to process more regular payments
- c. Consider current progress on-site

Option 4 – The Provision of Advance Payment(s) to the Supplier

- a. Consider whether there is value for money in securing continuity of supply of critical work in the medium and long term
- b. Consider the amount of advance payments being made to the same supplier
- c. Consider how and when advance payments will be repaid
- d. Ensure the purpose of any advance payments made is clear

Comment

All of the above options should be considered by the contracting authority on a case-by-case basis, with regard to the financial implications/risk and legal obligations of the contracting authority.

The contracting authority should document its decision-making process for the purpose of any potential future challenge under procurement legislation or by way of judicial review.

In relation to advance payments, many contracting authorities restrict such payments to a certain value and may need to relax their own financial procedure rules to accommodate any advance payments. Contracting authorities may also need to consider waiving the requirement of any advance payment bonds, as it will become very difficult and costly to have these in place under the current situation. Contracting authorities will need to consider each case separately, but will likely take on greater risks of suppliers’ insolvency and the inability to reclaim any sums paid.

In relation to advance payments related to materials purchased, or to be purchased and stored off-site, the contracting authority will need to ensure an appropriate vesting arrangement is in place and appropriate vesting certificates are issued. There will be practical difficulties and parties may consider relying on videoconferencing technologies to carry out inspections.

Where the contracting authority is to consider paying disputed invoices now and reconciling later, the contracting authority and its project managers should continue issuing payment and pay less notices, as required under the relevant construction contract. Contracting authorities may also consider entering into side agreements to allow them to reclaim the disputed sums (as a debt or through set-offs), once the supplier is no longer considered "at risk".

Any amendments and changes to the programme and adjustment to the payment profile will need to be recorded and provide reasons for the changes at the time.

6. Further Advice

The PPN 02/20 notes that contracting authorities must act now to ensure suppliers at risk are in a position to resume normal contract delivery once the outbreak is over. In addition to the various forms of relief outlined in the Guidance, other forms of contractual relief and remedies may be available to an authority, which are not the subject to the Guidance or PPN02/20.

The major issues facing the construction industry are not just related to the financial instability of the "at risk" contractors/suppliers, but also delays and associated costs on many existing projects as a result of COVID-19. Under the standard JCT Design and Build 2016 form, for example, unless instructed by the employer to suspend/postpone works, the contractor may be given an extension of time due to COVID-19, but any entitlement to loss and expense claims will be unlikely. For an extension of time claim, the contractor will also need to demonstrate the expected effects of the current disruption, as well as estimate the relevant delay on the programme. This becomes more difficult for the contractor to rely on relevant events mechanisms, as the current government policy is not to close construction sites, but to follow the Construction Leadership Council's published guidance and exercise social distancing rules and safe working practices.

In this regard, please see our recent publication [COVID-19 Impact on UK Construction Contracts](#).

Note: PPN 02/20 should be read in conjunction with all Cabinet Office guidance published on public procurement during the COVID-19 pandemic. This can be found [here](#). It is anticipated that this will be updated regularly by the Cabinet Office, so do check regularly whether any new guidance has been published.

In addition, on 2 April 2020, the Infrastructure and Projects Authority published [guidance](#) for contractors in PFI/PF2 contracts, which may be of relevance.

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