

Insights

NEC, INTERPRETING PAYMENT NOTICES AND NEGATIVE CERTIFICATES

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SUMMARY

There have been a number of cases about the validity of payment notices recently, which shows that 'smash and grab' adjudications are still seen as an effective way to improve cash flow. The recent decision in **United Utilities Water Ltd v Northstone (NI) Ltd (t/a Farrans Construction)** [2026] EWHC 1057 (TCC) considered whether the contractor was required to, and failed to issue, a pay less notice within a one day period, looking at the validity of the payment certificate and the effect of dates inserted by CEMAR. This was in the context of an amended NEC3 ECC Option C form of contract with bespoke amendments.

WHAT HAPPENED

The case concerned water infrastructure works in West Cumbria. Under the contract entered into in 2017, the joint venture contractor agreed to construct 32 kilometres of cross-country raw water aqueduct and 24 kilometres of network water mains pipelines.

Following the start of the works, there was a growing number of disputes and compensation events, which meant the pain share was increasing and there was a concern that this would affect behaviours and other contracts as part of the same project.

This led to a settlement agreement in 2018 and a deed of variation in 2021, which changed the payment basis from Option C to Option A and introduced a milestone schedule for the remaining activities in the activity schedule. The contractor could apply for payments as soon as each milestone was completed and the payment period was reduced from 35 days to 15 days. The initial total of the Prices was £85m and this was increased to over £130m.

In October 2024, the contractor applied for payment in respect of Milestones 9 and 11. This was done via a single communication using CEMAR (a cloud-based IT system used on the project to manage the contract) and enclosing two applications for payment. The Project Manager

responded on 11 October 2024 saying that Milestone 9 had been achieved but not Milestone 11. The Project Manager then used CEMAR to issue payment notice PA-70, responding to the two payment applications and identifying the "amount due" as a negative payment in the sum of - £3,269,328.05.

That sum had been calculated in accordance with the definition set out in Core Clause 50.2 and the notice enclosed two supporting schedules which had been uploaded to CEMAR on 10 October 2024 in which the Project Manager set out the assessment for each of the two applications. The contractor responded with a payment reduction notice (pay less notice) dated 17 October 2024 (received on 18 October 2024), which was said to be pursuant to clause Y2.3 of the contract and without prejudice to the position of the contractor that no payment reduction notice was required.

The employer commenced an adjudication on the basis that the pay less notice was 6 days late, as it should have been issued by 12 October, i.e. within a day of the payment notice. The adjudicator agreed and held that the contractor was obliged to pay the employer £3,269,328.05.

THE PARTIES' ARGUMENTS

When the employer started enforcement proceedings, the contractor issued a Part 8 claim to decide whether PA-70 was a valid payment notice and, if so, was the contractor obliged to issue a pay less notice if it wished to pay less than the amount notified.

The contractor argued that the payment notice uploaded on CEMAR showed a later due date of 8 November and that it was not served by post or email, and that therefore PA-70 was not free from ambiguity. This was also because on the assessment tab, whilst there were details of how the Project Manager had come to the two different figures (minus £3,269,328.05 in respect of Milestone 9 and nil in respect of Milestone 11) there was only a single payment notified. It was also argued that identifying a negative figure did not automatically mean that the employer was in fact demanding repayment.

The employer argued the issues were not suitable for a Part 8 claim, as it was necessary to look at the relevant factual background and the context for the payment notice. It was said that it was relevant that the earlier decision by Joanna Smith J in **Advance JV v Enisca Limited** [2022] EWHC 1152 (TCC) was in connection with the same project and was based on the same NEC3 contract and use of CEMAR.

The employer's position was that, when interpreting the payment notice, it is necessary to decide what the reasonable recipient of the notice would consider when receiving it, which was not possible on the evidence presently available before the court. This was because the contractor argued the background to the deed of variation was irrelevant and the contractor's witnesses did not address in any detail the evidence on the background provided by the employer's witness.

That evidence concerned the benefit to the employer in changing the payment basis, and for the contractor in having a shorter payment period, but also the fact that both parties knew that it was unrealistic to try to change CEMAR to reflect the new terms agreed. That evidence also highlighted the fact that the amended terms were a substantial benefit to the contractor, and while they required the employer's team to assess payment very quickly, the contractor knew the payment periods and could be ready to issue a pay less notice within one day.

THE COURT'S APPROACH

The judge agreed with the employer that the issues raised by the contractor were not suitable for a Part 8 determination.

This was because the issues were not limited to the interpretation of the contractual wording in the context of the Housing Grants, Construction and Regeneration Act 1996. The main issue was how a reasonable recipient would have understood the notice and while the employer provided some evidence of the background, the contractor did not provide enough evidence to enable the court to interpret the language chosen in the contract by the parties within the relevant factual matrix.

It also held that it was relevant that the parties to the contract were sophisticated and experienced and were required to act in the spirit of mutual trust and cooperation. In particular, the judge highlighted the lack of evidence about the amendments to the contract, how CEMAR was used in practice before and after the amendments were agreed, and what was understood to be the procedure using CEMAR after the amendments to the contract. These factual matters were key to the interpretation of the notices and what would be understood by the reasonable recipient.

On that basis, the contractor's claim was rejected and the adjudication decision was enforced.

KEY TAKEAWAYS

This decision concerns a common situation, where initial issues on a project are resolved by negotiation and the parties in effect 'reset' the contract based on settling past issues and agreeing a different commercial basis which they believe would result in better delivery. This is often a good way to resolve issues and avoid disputes from escalating, but this decision shows that it is necessary for the parties to implement any such changes correctly and understand their practical impact.

When it comes to the validity of payment notices, there have been a number of recent decisions as to whether errors or deficiencies in a notice result in invalidity. This decision is a useful reminder that this is a question of interpretation which is based on the objective standard of the reasonable recipient, combined with the subjective knowledge that the parties have and the background and context for the relevant circumstances.

It is also interesting to note that while the judge did not have to decide the impact of having just one day to issue a pay less notice, it was relevant that these were sophisticated and experienced parties and that, as required under the NEC form of contract, they were required to act in the spirit of mutual trust and cooperation. While the judge did not expand on the latter point, it can be assumed that this is why it was necessary to have evidence as to what the parties knew about the use of CEMAR following the changes to the payment periods. Like with the other decisions on the validity of payment notices, the wider message is that each case does not only depend on the contract wording but also the factual circumstances and what was known to the parties.

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