

## **Payment certification problems: Who is to blame?**

*Peer reviewed*

### **Abstract**

Problems with payment certificates in the construction industry have always been a popular topic which has attracted wide attention, but especially nowadays with complex and fast-track projects. As these problems often result in expensive disputes between the Employer and Contractor it was necessary to investigate what the problems are and who is to blame for these problems. A survey was done amongst twenty one Contractors and Quantity Surveyors to get their views on these problems and the results showed that there are a fair number of Contractors who inflate their payment claims, that the Employer is not always paying the Contractor within the stipulated time and that Contractors are of the opinion that the Quantity Surveyors valuation is not a true reflection of the work done.

Keywords: payment certificates, construction industry, disputes, JBCC 2000

### **Abstrak**

Probleme met betalingsertifikate in die konstruksie industrie het altyd wye aandag geniet en is veral deesdae tydens komplekse en snelgang projekte 'n gewilde onderwerp. Hierdie probleme eindig gereeld in duur dispute tussen die werkgewer en kontrakteur en daarom was dit nodig om te bepaal wat hierdie probleme is en wie verantwoordelik daarvoor is. 'n Opname is gedoen onder een en twintig kontrakteurs en bourekenaars om hulle siening oor hierdie probleme te kry en die resultate het getoon dat daar 'n aantal kontrakteurs is wat hulle betalingseise onregmatig vergroot, dat die werkgewer nie altyd die kontrakteur op tyd betaal nie en dat die kontrakteur van die opinie is dat die bourekenaars se waardasie nie 'n ware weergawe is van die werk wat gedoen is nie.

Sleutelwoorde: betalingsertifikate, konstruksie industrie, dispute, JBCC 2000

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## 1. Introduction

One of the biggest problems encountered in the construction industry is that of endless disputes between the Employer, professional team and the building Contractors regarding the valuation and payment of monthly interim payment certificates. Cheung *et al.* (2000) are of the opinion that resolving disputes has become part of routine management functions for project participants. Finsen (1999) supports this view by stating that a growing number of building contracts end in disputes because "the pressure has been on the construction industry to build more and more in less and less time; the fast-track contract has become the norm and under pressure, mistakes are inevitable". Bonheim (1999) states the most significant issues of dispute facing the construction manager, before litigation or arbitration is invoked, are the pricing of variations, disputes relating to payment certificates and repudiation or cancellation of the contract. According to Broadmore (2006), "Where any form of payment is involved there is always a fear on the part of the paying party that there may be an overpayment followed closely by the insolvency of the party who has received payment." Broadmore (2005) also states that "Creditors are entitled to prompt payment of debts ... if compliance with a deadline is overlooked; the consequences can be harsh and irreversible." Many of these disputes are as a result of increasing complex construction projects (Cheung & Suen, 2002).

These disputes occur even though there are specific clauses set out in almost all contract documents used in the construction industry. Under the principles of the Roman-Dutch common law a construction contract is an 'entire' contract. This means each party must perform its obligations in their entirety. Thus the Contractor is not entitled to any payment until he has completed what he has been contracted to do i.e. the Contractor must complete the works (building) in all respects before the employer is required to pay. Such a situation would be quite untenable for a Contractor, who would then have to carry the costs of the building operations for many months without payment.

To overcome this, almost all building contracts provide for regular payments to be made to Contractors, usually after certain stages of work have been completed, or at regular monthly intervals. In both the JBCC 2000 Principal Building Agreement (PBA) and the ISAA white form contract, there is provision for the Contractor to be

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paid on a monthly basis, and the honouring of the monthly payment certificates by the employer is the employer's primary obligation in terms of the building contract. The principal agent or architect issues monthly payment certificates reflecting the approximate value of work done and materials supplied up to the date of the valuation, less the amounts previously paid to the Contractor. According to the JBCC 2000 PBA (Clause 31.1), a payment certificate needs to be issued every month, even if it is a nil or a negative amount.

The JBCC 2000 PBA (Clause 31.2) further sets out that the Contractor shall assist the principal agent in the preparation of the payment claim in respect of an interim payment certificate by providing the principal agent with all necessary documentation and assessments of quantified amounts of work completed. The principal agent shall not, in any way, be relieved of his duties to provide an interim payment certificate, even if the Contractor has not provided relevant documentation for a payment certificate.

The value certified in such an interim certificate must include a reasonable estimate of the value of the work executed, a reasonable estimate of the value of materials and goods on site, and all amounts which have been previously certified in payment certificates. The valuing of an interim payment certificate is an extremely important process, not only for the Contractor but also for the Employer as it affects their projected cash flows. For this reason it is of utmost importance that an accurate estimate of the value of each monthly certificate is calculated in order to keep both parties satisfied.

Notwithstanding these contractual arrangements, disputes occur regularly.

## **2. Reasons for disputes**

A survey undertaken by Hughes (2003) revealed that disputes can be minimised to a great extent if there is better communication between the relevant parties and that they should assist each other better to avoid these disputes. In order to determine how this can be improved it was necessary to investigate the whole 'payment' issue. Research was undertaken amongst twelve Quantity Surveyors (registered with the South African Council for the Quantity Surveying Profession) and nine building Contractors (registered with the MBA), all in the Eastern Cape Province of South Africa. Although the survey was conducted in this province only, there is no reason to believe that the results would be different in any other regions of South Africa.

The purpose of the paper is not to point fingers at anyone, but rather to determine what the major problems are and how they can be eliminated.

The following tables indicate the views of the Quantity Surveyors and the building Contractors on issues affecting the payment of work.

## 2.1 Person preparing payment certificates

As the valuation of the work completed should be as accurate as possible, the person doing the valuation should be a senior experienced person. The following table indicates who in the Contractor's firm and who in the Quantity Surveyor's firm is responsible for valuating work to be included in a monthly payment certificate.

Table 1: Person preparing valuation of payment certificates

Person	Contractors	Quantity surveyors
	percentage (%)	percentage (%)
Contract manager	44	17
Contractor's quantity surveyor	56	-
Foreman	-	-
Student	-	-
Senior PQS	-	83
Junior PQS	-	-
Total	100	100

As seen in table 1, 56% of the Contractors stated that the Contractor's Quantity Surveyor is preparing valuation for monthly payment certificates while the remaining 44% of the Contractors maintain that the Contract Manager does the monthly payment certificates. The preparation of monthly payment certificates by Quantity Surveyors is done mainly by a senior Quantity Surveyor (83%).

This indicates that persons in senior positions should be involved in preparing monthly payment certificates and one would expect no major discrepancies.

## 2.2 Method of calculating value of payment certificate

Table 2: Method of calculating value of payment certificates

<i>Method used</i>	<i>Contractors</i>	<i>Quantity surveyors</i>
	<i>percentage (%)</i>	<i>percentage (%)</i>
Accurate measurements on site	83	0
Estimates / rough quantities	17	100
Total	100	100

There are various methods for calculating the value of interim claims; these include accurate measurements conducted on site or rough estimates of quantities taken on site. All the Quantity Surveyors have indicated that they use estimates or rough quantities to determine the value of the certificate while 83% of the Contractors base their claims on accurate measurements whilst 17% of them use the estimating/rough quantities method.

## 2.3 Inflation of value of certificate to assist Contractor's cash flow

As mentioned earlier, the value of payment certificates affects the cash flow of both the Contractor and the Employer, and there is a perception that Contractors inflate their payment claims to assist with their cash flow. The following table indicates whether Contractors do inflate their payment claim to assist with their cash flow.

Table 3: Inflation of value of payment certificates

	<i>Contractors</i>	<i>Quantity surveyors</i>
	<i>percentage (%)</i>	<i>percentage (%)</i>
Yes	44	42
No	56	58
Total	100	100

Contractors and Quantity Surveyors are both of the opinion that more than 40% of Contractors inflate the value of their payment claims to assist with their cash flow. This is an alarmingly high percentage of Contractors and it may have disastrous consequences for the Employer if the Contractor goes insolvent, especially when there is no provision for sureties or retention monies. Quantity

Surveyors should thus be very careful when evaluating the Contractor's claims in determining the value of the payment certificate. Contractors should refrain from such practices.

## 2.4 Extent of late payment by Employer

Clause 31.9 of the PBA states that the Employer shall pay to the Contractor the amount certified in an interim payment certificate within seven days of the date for issue of the payment certificate. Table 4 shows the number of days that the Employer is late with the payment to the Contractor i.e. after the 7-day period.

Table 4: Perceptions of late payment by Employer

Number of days	Contractors	Quantity surveyors
	percentage (%)	percentage (%)
0 days	-	9
1-7 days	62.5	58
8-11 days	12.5	16.5
More than 11 days	25	16.5
Total	100	100

The table indicates that the majority of payments to the Contractor are made late, even if it is less than 7 days late. Twenty-five per cent of the Contractors maintain that they are paid more than 11 days late. This has serious consequences for the Contractor and may be one of the reasons why they have cash flow problems. Architects or Principal Agents should thus ensure that payment certificates are issued in sufficient time to the Contractor for ongoing submission to the Employer for payment. They should also inform the Employer of the importance of timeous payment to the Contractor. The reason for the late payments can either be the Quantity Surveyor not providing the Principal Agent with the necessary payment information timeously; the Principal Agent being late in issuing the payment certificate; the Contractor submitting the payment certificate late to the Employer; or the Employer delaying the payment.

To determine who is responsible for the late payment, Contractors and Quantity Surveyors expressed their opinions as follows:

## 2.5 Person causing late payments to Contractors

Table 5: Person causing late payments to Contractor

Person	Contractors	Quantity surveyors
	percentage (%)	percentage (%)
PQS	40	-
Principal agent / architect	-	25
Contractor	-	12.5
Employer	60	62.5
Total	100	100

The majority of both the Contractors (60%) and the Quantity Surveyors (62.5%) are of the opinion that the Employer is causing late payments. The remaining 40% of Contractors blame the Quantity Surveyor while 25% of Quantity Surveyors blame the Principal Agent / Architect and 12.5% blame the Contractor. It must be noted (as can be expected?) that none of the Contractors or the Quantity Surveyors blame themselves as being responsible for causing late payments.

## 2.6 Failure of Contractor to provide necessary information

Clause 31.2 of the JBCC 2000 PBA places an obligation on the Contractor to “assist the Principal Agent in the preparation of the payment claim information for an interim payment certificate by providing him all relevant documents and assessments of quantified amounts of work completed”.

Table 6: Failure by Contractor to provide necessary information

Frequency	Contractors	Quantity surveyors
	percentage (%)	percentage (%)
Never	22	-
Rarely	67	67
Sometimes	11	33
Often	-	-
Always	-	-
Total	100	100

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Sixty seven percent of both the Contractors and the Quantity Surveyors are of the opinion that the frequency of necessary information being provided late is 'Rarely', while a fair number of respondents opined that this happens 'Sometimes'. Only 22% of the Contractors were of the opinion that this happens 'Never'.

Although Clause 31.2 of the JBCC 2000 PBA states that the Principal Agent shall not be relieved of his responsibility to issue an interim payment certificate whether or not such information is provided by the Contractor, the provision of the relevant information should assist all parties in finalising the payment certificate within the specified time.

### **2.7 Late payment as a result of Contractor failing to provide tax invoice**

Clause 31.9 of the JBCC 2000 PBA states that the Contractor must also provide the Employer with a tax invoice for the amount due stated in the payment certificate, failing which payment cannot be made by the Employer. Table 7 shows the extent of late payments as a result of tax invoices not being provided by the Contractor.

Table 7: Frequency of late payment as a result of late submission of tax invoice

<i>Frequency</i>	<i>Contractors</i>	<i>Quantity surveyors</i>
	<i>percentage (%)</i>	<i>percentage (%)</i>
Never	23	17
Rarely	33	58
Sometimes	44	25
Often	-	-
Always	-	-
Total	100	100

The above Table clearly shows that not submitting the tax invoice has resulted in the late payment of certificates in a fair number of instances. It is not clear why Contractors do not submit their tax certificates timeously as it is to their own disadvantage and affects their cash flow negatively.



## 2.8 Quantity Surveyor's Valuation of work completed

Contractors were requested to provide an indication of whether the Quantity Surveyor's valuation of the value of the work completed for payment certificates is a true reflection of the value of work completed. Table 8 shows the results.

Table 8: Accuracy of Quantity Surveyor's valuation of work completed

<i>Frequency</i>	<i>Contractors</i>
	<i>percentage (%)</i>
Never	-
Rarely	22
Sometimes	44
Often	22
Always	12
Total	100

A fair number of Contractors are of the opinion that the Quantity Surveyor's valuation is not a true reflection of the value of work completed. Some of the reasons for this may include:

- Quantity Surveyors not spending enough time on the valuation of work done. As the valuation of interim payment certificates is only one of the many functions they perform, it may be that they neglect this function as they do not regard it as very important;
- Quantity Surveyors not wanting to 'overvalue' the work (in case Contractor going insolvent);
- Quantity Surveyors being aware that Contractors tend to inflate their payment claims (see Table 3 above);
- Contractors (and Sub-Contractors) not providing the necessary information to enable the Quantity Surveyor to value the work accurately;
- Employers requesting the Quantity Surveyor to 'undervalue' to assist with their cash flow; or
- Principal Agent adjusting the Quantity Surveyor's valuation for the payment certificate.

It is vital that the value of each interim payment certificate is a true reflection of the value of the work completed. Contractors and Consultants should work together closely to arrive at a value which truly reflects the value of work done to assist both the Contractor and the Employer. Undervaluation results in increased escalation payable to the Contractor as the work is escalated using higher indices when eventually certified.

## 2.9 Underpayment by Employer

Table 9: Underpayment by Employer

Frequency	Contractors	Quantity surveyors
	percentage (%)	percentage (%)
Never	-	67
Rarely	67	33
Sometimes	22	-
Often	11	-
Always	-	-
Total	100	100

Two-thirds of the Quantity Surveyors were of the opinion that the Employer never underpays the Contractor. Two-thirds of the Contractors and the remaining third of Quantity Surveyors are of the opinion that the Employer 'rarely' underpays the Employer. A fair number of Contractors, however, maintain that underpayment does occur 'sometimes' (22%) and even 'often' (11%). The research did not investigate why this practice is taking place, but Employers should not make themselves guilty of this practice as it is not in accordance with the payment clauses in the PBA.

## 2.10 Default interest payable by Employer

Although the Contractor is entitled, in terms of Clause 31.11 in the JBCC 2000 PBA, to default interest payable by the Employer for payment certificates paid late, it seems that Contractors do not always insist on or take legal action if Employers fail to do this. The extent to which Contractors insist on their right to receive default interest is shown in Table 10.

Table 10: Default interest paid by Employer

<i>Frequency</i>	<i>Contractors</i>	<i>Quantity surveyors</i>
	<i>percentage (%)</i>	<i>percentage (%)</i>
Never	22	-
Rarely	67	17
Sometimes	11	8
Often	-	42
Always	-	33
Total	100	100

From the above table it appears that there is generally a fair difference of opinion between Contractors and Quantity Surveyors on whether Contractors insist on their right to receive default interest from the Employer. The majority of Contractors (22%) 'never' insist or only 'rarely' (67%) insist, while the majority of Quantity Surveyors are of the opinion that the Contractors 'often' (42%) or 'always' (33%) insist. Contractors are entitled to default interest and the fact that they almost never insist on this right to default interest may worsen the problem of late or underpayment by the Employer.

The respondents were requested to provide reasons why they do not insist on their right to default, and the following reasons were put forward:

- To maintain a good relationship with the Employer (71% of Contractors, all Quantity Surveyors);
- To ensure a smooth handover at the end of the project (14% of Contractors); and
- The hassle of getting approval (14% of Contractors).

The above shows that the majority of Contractors and Quantity Surveyors were of the opinion that legal action is not taken against Employers to maintain good relationships with him; possibly to secure future work.

### **3. Conclusion**

It is evident from the results of the survey that there are many problems and irregularities regarding interim payments to the Contractor for work done. It shows that there are a fair number of Contractors who inflate their payment claims, that they do not always provide the necessary information to the Consultants and that late payments are frequently caused by failure to provide tax invoices to the Employer. The results also showed that the Employer is not always paying the Contractor within the stipulated time and that Contractors are of the opinion that the valuation for work done is not a true reflection of the actual work done. A fair number of Employers are also guilty of underpaying the Contractor and most of the Contractors and Quantity Surveyors maintain that the Employer is the person responsible for late payments to the Contractor.

One of the reasons for many of these irregularities may be as a result of incompetent or inexperienced persons handling interim payment certificates. However, the results showed that it is senior Contractors and Quantity Surveyors who are responsible for evaluating, preparing and submitting interim payment certificates. These persons should thus know what is expected of them in terms of the contract conditions and should assist each other to minimise problems. If all parties communicate their requirements well in advance to one another and provide the necessary information which is required in terms of the contract conditions, there should be no reason why payments are late or not reflecting the true value of work completed. Many Contractors should also re-think whether they should not insist on their right to default interest payable by the Employer as this may be one of the reasons why Employers keep on paying them late or underpaying them.

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