

To:

Chief Executives (local authorities England only)
Clerks to Police, Joint Fire and Transport Authorities

**Please circulate to those responsible for:
Procurement, architectural, building and construction
related services**

Retention of payments in building services and constuction contracts

28 April 2004

Guidance on Retentions

Dear Colleague

Please find attached guidance on the retention of payments in building services and construction contracts issued by the LGA/FPS (Federation of Property Societies) Procurement panel on behalf of the Local Government Task Force on Construction.

The guidance is based on the principle of developing long term strategic relationships contained in the "Rethinking Construction" report. It recommends that the retention of payments within building contracts as a form of insurance to guarantee satisfactory completion of projects, should be phased out as part of longer term partnering arrangements.

This should be achieved through more effective risk based assessments of contracts and contractors and the development of credible relationships which establish trust between the parties that guarantee satisfactory completion of projects.

For further information please contact:

Peter Bishop
Director
Local Government Task Force
Constructing Excellence
25 Buckingham Palace Road
London SW1W 0PP

telephone 020 7592 1100
e-mail - peter.bishop@constructingexcellence.org.uk

Yours sincerely

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Local Government House, Smith Square, London SW1P 3HZ
DX 119450 Westminster 2 Email info@lga.gov.uk
Tel 020 7664 3000 Fax 020 7664 3030
Information centre 020 7664 3131 www.lga.gov.uk

Retentions

The LGA/FPS Procurement panel has been approached by the Local Government Task Force to give a lead to local authorities on the issue of the use of retentions in building contracts.

It has become common practice for standard forms of contract in the construction industry to include provisions for a small percentage of payments to contractors to be retained as a form of financial security for the employer. If a contractor fails to comply with the contract, [for example in respect of the quality of the completed building (defects), or by not meeting the completion date], then the retention held by the employer provides a fund to which the employer has immediate access in order to meet the cost of these matters.

This has been a subject that has caused much debate over the years and with the continued development of “Rethinking Construction” principles clearly needs re-consideration.

Retentions are not compatible with long term partnering arrangements as recommended by Rethinking Construction. They are an added cost to the client and add no value to the project. The key is for the team to concentrate on providing a good set of working relationships and this should include the involvement of the whole supply chain.

The onus is on the team to demonstrate that they can perform without external levers. They must show they can and will do it right first time, without threat. Once this credibility is established clients will have sufficient guarantees about a satisfactory, defect free, completion of the project and thus the desire for retentions to be applied will be removed.

At present, it would be difficult to justify their removal in all projects without some alternative guarantees being in place to the satisfaction of the client. This could be achieved by the development of an insurance backed warranty scheme, provided by the contractor and paid for by the client through the contract.

However if applied properly under the terms of the contract, a retention clause is transparent to all, the contractor is paid at the end of the defects period and the industry is not paying insurance premiums to third parties to achieve the level of comfort which ensures client’s interests are protected.

A better solution could be for a risk assessment which would be carried out on a contract by contract or contractor by contractor basis to determine whether the risk involved is sufficient to require the retention or bond.

In conclusion it is clear that retentions are not within the spirit of Rethinking Construction and need to be phased out. However partnering teams, which include the client and the whole supply chain, need to demonstrate that they are able to deliver and complete projects that are right first time.

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