



Practice of Cash Retention Under Construction Contracts: Public Consultation Findings



ECONOMY AND LABOUR MARKET

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Foreword

It has been recognised that the circumstances arising from the COVID 19 pandemic has hastened the change in some elements of the way we work. It has stimulated unprecedented levels of collaboration between government and industry which we now seek to build on.

The construction industry touches every part of Scotland's economy and is vital to our future prosperity. With a turnover of around £19 billion per annum it provides £7.8 billion Gross Value Added to the Scottish economy and employs 143,000 people in over 50,000 enterprises.

Improvements to the sector's productivity and profitability remain key to continuing to address Scotland's construction needs and to allow the sector to invest in its people, innovation, skills and the new technology required to take advantage of the emerging opportunities in areas such as retrofit, offsite construction and in the major infrastructure opportunities emerging within the wider UK and internationally.

However, the industry faces a number of challenges, including ensuring prompt and fair payment to firms within the supply chain. Cash retention is one example of a payment practice vulnerable to both insolvency and abuse.

Unjustified late and non-payment of retentions are regularly raised by parts of the industry as being a barrier to growth within the construction sector. These practices can cause problems, particularly for small business owners, who rely on a steady cash flow. We are committed to working with the sector to improve payment practices and that is why we published a consultation seeking views on the practice of cash retention under construction contracts. I am grateful to all those who took time to respond to the consultation and who participated in wider discussions.

Responses were received from a range of organisations and these clearly illustrate the breadth of views within the sector on the practice of retention, and the possible policy solutions to addressing the issues associated with their use. These range from maintaining the current approach; to protecting retentions in a deposit scheme; and to introducing a ban on cash retentions. This document contains a summary of the responses during the open consultation period. It provides a useful base to consider the impact of policy options and highlights that further work and evaluation is required. We will continue to work with industry to build consensus for a policy option that addresses the problem of unjustified and late payment of cash retentions. We note that the UK Government has taken time to consider its consultation on cash retention and this supports the evidence that this will not be easy to resolve.

Executive Summary

Respondents

1. The consultation attracted thirty-three respondents, the majority of which were organisations: twenty-five organisations, eight individuals.
2. Most of the respondent's role in the construction sector were as 'sub-contractors' (n14), with 'client' and 'Tier 1 contractor / sub-contractor' having seven and six respondents, respectively. Only one respondent was a 'Tier 1 contractor.'
3. The majority of respondents were 'businesses that were subject to retentions' (n13), and 'business that uses / subject to retentions' (n8) ('Client who used retentions' and 'not exposed to retentions' had six respondents each.)

Section A: Supporting Documentation and the Pye Tait Report - Retentions in the Scottish Construction Industry

4. In line with the Pye Tait report conclusion, respondents were almost in **unanimous agreement** (85% 'fully agreeing', 9% 'partially agreeing') that the "*financial consequences for contractors and subcontractors in the event of a large organisation going into liquidation can be significant*".
5. When asked whether they thought '*some form of assurance is needed in construction contracts*', the response was **almost unanimous**: 94% agreed with this and only 6% disagreed.
6. However, when asked how '*effective do you feel the current system of retention is*' there was a **mixed response** by respondents: 36% thought it was 'not effective at all' and only 9% thought it was 'very effective' (39% thought it was 'partially effective' and 15% thought it was 'slightly ineffective; 9% thought it was 'neither effective nor ineffective').
7. A majority of respondents thought that **retentions were not** '*the best form of assurance within construction contracts*' (22 respondents said 'no', 11 said 'yes'), although there was **no clear consensus on 'what other form of assurances'** would be preferred instead.

Section B: Non-Payment of the Retention

8. A clear majority thought non-payment was a 'very significant' or 'fairly significant' issue, 58% and 24% respectively.
9. There were **many reasons given for on-payment of retentions**, either by those being subject to retentions or those holding retentions, including:

insolvency, contractors not returning to fix defects, poor quality work, legal fees being too costly to pursue, and sub-contractors using the money as ‘free banking.’

10. Of the **total value of retentions due to be released**, to and by respondents, in the past 12 months, most were under £200k with a small number above this figure. Similarly, where retention money was due to respondents, most were under £100k.
11. Of the respondents that had experienced **unpaid retentions** (n10), on average they believed that approximately **60% of these were unjustified**.
12. When asked whether they **challenged the non-payment of retention** *that occurred due to the payer citing obligations under another construction contract not being met* there was fairly even split between respondents, with ten saying they did and eight did not.

Section C: Late Payment of the Retention

13. Late payment of retentions, like non-payment, **was also an issue for the majority of respondents** (56% saying it was a ‘very significant’ and 21% ‘fairly significant’ issue).
14. A small number of respondents provided further information on reasons for late payment: they did not meet the provisions of the contract; payer cited that obligations under another construction contract had not been met; cash flow problems with holding company and; poor quality work.
15. Of the retentions paid late, the majority (n8) estimated that between **75 – 100% of these had been unjustified**, with only two believing this to be 51 – 75% and three believing it between 26 – 50%.
16. For the **amount of time** they believed to have been unjustified, three waited between 1 – 3 months, six waited 3 – 6 months, three waited 6 – 12 months and two waited over a year.
17. The total median estimated cost of pursuing late (and ultimately unpaid) was £2,500 per respondent.

Section D: Existing Alternative Mechanisms to Retentions

18. When asked what options they thought should be ‘*applicable for wider use across the whole sector*’,¹ most respondents (42%) agreed that **retentions**

¹ Question 1c: Which of these do you think would be applicable for wider use across the whole sector? Section D - 1c

should be held in trust, with 27% agreeing with **retention bonds** and 24% saying **escrow stakeholder accounts**.

19. Respondents were almost split when asked whether they thought it was 'important for Scotland to use the same mechanism of assurance in constructions contracts as the rest of the UK' with eleven disagreeing or partially disagreeing and twelve fully agreeing or partially agreeing. This split in support was also the case regardless of whether respondents were from organisations that worked exclusively in Scotland or those that worked across the UK.
20. The **majority of respondents fully agreed or partially agreed** (42% and 24% respectively) that a 'retention deposit scheme' and/or holding retentions in trust could eliminate some of the critical issues associated with retentions (notably the risk of delayed or non-payment of retention monies) and provide surety against defects'. Only 9% disagreed completely, and 6% partially disagreed.

Section E: Retention Deposit Scheme

21. Respondents were **mostly in favour of the use of a retention deposit scheme** that '*could be used for all contracts or only for contracts over a certain value*', with 48% of respondents in favour for 'all contracts' and 30% for 'contracts over a certain value'. Only 15% were 'against its use'.
22. A **slight majority of respondents (n17) disagreed** that 'it is important to place a threshold on the application of any measure requiring retentions to be held in trust or ring-fenced in another way',² compared to those who agreed (n13). Of those respondents who did agree, nine thought that less than £100k should be the minimum value of the total retained money (the retention) should it commence, three thought between £100k and £500k, and only one thought between £500K and £1m.
23. When asked to what extent they thought a retention deposit scheme may allow for a) *a fairer approach to retentions*³ b) *a more neutral approach*⁴ and c) *a more protected approach*,⁵ **clear majority either fully agree or partially agreed with all three statements**.

² Question 1a: Is it important to place a threshold on the application of any measure requiring retentions to be held in trust or ring-fenced in another way and, if so, at what minimum value of the total retained money (the retention) should it commence? Section E - 1a

³ Question 2: To what extent do you think a retention deposit scheme may allow for a fairer approach to retentions? Section E - 2

⁴ Question 2a: To what extent do you believe a retention deposit scheme allows for a more neutral approach to retentions? Section E - 2a

⁵ Question 2b: To what extent do you think a retention deposit scheme may allow for a more protected approach to retentions? Section E - 2b

1. Introduction

There is evidence that some payment practices prevalent in the construction industry are a barrier to investment, productivity and growth. Cash retention, where the process is misused or abused, can be one such practice.

As a sum of money withheld from the contractually-agreed amount due on a construction project, the purpose of a retention is to mitigate risk should some of the work not be completed satisfactorily, or any resulting defects not be rectified by the contractor.

The part of the contract sum which is held back is intended to provide a means of incentivising contractors and subcontractors to return to correct any defects during a specified period of time or to provide towards a means of funding the procurement of another contractor to do so if necessary, as outlined in contract terms and conditions.

In most cases a retention is imposed by the client employing the main (also known as Tier 1) contractor and this is mirrored in all subsidiary contracts throughout the supply chain.

Following concerns expressed by parts of the industry, the Scottish Government agreed to undertake a review of retention payments. To support the review, the Scottish Government commissioned independent research from Pye Tait and that research is published alongside this consultation. It illustrates the challenges with retentions - in particular understanding the extent to which this practice has a negative impact and what solutions would be effective and proportionate in addressing this.

The UK Government undertook a similar review of retention payments in the construction industry, which concluded in January 2018, and was published in January 2020.⁶

⁶ Available at:

https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/868630/retention-payments-in-the-construction-industry-summary-of-responses.pdf

2. Conducting the consultation exercise

On the 4 December 2019, the Scottish Government published a consultation paper which sought information on the practice of cash retention under construction contracts and gathered views on the supporting documentation. The consultation was open for 23 weeks and closed on the 13 May 2020.

The purpose of this consultation was to seek information on the practice of cash retention in public and private sector construction contracts in Scotland and to gather views on the findings of the supporting documentation.

The Pye Tait report on Retentions in the Scottish Construction Industry⁷ was published in conjunction with the opening of the consultation process. It illustrated the benefits and challenges with retentions, in particular understanding the extent to which this practice has positive but also a negative impacts and what solutions would be effective and proportionate in addressing these.

A number of key issues were identified by the research:

- Evidence suggests that a significant proportion of companies say they deliberately avoid business in which retentions are involved.
- It suggests that the current system operates to the advantage of clients and Tier 1 contractors but to the disadvantage of medium and smaller companies, particularly where a contractor insolvency might occur.
- Qualitative evidence suggests that late and non-payment of retention monies is a significant issue for some contractors; and
- There is a need to investigate a fairer, more neutral and more protected approach to assurance in construction contracts.

Unjustified late and non-payment of a retention or any other amount owed is unacceptable. This consultation gathered views and information on:

- the effectiveness of existing prompt and fair payment measures for retentions;
- views on the Pye Tait independent research on retentions in the construction industry;
- late and non-payment of retentions;
- the effectiveness of existing alternative mechanisms to retentions; and
- the benefit of holding retentions in a retention deposit scheme or trust account.

⁷ Available at: https://consult.gov.scot/industrial-sectors/retention-payments-in-construction/supporting_documents/Retentions%20in%20the%20Scottish%20Construction%20Industry%20Pye%20Tait%20report.pdf

3. Summary of respondents

A total of thirty-three responses to the consultation document were received via Citizen Space – the online portal for government consultations – or the electronic response form (respondents who agreed to having their names published are listed in Annex A). The nature of the respondents is set out below (organisation by SIC codes are listed in Annex B):

Respondent Type:

- The majority of respondents were organisation: twenty-five organisations compared to eight individuals.
- Of the organisations that responded, half worked on construction projects across the UK, the other half worked exclusively in Scotland.
- The majority (79%) of all respondents had their headquarters in Scotland (twenty-six respondents out of thirty).

Nature of Business in Construction Sector:

Most of the respondent's role in the construction sector were as 'sub-contractors' (n14), with 'client' and 'Tier 1 contractor / sub-contractor' having seven and six respondents, respectively. Only one respondent was a 'Tier 1 contractor' (Figure 1).

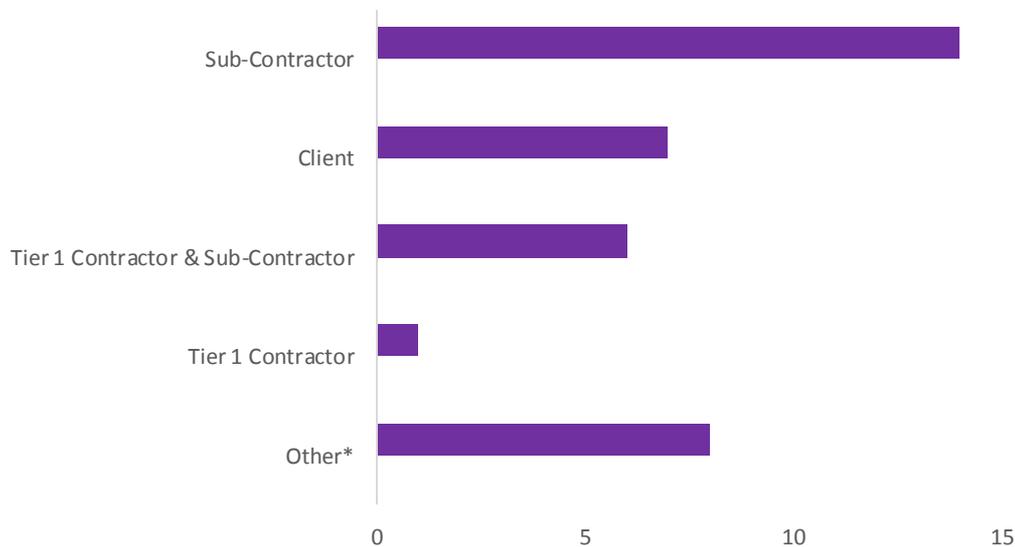


Figure 1: nature of business

* Trade associations (2); Contractor consultation body to all Tiers (2); Quantity surveying consultancy(1); Dispute resolution consultant (1); project manager (1).

Direct Employees (Excluding Sub-Contractors)

As shown in Figure 2, the number of respondent's direct employees were mostly spread across 'micro', 'small', 'medium' and 'large' categories. There were only three sole trader respondents.

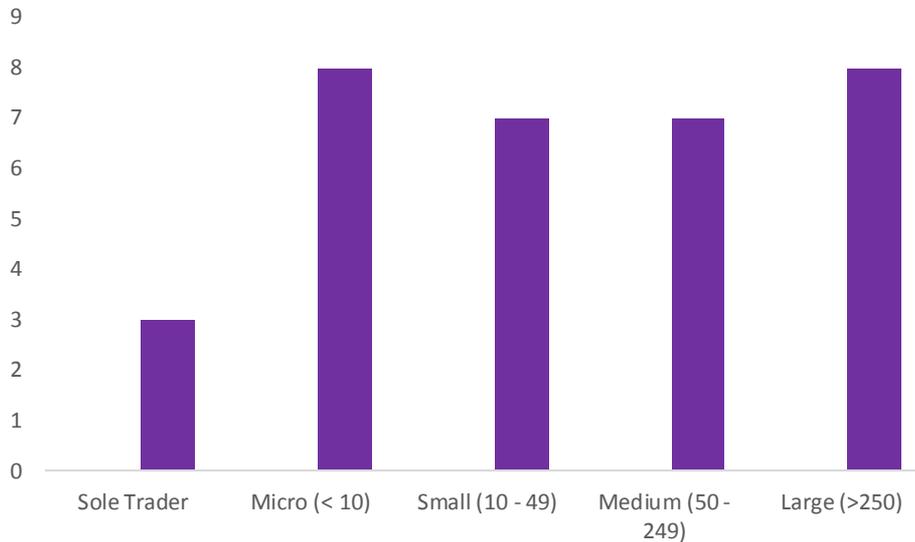


Figure 2: number of direct employees

Contracts Won and Experience of Using Retentions

The majority of respondents were 'businesses that were subject to retentions' (*n*13), and 'business that uses / subject to retentions' (*n*8) ('Client who used retentions' and 'not exposed to retentions' had six respondents each.)

Fifteen respondents had **contracts secured**⁸ in the twelve months preceding the survey, ranging from 6 to 400 contracts. The average number per respondent was 73, but this number is skewed by a few respondents; a more representative number is the **median which was 26**. Three respondents had also secured no contracts during this timeframe.

Eleven respondents had **issued contracts**, with the average being 133 issued. It is worth noting though that this figure was also skewed by a few respondents and the more telling figure is the **median which was 25**.

⁸ Question 1: Can you provide an estimate of the total number of construction contracts that your business both secured and issued over the last 12 months? Section B - 1 Total number of contracts secured There were 18 responses to this part of the question. Section B - 1 Total number of contracts issued

The combined total of all these contracts was £467,550,000, the average was £49,215,789, but the **median was £14,000,000**.⁹

Of the total construction contracts over the past twelve months, 16 respondents had won contracts that subjected them to a retention (a total of 895 contracts); 7 had issued contracts that had imposed a retention on others (a total of 672 contracts).¹⁰

Of the current contracts with retentions (where you are holding a retention or are subject to a retention) 19 were public sector and 17 were private sector.¹¹

⁹ Question 1a: What was their approximate combined value? Section B - 1b

¹⁰ Question 1b: Of the total construction contracts over the past twelve months, how many had retentions written into the contract (i.e. a client or main contractor is holding a retention against you or where you are holding a retention over others?)

¹¹ Question 1c: Approximately how many of your current contracts with retentions (where you are holding a retention or are subject to a retention) are for work undertaken in a) the public sector and b) the private sector (if zero enter 0) Section B - 1d public sector There were 19 responses to this part of the question. Section B - 1d private sector

4. Summary of responses

Section A: Supporting Documentation and the Pye Tait Report - Retentions in the Scottish Construction Industry

In line with the Pye Tait conclusion (hereby referred to as 'the report'), respondents were almost in **unanimous agreement** (85% 'fully agreeing', 9% 'partially agreeing') that the "*financial consequences for contractors and subcontractors in the event of a large organisation going into liquidation can be significant*". Only 6% of respondents 'partially disagreed'.¹²

Respondents were also **largely in agreement** (67% 'fully agreeing' and 3% 'partially agreeing') with the report's conclusion that "*retention money held in a main bank account can be used by the holder to fund expenditure on labour, plant and materials on other projects and/or as part of working capital*".¹³ However, 15% 'disagreed' and 9% 'partially disagreed' with this conclusion.

Figure 3 shows that while there were more respondents who agreed than disagreed, there was **more of a spread of answers** from respondents regarding the conclusion that "*some companies deliberately avoid business in which retentions are involved*".¹⁴

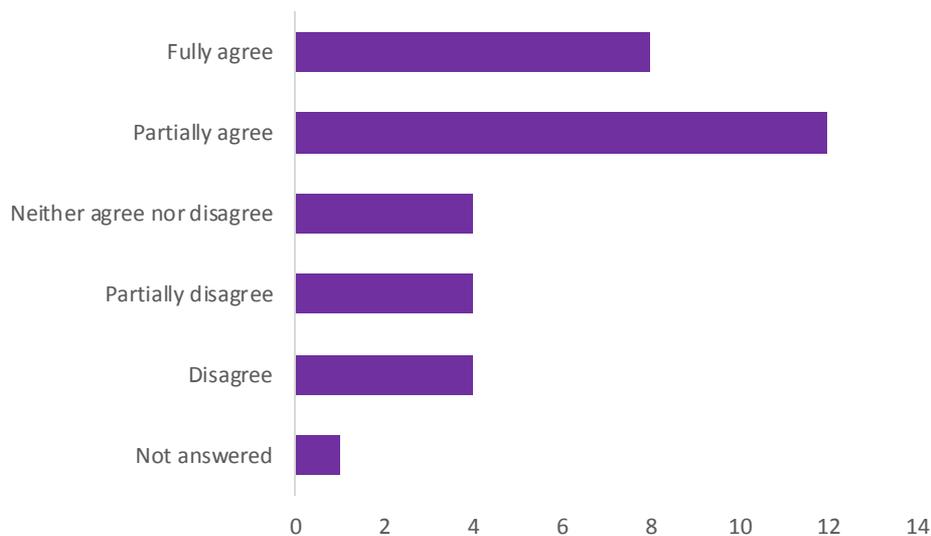


Figure 3: some companies deliberately avoid business in which retentions are involved

¹² Question 1: Do you agree with the Pye Tait conclusion/area for potential further investigation that "the financial consequences for contractors and subcontractors in the event of a large organisations going into liquidation can be significant"? Section A - 1

¹³ Question 1a: Do you agree with the Pye Tait conclusion/area for potential further investigation that "retention money held in a main bank account can be used by the holder to fund expenditure on labour, plant and materials on other projects and/or as part of working capital"? Section A - 1a

¹⁴ Question 1b: Do you agree with the Pye Tait conclusion/area for potential further investigation that "some companies deliberately avoid business in which retentions are involved"? Section A - 1b

Most respondents agreed with the report’s finding that an area for potential further investigation was that *‘alternatives to common retention practices are available but used infrequently’*:¹⁵ 67% ‘fully agreed’ and 21% ‘partially agreed’ (3% ‘disagreed’ and 6% partially disagreed’)

As Figure 4 shows, **respondents were split** on the report’s conclusion that *“the retention system in Scotland works reasonably well when all parties adhere to the letter and spirit of the agreement”*,¹⁶ with 30% ‘fully agreeing’ and ‘disagreeing’:

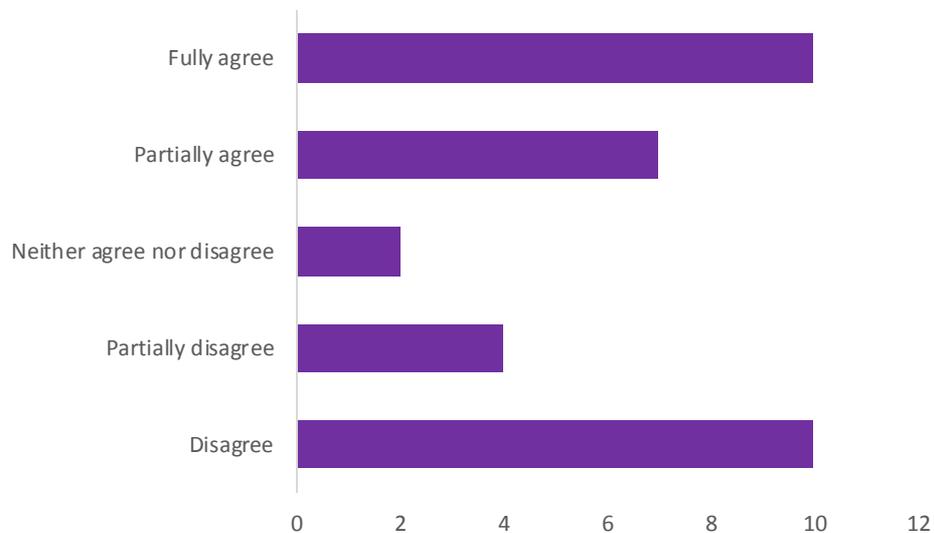


Figure 4: retention system in Scotland works reasonably well when all parties adhere to the letter and spirit of the agreement

Respondents selected what they believed to be the main intended purpose of the retentions scheme. **Most thought** that the scheme was a way to *‘encourage sub-contractors to return to fix any defects’* and as a means of funding *‘works required to fix defects in the event that the sub-contractor did not return’* (table 1 overleaf). (Ten respondents also thought that retentions worked as a *‘warranty against poor quality work’*.)¹⁷

¹⁵ Question 1c: Do you agree with the Pye Tait conclusion/area for potential further investigation that "alternatives to common retention practices are available but used infrequently"? Section A - 1c

¹⁶ Question 1d: Do you agree with the Pye Tait conclusion/area for potential further investigation that "the retention system in Scotland works reasonably well when all parties adhere to the letter and spirit of the agreement"? Section A - 1d

¹⁷ Question 2: Which of the following do you believe to be the intended purpose of retentions as part of construction contracts? Section A - 2

Table 1: intended purpose of retentions as part of construction

	Total	%
To encourage sub-contractors to return to fix any defects	23	70%
To fund works required to fix defects in the event that the sub-contractor did not return	23	70%
To act as a warranty against poor quality work	10	30%
Other*	5	15%

* Reputable firms will always return to fix defects and do not require retentions as an "incentive" (1); To protect against sub-contractor insolvency(1); To protect main contractor against insolvency(1); It is a pot of money that main contractors see as their potential margin (1); A way for major contractors to keep capital as long as possible. Unless a sub-contractor really pushes for it to be paid it is never paid or paid in full (1).

When asked whether they thought ‘some form of assurance is needed in construction contracts’¹⁸, the response was **almost unanimous**: 94% agreed with this and only 6% disagreed.

However, when asked how ‘effective do you feel the current system of retention is’¹⁹ there was a **mixed response** by respondents: 36% thought it was ‘not effective at all’ and only 9% thought it was ‘very effective’ (39% thought it was ‘partially effective’ and 15% thought it was ‘slightly ineffective; 9% thought it was ‘neither effective nor ineffective’).

A majority of respondents thought that **retentions were not** ‘the best form of assurance within construction contracts’²⁰ (figure 5) (twenty-two respondents said ‘no’, eleven said ‘yes’):

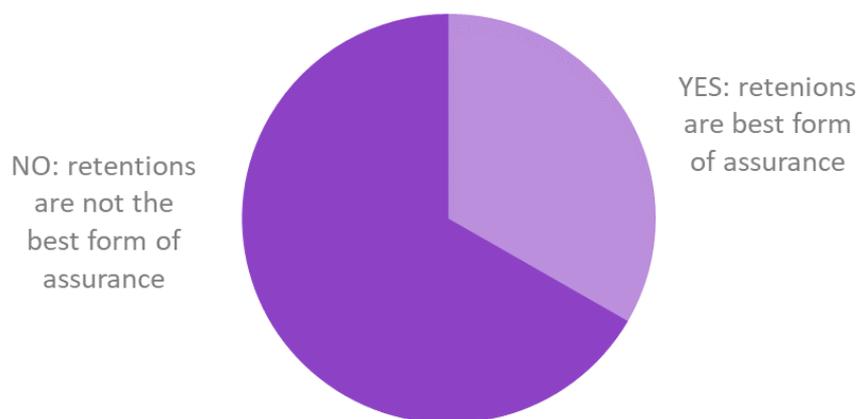


Figure 5: Do you agree that retentions are the best form of assurance in construction contracts

¹⁸ Question 3: Do you agree that some form of assurance is needed in construction contracts? Section A - 3

¹⁹ Question 3a: How effective do you feel the current system of retention is? Section A - 3a

²⁰ Question 4: Do you agree that retentions are the best form of assurance within construction contracts? Section A - 4

For the respondents that answered ‘No’ (n22) to the above question, these respondents gave the following answers when asked ‘*what other form of assurance they would prefer*’²¹ (table 2) (it should be note that there was far from a consensus and nine of the possible twenty-two did not provide an answer):

Table 2: Preferred form of assurance for construction projects

Retentions bonds	5	15%
Performance bonds	1	3%
Escrow stakeholder accounts	4	12%
Parent Company guarantees	4	12%
Other*	10	30%
Not answered	9	27%

* Please see Annex C for full list of written responses

When asked whether they agreed or not with the recommendation made within the report ‘*That action should be taken to create a fairer, more neutral and more protected approach to the practice of retentions*’²² the **majority were in agreement**: 76% said ‘yes’ (n25), with 24% saying ‘no’ (n8) (see Annex D for additional supporting reasons given in explaining these selections).

Of those that answered ‘yes’ (n25) to the above question, when asked ‘*what would you suggest for the practice of retentions*’²³, **nine suggested “ban the practice of retentions”** and **five respondents said “no action – I’m happy with current system of retention”** (it should be noted that the majority (n19) did not answer).

For the question of whether respondents ‘*actively avoid bidding for contracts subject to retention*’²⁴, **only a minority** of 9% outright reject this statement (table 3 overleaf):

²¹ Question 4a: If you answered no to Question 4 (i.e you do not think retentions are the best form of assurance within construction contracts) what would be your preferred form of assurance for construction projects? Section A - 4a

²² Question 5: The recommendation made within the Pye Tait research is - "That action should be taken to create a fairer, more neutral and more protected approach to the practice of retentions" Do you agree with this recommendation? Section A - 5

²³ Question 5a: If you answered yes to question 5 - how do you feel this could be achieved? Section A - 5a

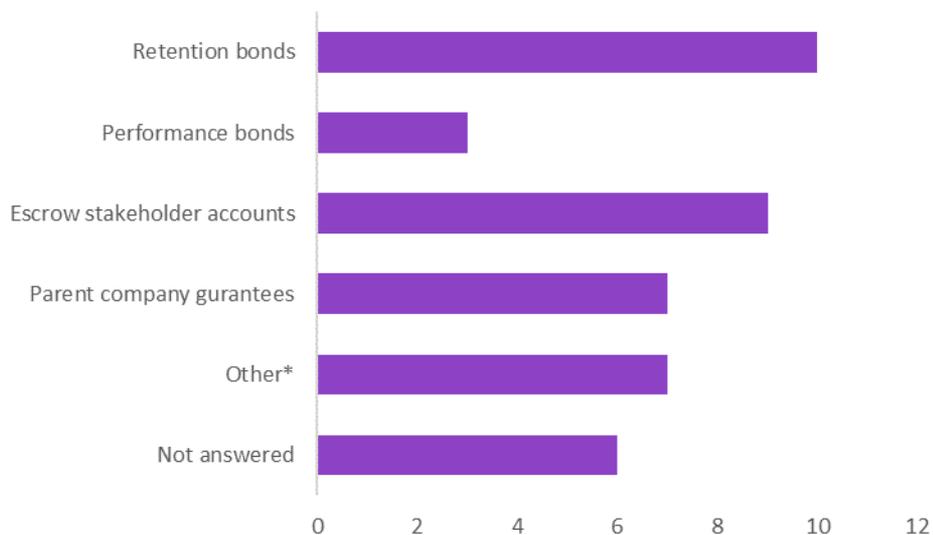
²⁴ Question 6: Do you actively avoid bidding for contracts subject to retention? Section A - 6

Table 3: Do you actively avoid contracts subject to retention

Yes	3	9%
No	9	27%
It depends on the value / type of contract	10	30%
Not applicable	7	21%
Not answered	4	12%

Related to the above question, respondents were also asked if they would ‘bid for contracts if an alternative to the current practice of retention was established or as Pye Tait recommend a “fairer, more neutral and protected approach to the practice of retentions”²⁵. **Most respondents said ‘yes’ to this (n13)**, and only four saying it ‘would depend on the type of contract’ and only two saying ‘no’ (eight were clients and not applicable, six did not answer).

Respondents were asked ‘If you were unable to use retentions what method of assurance would you use’.²⁶ As figure 6 highlights, **no one option was significantly preferred:**



* Retention Deposit Trust Scheme (if affordable); retention bonds, performance bonds; PCG; and guarantee bonds. Other answers also included: “would seek other non-retention using contractor”; “relevant only for Tier 1”; “a mixed approach would work best”.

Figure 6: Methods of assurance favoured other than retentions

²⁵ Question 6a: If so, would you bid for contracts if an alternative to the current practice of retention was established or as Pye Tait recommend a “fairer, more neutral and protected approach to the practice of retentions”? Section A - 6a

²⁶ Question 7: If you were unable to use retentions what method of assurance would you use? Section A - 7

For the last question in this section respondents were asked if their cashflow would be affected if they *'were unable to use retentions'*²⁷. Of those respondents who answered, **five said 'Yes, I hold retentions in a main bank account', four said 'No, I hold retentions in a separate account, and eleven 'did not hold retentions from others'**.

When asked the follow up question of what *'impact would not being able to use retentions for cashflow have on your business'*²⁸, **most did not believe there would be much impact**: five said it would be 'neither significant nor insignificant' and one said it would be 'fairly insignificant' and one said 'none', whereas only two said it would be 'very significant' and three said it would be 'slightly significant'.

Section B: Non-Payment of the Retention

When asked how significant an issue *'non-payment of retentions is in the construction sector'*²⁹, the clear majority thought it was 'very significant' or 'fairly significant', 58% and 24% respectively.

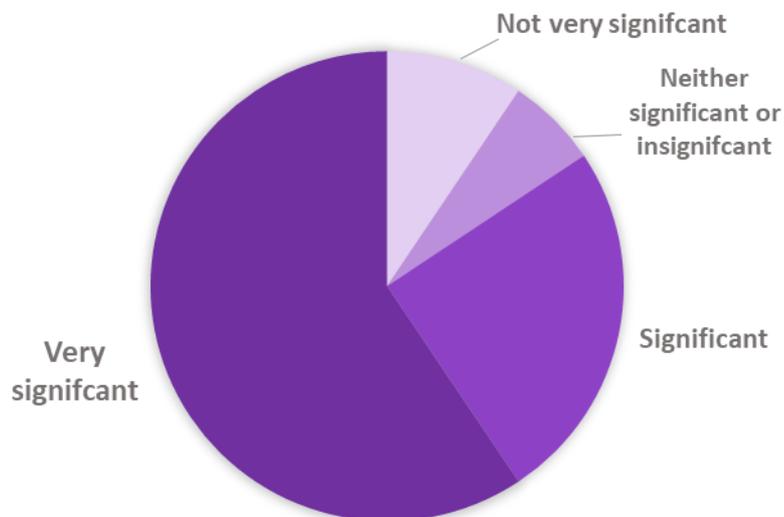


Figure 7: Significance of non-payment of retentions in the construction sector

²⁷ Question 7a: If you were unable to use retentions would your cashflow be affected? Section A - 7a

²⁸ Question 7b: If you answered yes above, what impact would not being able to use retentions for cashflow have on your business? Section A - 7b

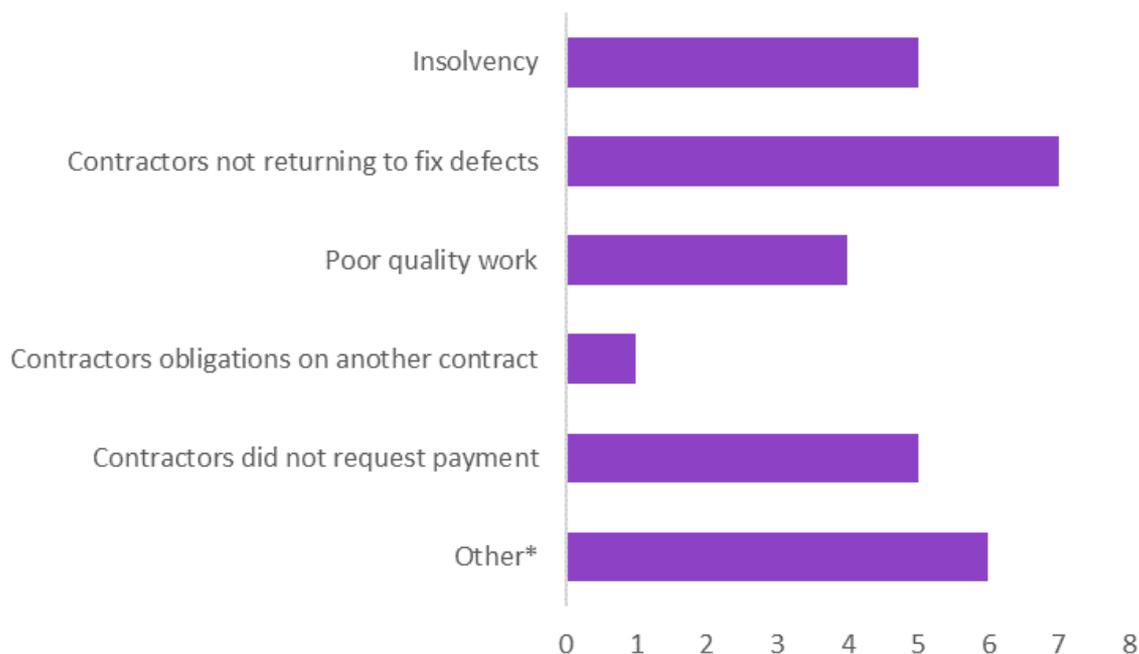
²⁹ Question 2: How significant an issue do you think non-payment of retentions is in the construction sector? Section B - 2

When asked what the ‘*main reasons for non-payment of retentions*’³⁰ were, a wide range of answers were provided. Of the options given, seventeen said ‘insolvency’, fourteen ‘contractors not returning to finish work’, and only four said ‘poor quality of work’.

Several others referenced the behaviours of the main contractor, including refusing to pay or avoiding paying because:

- know that legal action would be relatively too costly to pursue.
- use sub-contractors money as free banking.
- are unable to resolve defects satisfactorily.
- use release of retention as leverage to diminish a Final Account Value or to simply negotiate a further discount and
- hope that sub-contractor will just forget about it.

For those holding retentions in the past 12 months³¹ there was a mixture of answers to the question of what the **reasons for withhold payment of retentions**:



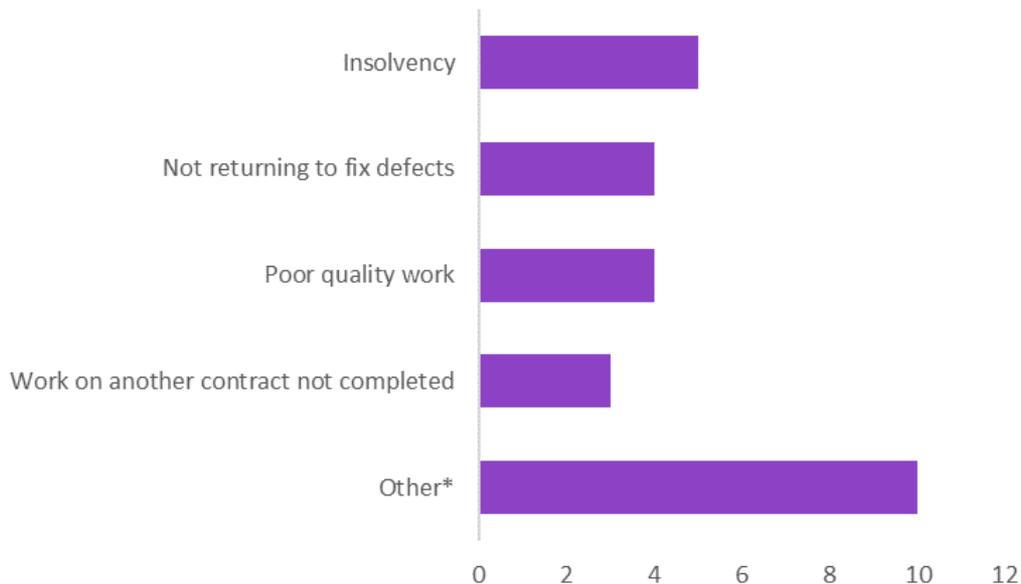
* Other included: perceived dishonest main contractor; stalling or refusing tactics related to cash flow with main contractor; outlawed practice of “pay when paid” invoked by main contractor; subcontractors hadn’t completed their defects so the principal contractor hadn’t received payment; final accounts not being paid.

Figure 8: Reasons for withholding payment for those holding retentions within the last 12 months

³⁰ Question 2a: What, in your experience, are the main reasons for non-payment of retentions? Section B - 2a

³¹ Question 3: If you have been holding retentions within the last 12 months and withheld payment. What were the reasons for doing so? Section B - 3

Similarly, a mixture of answers were also given when respondents were asked what the reasons were for non-payment if they have been **subject to a retention** within the last twelve months and this was not repaid³² (Figure 9):



* Other included: dishonest main contractor using stalling tactics, making false claims of defects, final accounts not being paid, and needing multiple reminders; main contractor insufficient funds due to awaiting other subcontractors addressing defects.

Figure 9: Reasons given for payment of retentions not being received within the last 12 months

Of 'the total value of retentions due to be released'³³ to and by respondents in the past 12 months, most were under £200k with a small number above this figure. Similarly, where 'retention money was due'³⁴ to respondents, most were under £100k with a lower amount at the higher end of above £200 (Table 4, overleaf).

³² Question 3a: If you have been subject to a retention within the last twelve months and this was not repaid - what were the reasons for non-payment? Section B - 3a

³³ Question 4: Approximately, what was the total value of retentions due to be released to you or by you over the last twelve months? Section B - 4

³⁴ Question 5: If retention money was due to you in the last twelve months, approximately how much of this was not released? Section B - 5

Table 4: Total value of retentions to be released / due to be released in the past 12 months

	£ released	£ due
< £10k	5	5
£10k - £50k	6	5
£50k - £100k	3	0
£100k - £200k	2	1
£200k - £500k	1	3
> £500k	5	0
Total	22	14

A small number of respondents also provided further information on the amount of retention not released³⁵ by certain categories:

Table 5: Further details on the reasons for this non-payment and the amount of retention

	No. of respondents	Total	Median £
Insolvency	3	£32,200	£6,500
Payer cited that obligations under another construction contract had not been met	2	£20,000	£10,000
I did/contractor did not return to fix defects	4	£113,500	£15,000
Poor quality work	2	£15,000	£7,500
I did/contractor did not claim payment of the retention	4	£103,400	£20,000
Other reasons	3	£25,100	£3,250

³⁵ Question 5b: Please provide further details on the reasons for this non-payment. Of the amount of retention not released, how much falls into each of the categories below:

Of the unpaid retentions, on average respondents (*n*10) believe that approximately **60% were unjustified**³⁶. Some of the reasons for this are included below³⁷:

- If main contractor does not complete their own defects the client does not pay them and in turn they do not pay the sub-contractor. This is even when sub-contractor has carried out any notified defects.
- There is no protection of money retained if the Main Contractor or Client becomes insolvent.
- Pay when Paid most common retort. "We still do not have the Making Good Defects Certificate under the Main Contract....."
- No demonstration of liability was made for the claimed defects.
- Works completed including all defects but due to the Main Contractor not obtaining their Making Good Defects Certificate releasing their retentions then they held onto monies due attempting to go back to back with releases relative to their contract.

When asked whether they challenged the non-payment of retention '*that occurred due to the payer citing obligations under another construction contract not being met*' there was fairly even split with **ten saying they did** and **eight did not**.³⁸

Of those **that challenged**, two said payment was then made, one said partial payment was made, two said payment was disputed, and two said nothing happened.³⁹

Section C: Late Payment of the Retention

Similar to the majority of responses that non-payment was an issue, likewise the majority of respondents also thought '*late payment*⁴⁰ was an issue for the construction sector (Figure 10 overleaf):

³⁶ Question 6: How much of the retentions not paid (question 5) were in your view unjustified within the contract terms?

³⁷ Question 6b: Why did you feel the non-payment of your retention was unjust?

³⁸ Question 7: Did you challenge the non-payment that occurred due to the payer citing obligations under another construction contract not being met (outlined in question 5a)? Section B - 7

³⁹ Question 7a: What happened when you challenged the non-payment? Section B - 7a

⁴⁰ Question 1: How significant an issue do you believe late payment of retentions is in the construction industry? Section C - 1

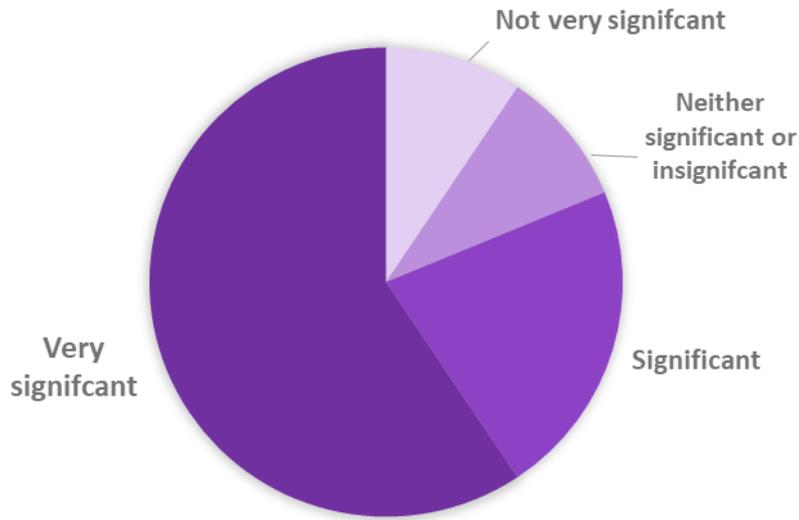


Figure 10: Significance of non-payment of retentions in the construction sector

Respondents were asked to supply the total value of retentions due to be released by them that was paid late.⁴¹ Of those that did make late payments, most were under £100k, with a small number £200k and above (table 6):

Table 6: Total value of retentions late in being released in the past 12 months

	£	%
< £10k	3	9%
£10k - £50k	6	18%
£50k - £100k	2	6%
£100k - £200k	0	0%
£200k - £500k	3	9%
> £500k	1	3%
Not applicable	13	39%
Not answered	5	15%

A small number of respondents also provided further information on the amount of retention released⁴² late by certain categories (Table 7 overleaf):

⁴¹ Question 2: Approximately what was the total value of retentions due to be released to you over the last twelve months that were paid late? Section C - 2

⁴² Question 3: Please provide further details on the reasons for late payment. Of the amount of retention paid late how much falls into each of the categories below?

Table 7: Further details on the reasons for late payment and the amount of retention

	No. of respondents	Total	Median £
I did not meet the provisions of my contract	3	£175,000	£75,000
Payer cited that obligations under another construction had not been met	2	£150	£75
The company holding the retention cited cash flow problems	3	£82	£27
Poor quality work	3	£160,000	£5,000

Of the retentions paid late, the majority (*n*8) estimated that between **75 – 100% of these had been unjustified**, with only two believing this to be 51 – 75% and three believing it between 26 – 50%.⁴³

For the **amount of time** they believed to have been unjustified, three waited between 1 – 3 months, six waited 3 – 6 months, three waited 6 – 12 months and two waited over a year.⁴⁴

Seventeen respondents provided an estimate of the cost to their business in ‘*pursuing late (including those that were ultimately unpaid) retention payments over the last twelve months*’⁴⁵ with the total **cost being £181,880** and the median cost of £2,500 (note that five respondents claimed that this process cost nothing, thus lowering the median – when removing these five the median rises to £6,500).⁴⁶

When asked whether they challenged *the late payment that occurred due to the payer citing that obligations under another construction contract had not been met*⁴⁷ **seven saying they did** and **none did not** (sixteen said it was not applicable to them and ten did not answer).

⁴³ Question 3a: What percentage of the retentions paid late (question 2) were in your view unjustified within the contract terms. Section C - 3a

⁴⁴ Question 4: For the amount that you believe was ‘unjustified’ what was the typical length of delay? Section C - 4

⁴⁵ Question 4a: Can you provide an estimate of the cost to your business in pursuing late (including those that were ultimately unpaid) retention payments over the last twelve months?

⁴⁶ Question 4a: Can you provide an estimate of the cost to your business in pursuing late (including those that were ultimately unpaid) retention payments over the last twelve months?

⁴⁷ Question 5: Did you challenge the late payment that occurred due to the payer citing that obligations under another construction contract had not been met (outlined in question 3)? Section C - 5

Of those **that did challenge**,⁴⁸ three reported payment being made. One said 'partial payment' was made, two said 'nothing happened', one has 'resorted to legal action', and one said they had 'decided not to continue pursuing due to cost' (twelve said it was not applicable and thirteen did not answer).

Respondents were also asked if they had been previously been aware that *'the 2011 amendments to the "Housing Grants, Construction and Regeneration Act 1996" mean it is no longer possible to make payment, including retention payments, conditional on the performance of obligations under another contract'*⁴⁹, to which the **majority of 58% said they had**, with 27% said they had not (15% did not provide an answer).

When asked if they would have *'challenged the late-payment (due to performance of obligations under another contract), if you had known that this is what the "Housing Grants, Construction and Regeneration Act 1996" means for retention payments'*⁵⁰, five said yes, one saying no, and four saying that it depended on the value of the contract (fourteen were not applicable and nine did not answer)

Respondents were asked for their thoughts on how future amendments to the "Housing Grants, Construction and Regeneration Act 1996" **be better promoted** to raise awareness.⁵¹

- Publicised through industry bodies
- Webinar and online training sessions
- Target learning to small and medium sized contractors
- Scottish Government should publish advice clearly stating legal responsibilities

Respondents **were split** when asked whether they had encountered *'companies which artificially inflate their tender price where a retention is being applied'*,⁵² with ten saying they had and twelve saying they had not, with six being unsure.

⁴⁸ Question 5a: What happened when you challenged the late payment? Section C - 5a

⁴⁹ Question 6: Were you previously aware that the 2011 amendments to the "Housing Grants, Construction and Regeneration Act 1996" mean it is no longer possible to make payment, including retention payments, conditional on the performance of obligations under another contract?

⁵⁰ Question 6a: Would you have challenged the late-payment (due to performance of obligations under another contract), if you had known that this is what the "Housing Grants, Construction and Regeneration Act 1996" means for retention payments? Section C - 6a

⁵¹ Question 6b: How could future amendments to the "Housing Grants, Construction and Regeneration Act 1996" be better promoted to raise awareness? Section C - 6b

⁵² Question 7: It has been suggested that some parties to construction contracts ask contractors to give an overall discount on the contract price or interim payment related thereto, in return for ensuring prompt payment. Have you encountered this practice? Section C - 7

Section D: Existing Alternative Mechanisms to Retentions

Over the last twelve months, a **small number of respondents** said they had either alternative mechanisms to retentions in place or alternative mechanisms for implementing retentions.⁵³ Three used 'retention bonds', two used 'performance bonds', and one used 'parent company guarantees (PCGs)'. None had used 'escrow stakeholder accounts' or 'retentions held in a trust'⁵⁴ (twenty-five did not answer).

An **equal number of respondents** (*n*5) used these mechanisms in addition to or as an alternative to retentions ⁵⁵ (twenty-three did not answer).

When asked what options they thought should be '*applicable for wider use across the whole sector*',⁵⁶ most respondents (42%) agreed that **retentions should be held in trust**, with 27% agreeing with **retention bonds** and 24% saying **escrow stakeholder accounts** (figure 11).

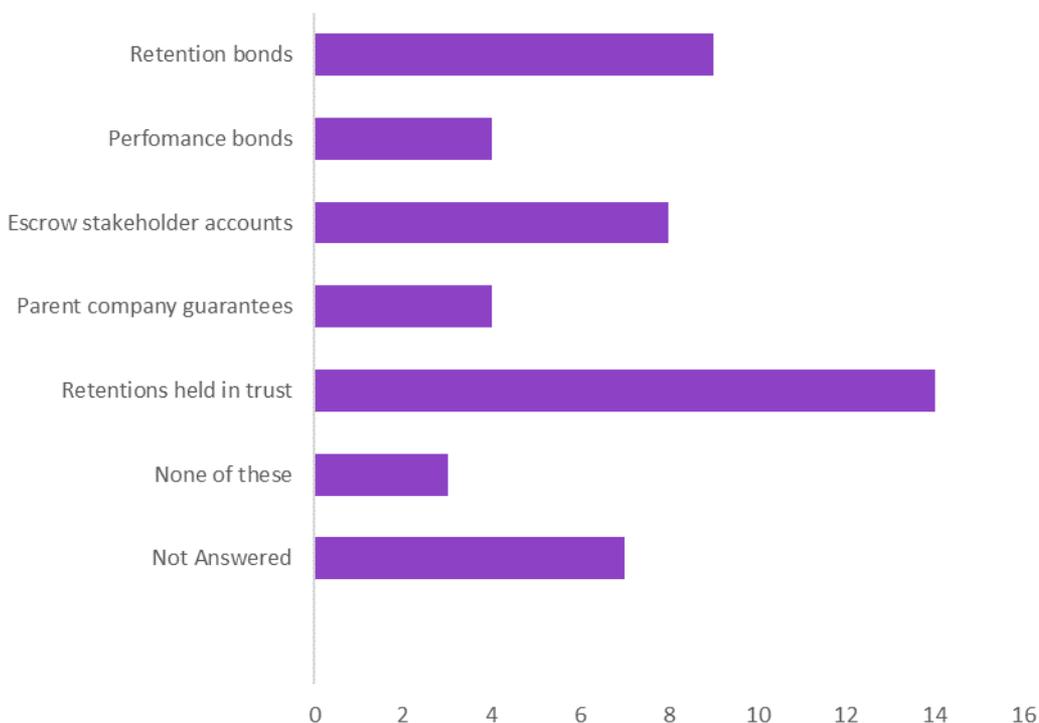


Figure 11: Options that could be applicable for wider use across the whole sector

⁵³ Question 1: Over the last twelve months, approximately how many of your construction contracts, have had alternative mechanisms to retentions, or alternative mechanisms for implementing retentions applied? Section D - 1

⁵⁴ Question 1a: Which alternative mechanisms were utilised? Section D - 1a

⁵⁵ Question 1b: Were these additional mechanisms used in addition to or as an alternative to retentions? Section D - 1b

⁵⁶ Question 1c: Which of these do you think would be applicable for wider use across the whole sector? Section D - 1c

Respondents were almost split when asked whether they thought it was *'important for Scotland to use the same mechanism of assurance in constructions contracts as the rest of the UK'* with eleven disagreeing or partially disagreeing and twelve fully agreeing or partially agreeing (figure 12). This split in support was the case regardless of whether respondents were from organisations that worked exclusively in Scotland or those that worked across the UK.

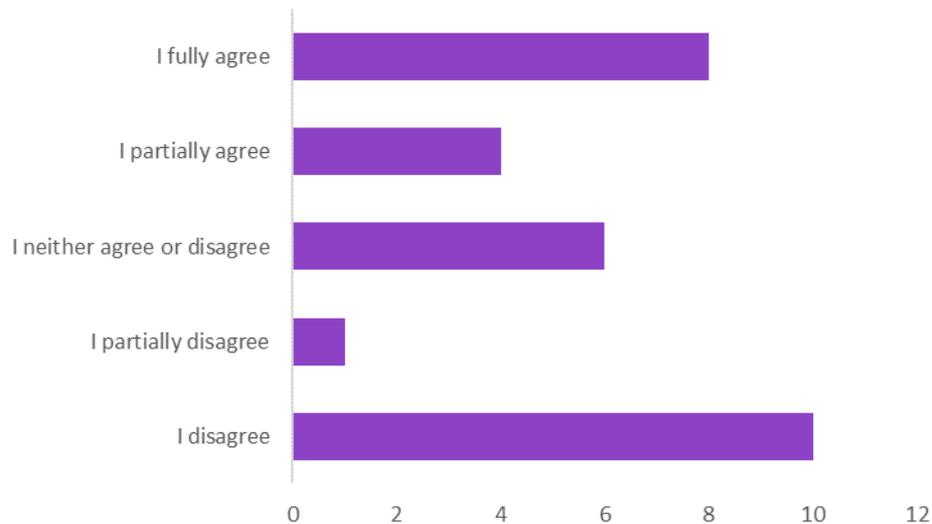


Figure 12: Importance for Scotland to use the same mechanism of assurance in constructions contracts as the rest of the UK

The **majority of respondents fully agreed and partially agreed** (42% and 24% respectively) that *'retention deposit scheme and/or holding retentions in trust could eliminate some of the critical issues associated with retentions (notably the risk of delayed or non-payment of retention monies) and provide surety against defects'*.⁵⁷ Only 9% disagreed completely, and 6% partially disagreed.

Respondents gave a variety of answers⁵⁸ as to why they believed this:

- Prevent loss in insolvency. This would provide much needed cash and confidence in the supply chain for investment.
- Release of retention should be granted as and when each trade has completed works. In the case of the Main Contractor going into insolvency

⁵⁷ Question 3: To what extent do you agree that a retention deposit scheme to protect retentions should be applied to the whole sector? Section D - 3

⁵⁸ Question 3a: Please explain the reasons for your answer to question 3 Section D - 3a

then another Main Contractor or the client can be appointed with their held retention to complete any defects.

- Those who fail to honour their obligations and therefore 'earn' release of retention will still complain
- It could eliminate some of the critical issues but it would be necessary to see what form such schemes would take before it could be said that such schemes would eliminate the issues.
- A deposit scheme would provide a safe vehicle for the cash while still providing a mechanism to access the monies in the event a firm fails to return to rectify non-compliant work.
- Having such a scheme would mean that the delay in releasing retentions would be substantially reduced or even eliminated and firms in the supply chain would have their monies protected from upstream insolvencies.
- In addition, disputes over the release of retentions could be resolved more efficiently.
- Incidence of delayed release/non-release of retentions would be substantially reduced or even eliminated.
- A serious defect can way exceed the retention fund in terms of costs to put right. The retention does not always incentivise contractors to return - the fear of being sued and reputational damage is far more powerful than taking a swipe out of cash flow. Chances are, if a contractor does not return and the retention fund is exceeded in remedying legitimate defects then they would be pursued for the balance in any event.
- Incidence of delayed release/non-release of retentions would be substantially reduced or even eliminated.
- A deposit scheme will simply provide a safe receptacle for the cash. Recourse to the monies would still be possible if a contractor has failed to return to rectify defects.
- Many issues around delayed retention payments relate to the initial release by the clients, greater emphasis/obligations are required on the contractual timescales for issuing defect schedules, what constitutes a defect and the requirement to demonstrate liability
- Provided there is an option to ask an expert involved I think the project to certify the works completed
- The scheme will still require agreement by the Client to release the retention. This could still incur delays/non-payment.
- There will probably still be opportunities to block retention release depending on financial outcomes of contracts and the commercial attitude of those involved. Getting paid for work properly done can sometimes be a bigger issue than retention release and aggressive commercial attitudes are not uncommon"

Section E: Retention Deposit Scheme

Respondents were **mostly in favour of the use of a retention deposit scheme** that *'could be used for all contracts or only for contracts over a certain value'*,⁵⁹ with 48% of respondents in favour for 'all contracts' and 30% for 'contracts over a certain value'. Only 15% were 'against its use':

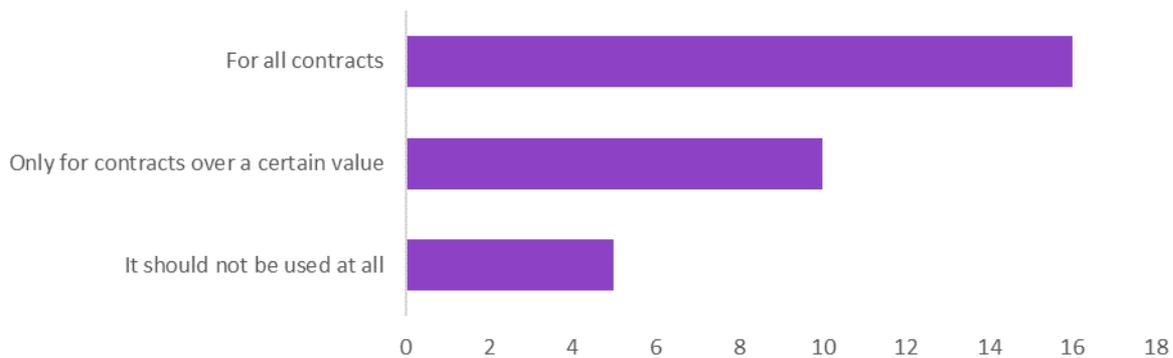


Figure 13: Support for use of retention deposit scheme

A **slight majority of respondents (n17) disagreed** that *'it is important to place a threshold on the application of any measure requiring retentions to be held in trust or ring-fenced in another way'*,⁶⁰ compared to those who agreed (n13).

Of those respondents who did agree, nine thought that less than £100k should be the minimum value of the total retained money (the retention) should it commence, three thought between £100k and £500k, and only one thought between £500K and £1m.

When asked to what extent they thought a retention deposit scheme may allow for a) *a fairer approach to retentions*⁶¹ b) *a more neutral approach*⁶² and c) *a more protected approach*,⁶³ **a clear majority either fully agree or partially agree with all three statements** (figure 14 overleaf):

⁵⁹ Question 4: How strongly do you believe that a retention deposit scheme and/or holding retentions in trust could eliminate some of the critical issues associated with retentions (notably the risk of delayed or non-payment of retention monies) and provide surety against defects. Section D - 4

⁶⁰ Question 1a: Is it important to place a threshold on the application of any measure requiring retentions to be held in trust or ring-fenced in another way and, if so, at what minimum value of the total retained money (the retention) should it commence? Section E - 1a

⁶¹ Question 2: To what extent do you think a retention deposit scheme may allow for a fairer approach to retentions? Section E - 2

⁶² Question 2a: To what extent do you believe a retention deposit scheme allows for a more neutral approach to retentions? Section E - 2a

⁶³ Question 2b: To what extent do you think a retention deposit scheme may allow for a more protected approach to retentions? Section E - 2b

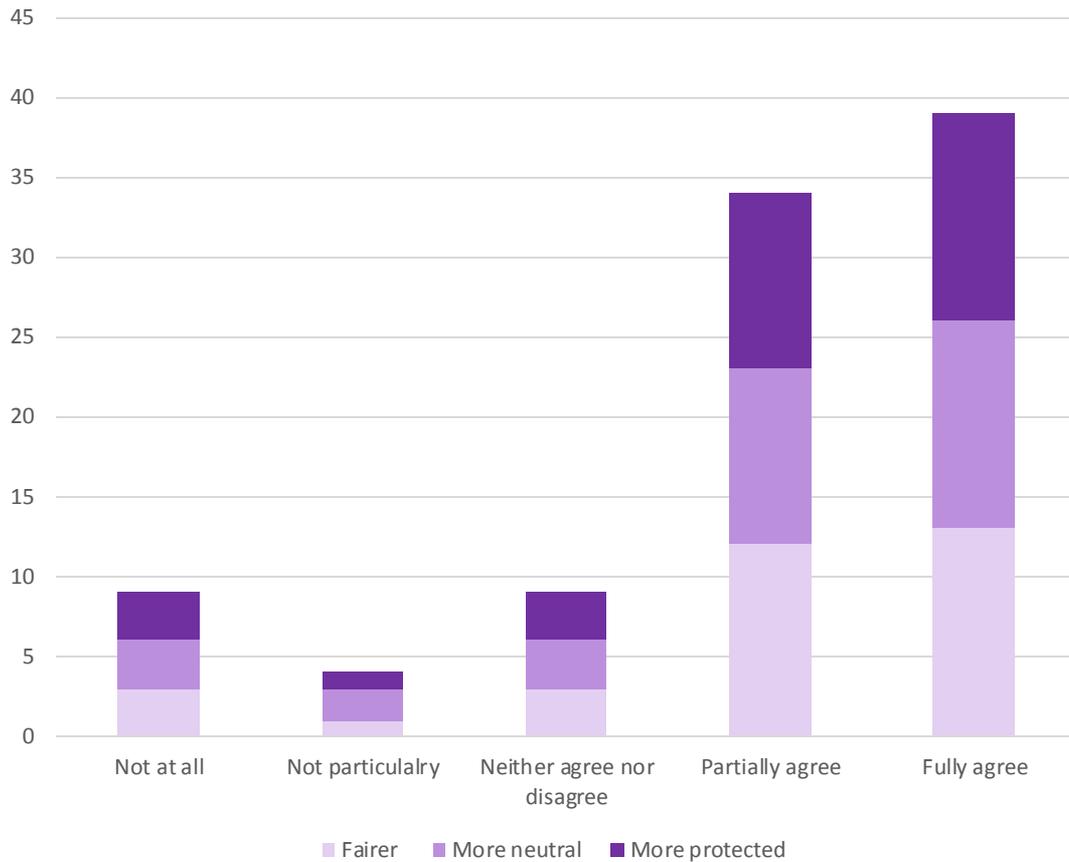


Figure 14: Perceptions of fairness, neutrality and protection of retention deposit scheme

Respondents were given a list of options from which to select features they believed *'should be included within a potential future retention deposit scheme'*⁶⁴. Most selected several options demonstrating **support for multiple features** to be included in such a scheme (table 8 overleaf).

⁶⁴ Section E – 3. Question 3: Which of the features listed below do you believe should be included within a potential future retention deposit scheme? Section E – 3.

Table 8: Options to be included within a potential future retention deposit scheme

	<i>n</i>	%
The scheme should be set up on a statutory footing	23	70%
Any disputes about the operation, amount and timing of the release of retention payments will be dealt with by existing dispute resolution processes	23	70%
The scheme can only hold retention money (plus any related interest)	22	67%
The money will be held in trust for the payee	21	64%
Businesses holding retentions under construction contracts (as defined by Part 2 of the Housing Grants, Construction and Regeneration Act 1996) will be required to deposit retentions into the scheme	20	61%
Scheme operators would be required to report on an annual basis on their performance	19	58%
Where the contract makes no such provision, the Scheme for Construction Contracts will imply relevant terms requiring retention money to be held in a deposit scheme	12	36%
The market will deliver private provision of any retention deposit scheme	11	33%

Other general additional comments⁶⁵ were provided regarding the retentions scheme, including the below:

- The approach to quality and the need to drop the assumption that defective work is a 'given'
- Retention should be scrapped altogether
- A fast, cost effective way of chasing smaller debts to be included i.e. retention paid out on a set date if no justified objection is received

Several respondents (*n*5) provided the same reply. For the sake of completion this has been quoted verbatim below:

“We do not believe that an option for contracts to make provision for depositing retentions in a scheme (with the Scheme for Construction Contracts providing the fall-back provisions) is a viable one especially for small firms. There will always be the difficulty for them of trying to assess whether the contractual provisions comply with the law. The English Court of Appeal judge Lord Justice Coulson

⁶⁵ Question 3a: Are there any additional features to the operation of a “retention deposit scheme” that you would recommend? Section E - 3a

has (extra-judicially) described the Scheme's payment provisions as a "drafting nightmare". It would be far easier and tidier for them to have the matter exclusively addressed by regulation. SEC Group has already been working on the structure for a scheme based on a distributed ledger (DLT) platform. The cost involved would be 0.23% of contract value. This would be paid by the client (or just by the main contractor if it and not the client is withholding retentions from the supply chain). This percentage figure would include the cost of administration and the provision for an insurance policy to cover any shortfalls in the scheme. A detailed explanation of how the scheme would operate is attached.

The document is hosted on website: www.rdch.co.uk and the direct document link is:

<https://static1.squarespace.com/static/5dd3ab2c9f3951087bb5a80f/t/5df659ff4f4ce57dd2510945/1576426549775/RDCH+Flyer>

It is also very important that the scheme is centralised in a single entity to allow for reduced costs, the provision of insurance, and the collection of critical data that can provide the essential transparency and trust to engage lenders and insurers, as well as providing useful data for policy makers."

Of the respondents that answered, the **clear majority (70%)** thought that the 'cost per contract (as a percentage) you would be willing to incur if it meant that your retention was held in trust in a retention deposit scheme'⁶⁶ should be below 1% of the contract value. Of the other respondents 12% said it should be 'between 1% and 3%', only 3% said over '3% but under 5%'.

For the 'price they would be willing to pay for a retention deposit scheme dependent on contract value'⁶⁷, **more respondents agreed** with this than disagreed (52% compared to 33%, respectively) (15% did not answer)

For the 'what cost would you be willing to pay (per contract) for the administration of a retention deposit scheme'⁶⁸, the clear majority of 51% said below 1% of the contract value, with 9% saying it depended on the value of the contract (39% did not answer).

⁶⁶ Question 4: Were you to have retentions held from you, what cost per contract (as a percentage) would you be willing to incur if it meant that your retention was held in trust in a retention deposit scheme? Section E - 4

⁶⁷ Question 4a: Is the price you would be willing to pay for a retention deposit scheme dependent on contract value? Section E - 4a

⁶⁸ Question 4b: If you currently hold retentions, what cost would you be willing to pay (per contract) for the administration of a retention deposit scheme? Section E - 4b

5. Next Steps

This consultation has clearly illustrated the breadth of views within the sector on the practice of cash retention and it has identified some possible policy options to address the problems associated with their use.

In the last few months we have seen an unprecedented level of collaborative working across the construction sector, including rapid co-design, consultation and communication of working practices and contract administration to support industry restart and recovery in the midst of the COVID 19 pandemic. We aim to use the strengthened spirit of collaboration demonstrated through the work of the Construction Leadership Forum to build consensus within the construction industry where possible on how to resolve the problems associated with cash retentions.

The consultation has confirmed that there is a need to investigate further a fairer, more neutral and more protected approach to assurance in construction contracts. Organisations which commission construction work must have the ability to avoid becoming liable for costs arising from unmet contract performance by implementing a means of assuring it. We propose to work with the industry to carefully consider the emerging policy options including; the possibility of a retention deposit scheme, the phasing out of retentions completely or the viability of alternative mechanisms of assurance.

We will also continue to monitor the work of the UK Government following their own consultation on the practice of cash retention in 2017.

Annex A: List of Named Respondents

Scott Nicoll	Individual	Perth and Kinross Council
Len Bunton	Individual	Bunton Consulting
Derek Riddick	Individual	
Gordon Matheson	Organisation	Matheson Plumbing Company
Jacqueline Hacking	Organisation	North East Contracts Limited
Fiona Hodgson	Organisation	SNIPEF
Alan Wilson	Organisation	SELECT
Angus Pearson	Organisation	Fortis Contracts Ltd.
Yvonne Wilson	Organisation	Specialist Engineering Contractors' (SEC)
Gordon Nelson	Organisation	Federation of Master Builders

Annex B: Respondents by SIC Code

	Total	Percent
42130 Construction of bridges and tunnels	1	3.03%
42210 Construction of utility projects for fluids	1	3.03%
42220 Construction of utility projects for electricity and telecommunications	3	9.09%
42910 Construction of water projects	2	6.06%
42990 Construction of other civil engineering projects	7	21.21%
43110 Demolition	2	6.06%
43120 Site preparation	4	12.12%
43130 Test drilling and boring	1	3.03%
43210 Electrical installation	6	18.18%
43220 Plumbing, heat and air-conditioning installation	5	15.15%
43290 Other construction installation	2	6.06%
43310 Plastering	1	3.03%
43320 Joinery installation	2	6.06%
43330 Floor and wall covering	2	6.06%
43341 Painting	2	6.06%
43342 Glazing	1	3.03%
43390 Other building completion and finishing	1	3.03%
43910 Roofing activities	2	6.06%
43991 Scaffold erection	1	3.03%
43999 Other specialised construction activities	5	15.15%
Not applicable (Client)	11	33.33%
Not Answered	2	6.06%

Annex C: List of ‘Other’ Answers to Question ‘what would be your preferred form of assurance for construction projects’

"There are various Quality Initiatives currently ongoing in Scotland which ultimately should eradicate poor workmanship from construction contracts. The concept of Passive House, which combines zero carbon design with certified quality delivery will ensure that there are no significant defects (other than shrinkage). So the view of how construction is carried out should be considered rather than the idea of accepting defects as a 'Given' and then how you cater for the rectification of these. Future zero carbon design will drive this concept."

"We need an industry wide drive on improving quality on projects and thus negating the need for retentions. Retention is draining badly needed cash flow."

"Longer term guarantee and no retention, insurance backed."

"A project account to hold client money, all contract works to be paid direct on approved application. This will protect the project, client, sub-contractors and other people in the supply chain in the event of the Main Contractor or client going into administration. In regards to retention, as a micro business I spend huge amounts of time chasing payment for retention emailing and phone calls. Sometimes I never get the money as it is not worth chasing or the company goes into administration before I get to them. The amount of ignored emails and phone calls is ridiculous. Retention should be automatically distributed to all contractors and trades as soon as it is received, you should not even need to apply. Very occasionally this does happen but the majority of the time you chase retention for a minimum of 6 months anything up to 4 years before you give up. It is common practice in the industry for trades to write-off retention before they begin, do a rush job and not return for defects this causes a problem for everyone involved in the project."

"If there is a Project Bank Account [PBA], retentions could be protected within the PBA. Otherwise selection of firms based on their technical competence rather than on lowest price would reduce defects. Moreover, changing procurement strategies to include early supply chain involvement could help inform design decisions; poor design is often the cause of defects."

"We must change procurement strategies so that the supply chain is involved in the design process from the outset to reduce the incidence of defects. Furthermore firms should be selected on their demonstration of competence rather than on their ability to offer lowest price which often leads to defects. Until the procurement process is altered, these issues will remain in the industry."

"For major tier 1 Contractors, retention is not needed, just Parent Company Guarantees [PCGs]. For Tier 2 Contractors - Performance Bonds & PCG's or retention (not both). For Tier 3 - Retention funds"

"We must change procurement strategies so that the supply chain is involved in the design process from the outset to reduce the incidence of defects. Furthermore firms should be selected on their demonstration of competence rather than on their ability to offer lowest price which often leads to defects."

"If there is a PBA, retentions could be protected. Also selection of firms based on technical competence rather than lowest price would reduce defects, and changing procurement strategies to include early supply chain involvement could help inform design decisions - poor design is often the cause of defects."

"PBA , If there is a PBA in place, retentions or an agreed sum, could be protected within the PBA. and Firms should be selected on competence, not the lowest price, as this would reduce defects."

"Do not really understand the financial implication of systems above. My experience of the retention process, as a sub-contractor, is that main contractors hold onto retention monies, earning interest, often for years with no triggers for retention release. My preferred form of assurance would be that retention monies are held by an independent organisation for example; similar to the system for private landlord tenant deposits."

"Certification of partially completed works by qualified third party professional be it the architect, cost manager or engineer."

"Where applicable (such as larger public sector contracts), retentions can protected in project bank accounts. For contractors working exclusively for domestic clients, the contract administrator or Quantity Surveyor should administer the retentions, not the client. In both cases, retentions will be held by a third party, such as a retentions deposit scheme. Indeed this is how escrow accounts operate."

"At present retentions are the simplest form of providing assurances within the construction industry. The level they are set at and the timescales involved are however punitive. Furthermore if you are operating under more than one contract with a client separate retentions should not be held."

"A mixed approach of Bonds/Escrow and PCGs depending on the Client and Contractor involved in the contract. I also feel that the value of contract would determine what approach would be most effective. If the contract value is relatively low a cash retention may still be the most cost effective measure for both the Client and Contractor/Subcontractor, or in a Contractor/Subcontractor relationship."

Annex D: Supporting Reasons Given for Agreeing / Disagreeing with Pye Tait Recommendation

The recommendation made within the Pye Tait research is - "That action should be taken to create a fairer, more neutral and more protected approach to the practice of retentions" Do you agree with this recommendation?

Respondents that answered **YES**:

"A legal requirement that retention money be deposited in a similar fashion to tenant deposits, I suppose a similar end might be achieved by use of Escrow. On short projects this may also serve to discourage the practice of retention altogether as the administration involved may come to be seen as disproportionate to the benefit."

"Retention should never equate to more than the final profit margin so there should be a cap on the % with company guarantees used over and above. There needs to be clearly identified a neutral party who can resolve disputes at a low cost. Currently if the main contractor refuses to pay part of a retention, there is usually no point pursuing it as the costs outweigh the benefit. This leaves smaller suppliers doing works for cost at best. Retention needs to be held by another party other than the main contractor with definite deadlines set and adhered to."

"Retention not to be deducted from small works agreements or contracts under certain value as the cost of recovery is greater than the sum held by the contractor, retention is treated largely as additional discount. Sub-contractors are bound by contract under defects liability period to rectify works."

"Retention periods should not be more than one year, on large contracts the value of retention should not be percentage based it should be limited."

"All monies should be held in a neutral position from the start until the end of the defects period. No-one should have access to these funds unless it is payment for work rendered on that project. Retention should be released as and when due to each sub-contractor. If 1 sub-contractor fails to adhere to their contract it should not affect the others. Once works are passed the retention should be paid and not held until everyone has met it."

"That all contracts should state that retention release is dependent on the completion by the subcontractor and that final retention should be issued 12 months after this date or have retention bonds, where the subcontractor can include this cost within their prelims or have no retention at all, but a legal statement needs to be signed at the beginning of the project, that the subcontractor will attend to any defects of their own making only. At the end of the day a company is only as good as their last project and if they do not deal with defects it could lead to a bad rep."

"By segregating retention monies in a scheme similar to the tenants' deposit scheme. This would be similar to PBAs where progress payments are ring fenced in a separate bank account."

"By having a statutory obligation to place cash retentions in a retention deposit scheme."

"The "Landlord" escrow account model where Contractors and Sub-Contractors retention fund will be held in trust. This will eliminate the retention (other people's money) being used by the higher tier party as working capital, thereby incentivising sharp practice to avoid payment. Also, where retention is being used as working capital, it can artificially improve (even on a short term basis) a trading entity's cash position, allowing Parties to trade precariously beyond that which their actual business ought to be."

"By having a statutory obligation to place cash retentions in a retention deposit scheme."

"Separate bank account for all contract funds overseen by client or clients representative not main contractor. Funds should be released on approval by M.C. with any discrepancies firstly decided by clients representative and then on to Adjudication if warranted."

"Any contractor or sub-contractor or any job should be enrolled in a construction industry scheme. These schemes would normally have a guarantee scheme within them. If either of these contractors fails to fulfil their obligation then their own scheme should be informed and the company potentially disciplined or struck off. The guarantee scheme then should be involved to cope with fulfilling the obligation. It would definitely get rid of an awful lot of fly by night companies and hopefully leave the good and compliant companies with a smoother way to fulfil all their obligations/contracts."

"By segregating retention monies in a scheme similar to tenants' deposit schemes, eg PBA's, where progress payments are ring-fenced in a separate bank account."

"Independent holder of the retention funds."

"By segregating retention monies within a scheme similar to the tenants deposit scheme s Where progress payments and final payment is ring-fenced ."

"Legal clause entered into all contracts where the employer must automatically release retention monies to contractor once their term/obligations are complete."

"Retention should not be applied automatically on every job regardless of best value."

"Retention should only be applied where it would provide a realistic incentive to return to fix defects. There should be a minimum contract value amount before retention is applied. For example a retention deduction of £3 on a £60 job provides no value and increases admin costs for both small/sub-contractor and main contractor in admin and

process costs. Main contractors should be required to have a system to release retentions monies after 12 months without small/sub-contractors needing to apply for retention payments."

"I think the needs of all parties concerned require to be addressed. Each party involved within the process requires more understanding from the various parties involved i.e. the client should understand how this would impact not just the contractor or sub-contractor but also the sub-contractor's sub-contractor/supplier etc. The chain of how retention impacts each party should be understood and everyone's concerns listened to."

"Either doing away with cash retentions or setting earlier retention release dates linked to the individual contractors sectional completion of their element of the works. As a specialist subcontractor working at the very start of a project particle completion may be some 2 - 3 years post completion of our works. There should also be an option for a third party professional to sign off the work triggering a retention. Any monies held in ret ions should be held in escrow"

"As per my answer to 4a, retention monies should be kept in a retention deposit scheme. The tenancy deposit schemes operating for tenants' are a working example of how such a scheme would operate. Ultimately the preference of FMB's membership is for retentions to be abolished in the medium to longer term. Introducing a retention deposit scheme would act as an immediate measure to address the issue. This would be part of a roadmap to remove retentions. The key point though, is that the status quo on current retentions practice must end."

"1: Retentions should only be on contracts over a certain value. 2: The principal contractor should be made to pay the subcontractor, providing the s/c has no defects, on an agreed date prior to the works commencing. There are too many principal contractors not paying the supply chain until they receive their retentions monies. This would encourage the principal contractor to complete defects quicker. 3: Retention monies should be held in a neutral bank account for protection in the event a principal contractor enters liquidation/administration."

"Stage releases & realistic caps being put in place. Earlier release after final completion."

"The process would need to be laid down in legislation. Currently we can be asked by Clients to provide both a retention amount and a performance bond. We do not see why this should be necessary to have both. It can be very difficult obtaining release of retention as time moves on and sites are sold by Clients to a third party. If monies were held in an escrow account, similar to a rental tenancy deposit scheme, there would be greater legal recourse for Contractors."

"The general Transport Scotland consensus, is that there needs to be some kind of assurance in place, but it is felt that the current system is only partially effective and retentions may not be the best form of assurance. That being said, until an alternative form of assurance is put in place it would be advisable to retain retentions. In situations

where retentions are not able to be used, other methods of assurance such as retention bonds, PCGs and escrow stakeholder accounts could be used. PCGs are often necessary with main contractors otherwise there is potential for defects not being repaired. Further, sometimes fixing serious issues can exceed the value of retentions held and some defects can arise after the release of retentions. Winding up a subsidiary company should not be an option to escape fixing defects. Escrow accounts offer the opportunity for a fairer mechanism for retention release (managed/adjudicated by an independent body) for subcontracts who cannot offer a PCG although it depends on the details of the agreement. The current contract provision adopted by Transport Scotland is the use of retention bonds, as an alternative to retention, although uptake is often varied. While PCGs are already adopted under our contracts, these are where the Contractor has had to rely on an entity to demonstrate the requisite economic and financial standing at procurement stage and are applied where a Contractor does not fulfil their obligations under the contract.”

Respondents that answered **NO**:

“No action - I'm happy with current system of retention.”

“Ban the practice of retention.”

“No action - I'm happy with current system of retention.”

“Ban the practice of retention” (x8)

Annex E: Summary of Consultation Questions

Question 1: Do you agree with the Pye Tait conclusion/area for potential further investigation that "the financial consequences for contractors and subcontractors in the event of a large organisation going into liquidation can be significant"?

Question 1a: Do you agree with the Pye Tait conclusion/area for potential further investigation that "retention money held in a main bank account can be used by the holder to fund expenditure on labour, plant and materials on other projects and/or as part of working capital"?

Question 1b: Do you agree with the Pye Tait conclusion/area for potential further investigation that "some companies deliberately avoid business in which retentions are involved"?

Question 1c: Do you agree with the Pye Tait conclusion/area for potential further investigation that "alternatives to common retention practices are available but used infrequently"?

Question 1d: Do you agree with the Pye Tait conclusion/area for potential further investigation that "the retention system in Scotland works reasonably well when all parties adhere to the letter and spirit of the agreement"?

Question 2: Which of the following do you believe to be the intended purpose of retentions as part of construction contracts? If Other - Please specify

Question 3: Do you agree that some form of assurance is needed in construction contracts?

Question 3a: How effective do you feel the current system of retention is?

Question 4: Do you agree that retentions are the best form of assurance within construction contracts?

Question 4a: If you answered no to Question 4 (i.e. you do not think retentions are the best form of assurance within construction contracts) what would be your preferred form of assurance for construction projects?

Question 5: The recommendation made within the Pye Tait research is - "That action should be taken to create a fairer, more neutral and more protected approach to the practice of retentions" Do you agree with this recommendation?

Question 5a: If you answered yes to question 5 - how do you feel this could be achieved?

Question 5b: If you answered no to question 5 - what would you suggest for the practice of retentions?

Question 6: Do you actively avoid bidding for contracts subject to retention?

Question 6a: If so, would you bid for contracts if an alternative to the current practice of retention was established or as Pye Tait recommend a "fairer, more neutral and protected approach to the practice of retentions"?

Question 7: If you were unable to use retentions what method of assurance would you use?

Question 7a: If you were unable to use retentions would your cashflow be affected?

Question 7b: If you answered yes above, what impact would not being able to use retentions for cashflow have on your business?

Question 8: Is there anything else you would like to say about the Pye Tait research?

Question 1: Can you provide an estimate of the total number of construction contracts that your business both secured and issued over the last 12 months?

Question 1a: What was their approximate combined value?

Question 1b: Of the total construction contracts over the past twelve months, how many had retentions written into the contract (i.e. a client or main contractor is holding a retention against you or where you are holding a retention over others?)

Question 1c: Approximately how many of your current contracts with retentions (where you are holding a retention or are subject to a retention) are for work undertaken in a) the public sector and b) the private sector (if zero enter 0)

Question 2: How significant an issue do you think non-payment of retentions is in the construction sector?

Question 2a: What, in your experience, are the main reasons for non-payment of retentions?

Question 3: If you have been holding retentions within the last 12 months and withheld payment. What were the reasons for doing so?

Question 3a: If you have been subject to a retention within the last twelve months and this was not repaid - what were the reasons for non-payment?

Question 4: Approximately, what was the total value of retentions due to be released to you or by you over the last twelve months?

Question 5: If retention money was due to you in the last twelve months, approximately how much of this was not released?

Question 5a: If you were due to release retention money in the last twelve months, approximately how much of this was not released?

Question 5b: Please provide further details on the reasons for this non-payment. Of the amount of retention not released, how much falls into each of the categories below:

Section B - 5b The company holding the retention became insolvent (Please provide cash value)

Section B - 5b Payer cited that obligations under another construction contract had not been met (Please provide cash value)

Section B - 5b I did/contractor did not return to fix defects (Please provide cash value £)

Question 6: How much of the retentions not paid (question 5) were in your view unjustified within the contract terms?

Question 6b: Why did you feel the non-payment of your retention was unjust?

Question 7: Did you challenge the non-payment that occurred due to the payer citing obligations under another construction contract not being met (outlined in question 5a)?

Question 7a: What happened when you challenged the non-payment?

Question 1: How significant an issue do you believe late payment of retentions is in the construction industry?

Question 2: Approximately what was the total value of retentions due to be released to you over the last twelve months that were paid late?

Question 3: Please provide further details on the reasons for late payment. Of the amount of retention paid late how much falls into each of the categories below?

Question 3a: What percentage of the retentions paid late (question 2) were in your view unjustified within the contract terms.

Question 4: For the amount that you believe was 'unjustified' what was the typical length of delay?

Question 4a: Can you provide an estimate of the cost to your business in pursuing late (including those that were ultimately unpaid) retention payments over the last twelve months?

Section C - 4a: As a value of your total construction contracts with a retention (Please provide cash value £)

Question 5: Did you challenge the late payment that occurred due to the payer citing that obligations under another construction contract had not been met (outlined in question 3)?

If you answered no above - why did you not challenge the late payment?

Question 5a: What happened when you challenged the late payment?

Question 6: Were you previously aware that the 2011 amendments to the "Housing Grants, Construction and Regeneration Act 1996" mean it is no longer possible to make payment, including retention payments, conditional on the performance of obligations under another contract?

Question 6a: Would you have challenged the late-payment (due to performance of obligations under another contract), if you had known that this is what the "Housing Grants, Construction and Regeneration Act 1996" means for retention payments?

Question 6b: How could future amendments to the "Housing Grants, Construction and Regeneration Act 1996" be better promoted to raise awareness?

Question 7: It has been suggested that some parties to construction contracts ask contractors to give an overall discount on the contract price or interim payment related thereto, in return for ensuring prompt payment. Have you encountered this practice?

Question 8: It has also been suggested that some companies artificially inflate their tender price where a retention is being applied. Have you encountered this?

Question 9: Do you have any further comments on late and non-payment of retentions?

Question 1: Over the last twelve months, approximately how many of your construction contracts, have had alternative mechanisms to retentions, or alternative mechanisms for implementing retentions applied?

Question 1a: Which alternative mechanisms were utilised?

Question 1b: Were these additional mechanisms used in addition to or as an alternative to retentions?

Question 1c: Which of these do you think would be applicable for wider use across the whole sector?

Question 1d: Please explain the reasons for your answer to question 1c

Question 2: Do you think it's important for Scotland to use the same mechanism of assurance in construction contracts as the rest of the UK?

Question 3: To what extent do you agree that a retention deposit scheme to protect retentions should be applied to the whole sector?

Question 3a: Please explain the reasons for your answer to question 3

Question 4: How strongly do you believe that a retention deposit scheme and/or holding retentions in trust could eliminate some of the critical issues associated with retentions (notably the risk of delayed or non-payment of retention monies) and provide surety against defects.

Question 4a: Please explain the reasons for your answer to question 4.

Question 5: Do you have any further comments on alternative assurance mechanisms available to the construction sector?

Question 1: Do you think a retention deposit scheme could be used for all contracts or only for contracts over a certain value?

Question 1a: Is it important to place a threshold on the application of any measure requiring retentions to be held in trust or ring-fenced in another way and, if so, at what minimum value of the total retained money (the retention) should it commence?

Question 2: To what extent do you think a retention deposit scheme may allow for a fairer approach to retentions?

Question 2a: To what extent do you believe a retention deposit scheme allows for a more neutral approach to retentions?

Question 2b: To what extent do you think a retention deposit scheme may allow for a more protected approach to retentions?

Question 3: Which of the features listed below do you believe should be included within a potential future retention deposit scheme?

Question 3a: Are there any additional features to the operation of a "retention deposit scheme" that you would recommend?

Question 4: Were you to have retentions held from you, what cost per contract (as a percentage) would you be willing to incur if it meant that your retention was held in trust in a retention deposit scheme?

Question 4a: Is the price you would be willing to pay for a retention deposit scheme dependent on contract value?

Question 4b: If you currently hold retentions, what cost would you be willing to pay (per contract) for the administration of a retention deposit scheme?

Question 1: What is your name?

Question 2: What is your email address?

Question 3: Are you responding as an individual or an organisation?

If responding on behalf of an organisation, please enter the organisation's name here.

Question 3a: If you are responding as an organisation does your business work on construction projects across the United Kingdom?

Question 4: Are your business headquarters registered in Scotland?

Question 4a: What is the nature of your business within the construction sector?

Question 4b: How many direct employees (i.e. excluding sub-contractors) does your business have?

Question 4c: What is your experience of retentions in the construction industry?

Question 4d: What SIC codes does your company operate under?

Question 5: The Scottish Government would like your permission to publish your consultation response. Please indicate your publishing preference:

Question 6: We will share your response internally with other Scottish Government policy teams who may be addressing the issues you discuss. They may wish to contact you again in the future, but we require your permission to do so. Are you content for Scottish Government to contact you again in relation to this consultation exercise?

Question: Please help us improve our consultations by answering the questions below. (Responses to the evaluation will not be published.)

Matrix 1 - How satisfied were you with this consultation?

Matrix 1 - How would you rate your satisfaction with using this platform (Citizen Space) to respond to this consultation?



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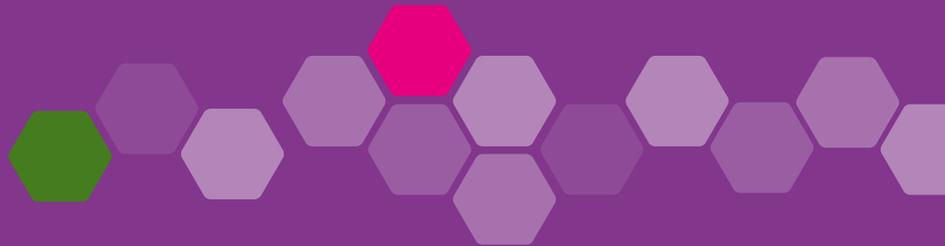
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