CROSSRAIL LIMITED

EXECUTIVE COMMITTEE (PSG) PAPER

SUBJECT: **Project Bank Accounts**

MEETING: **28th October 2009**

1.0 Purpose

The purpose of this paper is to seek Excom (PSG) approval to the strategy proposed for the adoption of Project Bank Accounts (PBAs) on Crossrail.

The paper:

- follows Excom's (PSG) agreement to the initial proposals submitted on 5th August 2009;
- provides a brief summary of the OGC's fair payment initiatives, including PBAs, and the business case rationale behind their adoption;
- includes an overview of how the PBAs would work and supporting notes on their roll out and adoption, including commercial and risk considerations;
- includes a case study on the use of PBAs on the Channel Tunnel Rail Link;
- has been produced by the PBA working group, which comprises representatives of CRL Finance, CRL Commercial and Crossrail Central.

The paper is structured as follows:

- an overview of PBAs;
- proposed PBA strategy;
- proposals for the roll out and adoption of PBAs;
- commercial and risk considerations;
- supporting appendices, including the finalised Crossrail Fair Payment Charter, background on the OGC fair payment initiatives relating to project bank accounts and the Channel Tunnel Rail Link case study.

2.0 Recommendation

It is recommended that Excom (PSG):

- approve the strategy proposed for the adoption of PBAs;
- give final approval to the Crossrail Fair Payment Charter;
- extend the remit of the PBA working group to develop the PBA strategy further including the development of implementation plans.

3.0 Project Bank Accounts, Overview

The OGC describe the PBA as a “fair payment for all system”, which ensures that the contractor and the contractor’s supply chain receive prompt payment of monies rightfully due through certified interim payments.

Under OGC proposals, the PBA is the medium through which payments are made, but it is not a contractor’s account and it can be set up in trust in order to protect the interests of the whole supply chain.

Further details of how OGC believe that a PBA would operate are given in Appendix A1.6.

Project Bank Accounts were successfully adopted on the Channel Tunnel Rail Link and a case study on how they were implemented is given in Appendix A1.7.

While the overarching objectives behind the CTRL and OGC PBA models are similar, there are differences in the establishment and operation of the PBA. By way of example, the PBAs established on CTRL did not use a trust arrangement and were used principally to provide cost visibility for the employer. The other principal differences are highlighted in Appendix A1.7.

Under NEC Option C the Employer pays a four week forecast of Defined Cost. One of the ways by which to mitigate any perceived risk inherent in the NEC approach is a PBA which gives significantly greater transparency of payments made by the main contractor.

4.0 Proposed PBA Strategy

Objectives

- The contractor for each of the NEC Option C main works contracts to be awarded after 31st March 2010, will be required to establish a PBA in joint names with CRL. This will require provisions to be included in earlier ITT documentation.
- CRL will review the applicability, benefits and practicality of adopting PBAs on any other contracts let after this date, including those to be let under NEC Option A (lump sum priced).
- It is not the intention to adopt PBAs on packages let under the enabling works framework contracts (including Royal Oak portal) because of the stage in their development and the potential impacts on the procurement process.

- The success of the PBA will be largely dependent on the adoption of an open book contractual approach. This is the standard approach under NEC Option C contracts.

- The PBA model to be adopted will broadly follow that used on CTRL (see Appendix 1.7) and will be updated in line with NEC3 to adopt the trust arrangement.

- The PBA will be used alongside payment mechanisms with the objective of keeping contractors in a cash neutral position.

- The contractual interim and final valuation process in NEC will be altered as required to cater for CRL's internal finance systems and processes.

- The development and implementation of the PBA will be driven by the PDP, with input and oversight by the CRL PBA working group made up from CRL Delivery, Commercial and Finance. The working group will report to Excom on progress and will liaise with the OGC and TfL.

Payment Periods and Programme

- OGC's model fair payment charter suggests that the period for payment from application through to receipt of certified monies should be 30 days for all tiers of the supply chain.

- The current CRL payment periods do not achieve this.

- There are two alternatives to achieve the 30 day target:

    - Increase the four week cost forecast included in the Contractor's payment (under NEC conditions) such that there are sufficient funds to allow payment to the supply chain at the intervals required to meet the 30 day payment objective.

    - CRL's payment period to be 16 days from the issue of the project manager's payment certificate and based on a 28 day assessment cycle.

    The activities that must be undertaken during this payment period are shown in Appendix 3, with a summary given in Figure 4.1 below.

- It is proposed that the conditions of contract be amended to provide that the final date for payment is 16 days after the date on which payment becomes due (the date of the Project Manager's certificate). This period is shorter than the 23 day period currently included in enabling works contracts.

- The advantages of a shorter payment period over an increase in the forecast amount are seen as being:
    - the potential for errors in calculating the forecast amount is less;
    - the level of funding sought by the Employer and interest on any borrowing is reduced; and
    - the amount of money held in the PBA is reduced which in turn reduces the risk of monies subject to insolvency proceedings, etc.
- The conditions of contract will be amended to provide that any notice of withholding is to be issued 5 days prior to final date for payment.

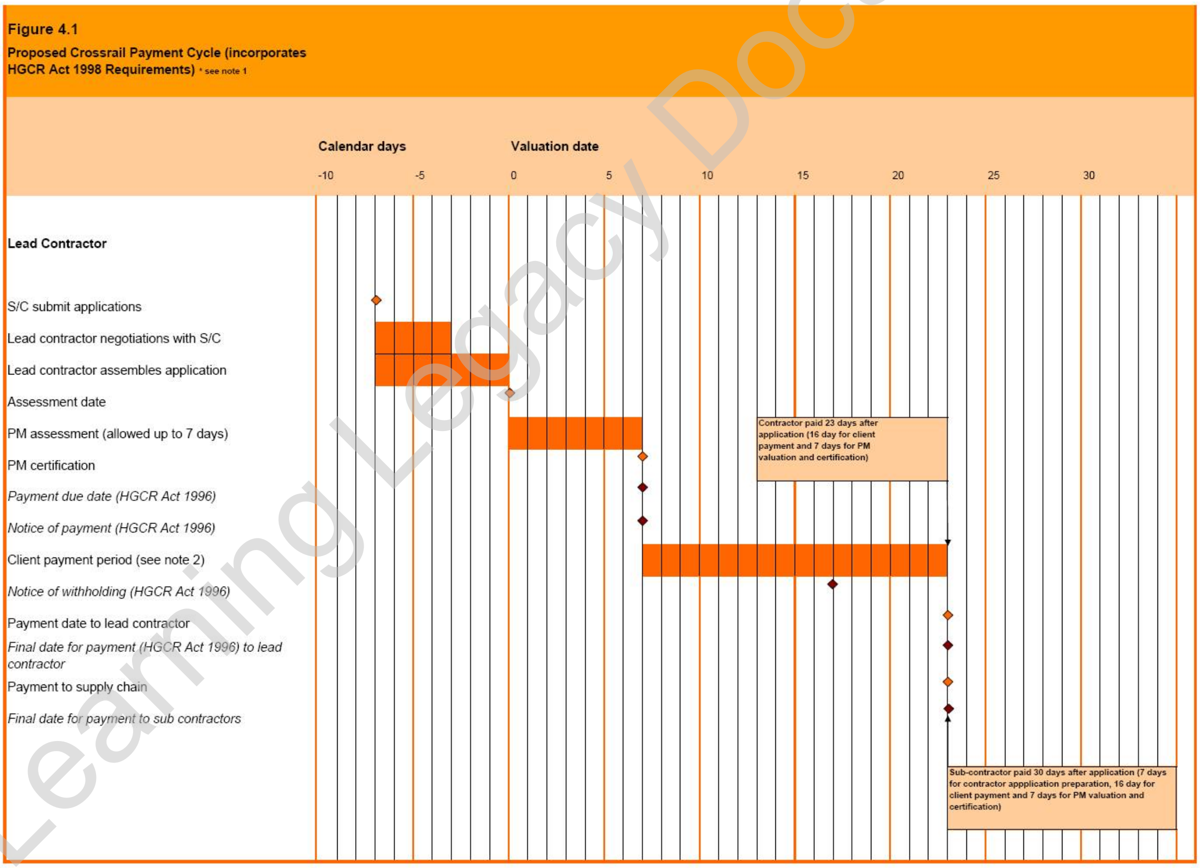


Figure 4.1
Proposed Crossrail Payment Cycle (incorporates HGCR Act 1998 Requirements) * see note 1

Notes:

1 PM considers any application but no obligation on the Contractor to produce application for payment . PM has to assess.

2 Client payment period 16 days.

Interest and Fees Due

- Beneficial ownership of interest gained on the PBA will be designated to CRL under the terms of the contract and trust deed.

- Justified fees arising from the normal operation of the bank account (such as transaction charges) would be part of the Defined Cost and therefore paid by CRL.

- Fees arising from the poor operation of the PBA (such as interest charges) will be classed as a Disallowed Cost and as such payable by the contractor.

Trust

- A trust deed will be put in place in respect of each contract which adopts a PBA. This trust deed would seek to allocate beneficial ownership of the monies contained within the PBA amongst the main contractor and subcontractors.

- Each trust deed would be signed by all participating parties (i.e. the employer, main contractor and designated subcontractors).

- The trust seeks to ensure that the supply chain receives sums due to it in the event of main contractor insolvency. It would allocate beneficial ownership of individual amounts due to participating subcontractors, seeking to prevent an insolvency practitioner for the main contractor being able to claim these monies.

- This trust arrangement has not yet been tested by the insolvency courts and there is a school of thought that the trust deed may not in fact achieve the desired result and that the amounts due to subcontractors might not in fact be protected against main contractor insolvency.

- There is a possibility that the trust arrangement could be considered to be a preference in the event of main contractor insolvency such that CRL could be held liable to pay sums which have been paid to subcontractors again. CRL Legal is taking specialist advice on this point and the PBA working group will revert to PSG in the event that there is considered to be any significant risk to CRL.

- The bank's charge for hosting the PBAs on the basis of the trust arrangement may be higher than if the trust arrangement was not adopted.

- Any deposit in a PBA will not be protected by the Bank of England consumer protection rules. It is not guaranteed that the trust would protect the monies but any means to mitigate this risk will be considered when agreeing the appointment terms of the bank.

- The PBA working group has not identified any other key disadvantages to the trust arrangement (other than the administrative process of putting the trust deed in place).

- It is proposed that CRL should adopt the trust arrangement albeit in the knowledge that it may not prove to provide the desired protection.

5.0 Roll Out & Adoption

The following approach is proposed for the roll out and adoption of Project Bank Accounts on Crossrail.

Legal and Contract

- Bespoke contract terms will be developed based on PBA clauses published in NEC3 amended to suit CRL's detailed requirements (see below). These will include:

  - mandating the use of a PBA for payment of all Defined Costs and defining the payment process and notice provisions required for its operation; and
  - defining the procedures by which a contractor sets up and implements a PBA.

- In addition, a form of trust deed will be developed, under which CRL will seek to provide protection for the supply chain.

- The NEC3 option C will provide an open book approach, allowing greater transparency of supply chain payments beneath tier 1.

Financial

- The selection of a bank will be at the discretion of the contractor but subject to CRL approval.

- A separate bank account will be set up by each separate contractor.

- Each bank account will be fully visible online with full transactional capabilities assigned to designated CRL staff. Each account will be reconciled weekly by the CRL finance team.

- All payments into each account must be made in line with CRL's Delegation of Authority.

- To ensure security is maintained, all notifications of payments and other instructions to the PBA will only be made by pre-registered contractor / client representatives.

- The proposed payment profile will be 23 days from application to pay the main contractor; 30 days from application to pay sub-contractors.

- Balances on each account should not exceed the latest assessment certificate (including 4 weeks forecast funding from the date of that assessment).

- The bank account and all procedures will be open to standard audit procedures by CRL internal audit and cost assurance teams and by KPMG external audit.

Procurement

- Tenderers will be briefed on the perceived benefits, format and operation of the PBA at tender period briefing meetings.

- Tenderers will be required to submit their proposals for compliance with the fair payment charter (including their willingness to enter into a trust arrangement if appropriate) as part of their tender submission and these will be evaluated.

Contract Administration

- The traditional contractual process of preparing and certifying monthly valuations or milestones will be unaltered by the PBA arrangement.

- The look-ahead period to be included in each monthly valuation will be four weeks, subject to whether adjustment is necessary to meet the 30 day supply chain payment period (see above).

- The tier 1 contractor will be able to draw down on the project bank account without client authorisation to make payments of Defined Costs and to transfer his fee for onward disbursement.

- The project bank account will be subject to client audit by the project manager to ensure only allowable amounts are drawn from the account.

- KPIs to monitor the number of days from assessment date to sub-contractor payment date will be prepared by the PDP in conjunction with CRL Finance.

- Consideration is being given by the PDP to the benefits of a programme and compliance (PACT) team and this will be the subject of a separate Excom paper.

- All contract related payments (including sub contract payments) will be made from the PBA.

- Sub contract invoices will be based on contractor's certified amounts.

Training

- Training of the client's team in the operation of the account and the benefits of its use for the whole supply chain will be a key to its successful implementation.

- The training will need to include:

  - operation of the account;
  - the process for establishing a PBA on a new project;
  - roles and responsibilities of key contacts at the selected bank;
  - the rationale for its use and the benefits; and
  - educating the supply chain during the tendering process.

Involvement of Others

- CRL have consulted the OGC throughout the development of these proposals, through a series of meetings and community practice groups.

- In view of the OGC's commitment to the Fair Payment Initiative & PBAs, it is proposed that CRL provide further feedback to OGC following the detailed development of CRL's proposals. This feedback would be done at meetings and through attendance at OGC best practice workshops.

- CRL will liaise with TfL and agree the use of PBAs. CRL Finance will work with TfL Group Treasury and arrange the normal project funding.

Publicity and Industry Consultation

- An external announcement should be made regarding the adoption of PBAs and CRL's objectives behind doing so.

- The PBA announcement could be done in conjunction with publicity regarding CRL's signing of a Fair Payment Charter.

- Consideration will need to be given to a joint announcement with the OGC and to the need for any follow on articles with the trade press.

- The objectives behind the adoption of PBAs and the proposed methodology for its implementation will be discussed with tenderers at tender briefing meetings.

6.0 Risk and Commercial Considerations

The NEC Panel prepared a document in June 2008 entitled "OGC fair payment practices for use with NEC Contracts".

The NEC document includes a series of proposed Z clauses which address the establishment of a project bank account, the procedures for making payments from it and the establishment of a trust deed.

The document also provides a series of guidance notes and flow charts relating to their application and the timescales to be adopted for assessment and payment under the project bank account arrangements.

Two banks, Barclays and the Royal Bank of Scotland" have now established project account facilities in line with OGC proposals. However, most other high street banks will be familiar with PBAs through the work done on CTRL.

It will be necessary to identify those banks which are able to provide PBAs based on the trust arrangement.

The principal risks associated with adopting PBA are shown in Figure 6.1 and are based on the findings of OGC and CRL's working group.

Figure 6.1 – PBA, Risk Review

	Risk	Mitigation
OGC1	Failure to achieve payment periods.	Confidence in achieving payment certainty. CRL needs to ensure that it can meet the timescales imposed for payment consistently.
OGC2	Contractor's failure to open PBAs.	There will be a contractual requirement to establish a PBA.
OGC3	Cost of implementation.	The majority of costs will be in the initial set up of PBAs and training. Most of these will be one off costs.
OGC4	Loss of cash flow benefits to the tier 1 contractor. The potential reluctance of main contractors to adopt PBAs due to the administrative burden involved and the loss of their ability to accumulate interest on amounts before making onward payments to the supply chain.	The cash neutral approach adopted on CTRL means that the contractor should derive significant savings in interest payments as well as obtaining more competitive sub contactor prices through certainty of payment. The reluctance of main contractors to adopt PBAs was not experienced on CTRL where main contractors appeared comfortable with the arrangement.
OGC5	Tier 1 contractor's due diligence of sub contract applications.	The vetting and agreement of sub contract interim and final valuations would be unaltered.

Figure 6.1 – PBA, Risk Review

	Risk	Mitigation
WG6	Potential for the employer to be drawn into payment disputes between main contractors and subcontractors.	It is considered that this risk could be realised if the NEC drafting was adopted in full since it requires the employer to sign the authorisation to make payment to individual subcontractors. It is proposed that this risk could be mitigated by removing this requirement and leaving the main contractor alone to sign these authorisations.
WG7	Risk that the trust arrangement which may be put in place around the PBA may not be sufficiently robust to provide the desired protection for subcontractors.	The adequacy of the trust arrangement to protect against main contractor insolvency cannot be known until the situation arises and is tested in the insolvency courts. The risk may, however, be reduced by ensuring that the period between payment by the employer into the PBA and the onward authorisation of payments to subcontractors is as short as possible. As noted above, CRL Legal is taking specialist advice over any potential risk to CRL associated with the trust arrangement.

APPENDIX 1 – Fair Payment Charter

A.1 Crossrail Fair Payment Charter

"Fair and transparent payment practices are essential to achieving successful integrated working on construction projects. In working with each other in good faith and in a spirit of mutual trust and co-operation, we agree that we will establish processes and systems to meet the 'Fair Payment' commitments set out below:

- Companies have the right to receive correct full payment as and when due. Deliberate late payment or unjustifiable withholding of payment is ethically not acceptable.
- 'Fair Payment' will apply equally between the client and lead contractor and throughout the supply chain
- The process will be transparent in order that members of the supply chain have certainty of how much and when they will be paid.
- Companies will consider, where appropriate, operating relevant contracts on an open book basis.
- The correct payment will represent the work properly carried out, or products supplied, in accordance with the contract. Any arrangements for retention and any withholding of payment due to defects or non-delivery will be proportionate and demonstrably justified in line with arrangements made at the time of contract.
- To ensure effective and equitable cash flow for all those involved, all contracts will provide for regular payments and have payment periods not exceeding 30 days.
- In order to avoid payment delays, the client and all supply chain members will agree payment procedures at the outset of their contracts. Payment will generally be through electronic transfer and will apply throughout the supply chain.
- Monitoring and auditing and problem resolution procedures will be agreed between the parties.

We the undersigned agree that this Charter is not intended to be a legally binding document and not used in construing any contractual commitment."

APPENDIX 2 – Project Bank Accounts, Supporting Notes

A.2 Fair Payment Practice

The Office of Government Commerce (OGC) produced a guide to "Fair payment practices" in June 2007 which makes the case for change in construction payment practices and follows on from a series of government initiatives in the 1990's, most notably Sir Michael Latham's recommendations in July 1994, which led to the Construction Act in 1996, and the Late Payment of Commercial Debts (Interest) Act of 1998.

The OGC have recently established a Fair Payments Community Group and will be taking action to achieve a greater take-up of best practice across Government Construction Clients. It is expected that the OGC Gateway Review process will be used to check that Clients are giving proper consideration to the use of Project Bank Accounts. Departments who are implementing the OGC Guidance include Defence Estates and the Ministry of Justice.

The OGC guide describes fair payment as being whether the contractual terms relating to the discharge of payment obligations and the payment process are fair and adhered to and it recommends principles and practices to be adopted in the public sector.

OGC highlight that poor payment practices in the construction industry give rise to substantial additional financing and transaction costs and they emphasise that certainty over how much and when payment is made builds up trust between supply team members and underpins collaborative working to achieve value for money projects for clients.

The stated aim of the improvements recommended by OGC is to provide greater certainty on payments to everyone in the supply chain and to optimise payments periods in order to minimise financing charges. Based on their analyses OGC contend that public sector clients could expect to save up to 2.5% on construction costs from the introduction of better payment practices.

OGC estimate that widespread adoption of these principles and fair payment practices set out in their guide would save the public sector some £200m rising to over £750m as the processes become embedded and confidence in the system increases. In the current economic climate it is also anticipated that the adoption of fair payment practices will help to reduce the risk of supplier failure due to cash flow problems.

OGC's proposals include:

- the adoption of a fair payment charter, which should be agreed and signed by the client and the main supply chain members working on a project or a framework of projects. An example of this charter is given in Appendix 2.
- targeting payment of the supply chain within 30 days.
- shorter payment periods, greater use of milestone payments and the inclusion of past performance on payment as a key pre-qualifying criterion for contractors.
- the introduction of project bank accounts where "practical and cost effective".

A2.2 Overview

The OGC guide recommends that public sector clients should adopt certain principles as the basis for reviewing their procurement strategy and procedures with regard to payment practices. These principles are embedded in what OGC call a "Fair Payment" charter.

- *Best "Fair Payment" practice process*
  Achievement of fair and efficient payment requires significant time commitments at the outset of a contract to agree and harmonise payment procedures and cycles in order to achieve the charter commitments of a maximum 30 day payment period.

- *Contractor relationships and selection*
  Evidence of good and current performance on "fair payment" should be a key pre-qualifying criterion for selection of lead contractors and through the "fair payment" charter or contractual arrangements to further tiers of the supply chain.

- *Simplification of interim measurement*
  OGC recommend the greater use of well defined milestone payments and payment schedules to simplify measurement and certification systems.

- *Retentions*
  Unfair withholding of retentions has an adverse impact on cash flow and is detrimental to relationships on site and clients are recommended to monitor implementation of the charter commitments.

- *Project Bank accounts*
  OGC see very good alignment between the establishment of a PBA and the "fair payment" principles and recommend progressive adoption where practicable and cost effective.

- *Performance monitoring*
  Client's are recommended to monitor their own and their supply chain's compliance with the fair payment charter. OGC intend to conduct a review of the progress on implementation of the fair payment charter in Jan 2010.

- *Cost of implementation*
  OGC acknowledge that the start up and training costs of PBAs will vary in accordance with project size and complexity. OGC state that costs of initial implementation would be between £5-£10k, much of which would not be required in full on follow on contracts. OGC anticipate bank charges would be offset by interest generated while interim payments are on deposit for larger projects.

A2.3 OGC Recommendations

The OGC make the following recommendations regarding the adoption of best "fair payment" principles and practices in the public sector:

- Formally adopt principles of "fair payment".
- Require "fair payment" charters to be signed.
- Introduce best practice payment processes targeted at achieving payments to the supply chain within 30 days.
- Consider more frequent interim measures, shorter guaranteed payment periods and advanced certification (not payment) in cases where contractors and suppliers can offer substantial discounts (cases of up to 10% have been quoted by OGC).
- Use evidence of good and current performance on "fair payment" as a key pre-qualification criterion for selection of lead contractors.
- Make greater use of milestone payments and payment schedules to simplify interim measurement process.
- Monitor charter commitments regarding fair contract terms and fair withholding of payment.
- Progressively specify the use of PBA where practicable and cost effective.
- Monitor compliance with the "fair payment" charter.

A2.4 Project Bank Accounts

OGC envisage that the client will set up a deposit account and will make payment of amounts due under the main contract directly into it. Before the client's money is paid into the account, the contractor must prepare a breakdown of the main supply chain payments included in its valuation.

Under the operating mandate for the account, the authorised signatories for the client and the contractor then release funds directly to the supply chain in the amounts contained within the contactor's breakdown.

The account itself is governed by a trust deed under which the key subcontractors can claim money if the contractor becomes insolvent and helps to segregate project funds from any other funds.

Under OGC's proposals, contractors would be prevented from delaying payments due. However, contractors would still determine the amounts due to sub contractors and set off and counter charges would remain unaltered.

The project bank account would not provide additional comfort in the case of client insolvency since the amount paid by the client into the account would only be the amount due to the contractor already. OGC trust arrangements would be designed to protect sub contractors who are party to the trust deed.

The main benefits of a Project Bank Account are seen as being that it:

- ensures the lead contactor and the supply chain receive prompt payment of monies rightfully due through certified payments;
- allows the supply chain to receive payment from a single central account rather than through the lead contractor;
- encourages greater transparency and cost efficiencies and puts and end to poor payment practices.

A2.5 Industry Endorsement

As highlighted by the Specialist Engineering Contractor Group (SEC), the National Audit Office Report on "Improving Public Services through better construction" (March 2005) has recommended the use of project bank accounts to ensure effective and fair payment mechanisms. The report can be found on the NAO website and SEC have publicly given their support to it's recommendations.

In its report, the NAO state that:

"Unfair payment practices such as unduly prolonged or inappropriate cash retention undermine the principle of integrated team working and the ability and motivation of specialist suppliers to invest in innovation and capacity.

Departments should have the appropriate visibility of the entire supply chain. Understanding how specialist contractors, and particularly small and medium sized enterprises, are engaged, evaluated and managed can contribute considerably to the achievement of value for money.

For example, Departments should ensure that they have in place effective and fair payment mechanisms, such as project accounts to provide certainty to suppliers payments dependent on delivery to time, cost and quality."

The NAO express the view that:

"The approach of using a single bank account for the entire construction ensures the timely payment of all parties and mitigates the risk of the main contractor unfairly withholding payments from suppliers further down the supply chain."

The NAO report quotes the case study of Defence Logistics Organisation Offices at Andover North in relation to project bank accounts:

"Defence Estates were concerned to ensure the timely payment of all parties working in the supply chain to manage risk that the prime contractor might unfairly withhold payment s from sub contractors. A project bank account was set up in trust for the whole supply chain and payments from it needed the authorisation of the client and the prime contractor. Defence Estates also had the ability to audit the account. The use of the single bank account helped to ensure the timely payment of all parties in the supply chain."

A2.6 OGC Proposals for the Establishment of PBAs

OGC envisage that there would be four key stages in establishing and managing a project bank account. These are broadly as follows:

- Early familiarisation training for client staff and, post contract, for the selected contractor;
- During early planning and pre-procurement;
- During the procurement of the contracting team;
- Following appointment.

The OGC report also highlights important considerations in relation to the following:

- *The operation of the project bank account*
  The PBA is the medium, through which payments are made, but it is not a contractors' account, it is set up in trust for the whole supply chain.

- *Transaction security*
  To ensure security is maintained all notifications of payment and other instructions to the PBA can only be made by pre-registered contractor/client representatives.

- *Payment process*
  The process of preparing and certifying valuations or milestones is unaltered by the PBA arrangement. The client's role where joint signatures or joint authorisation of transactions are adopted, is merely to confirm payments transfers from the account.

- *Visibility and auditability*
  In order to secure the support and trust of all parties, the account needs to be transparent and open to scrutiny and audit.

- *Trust status*
  The PBA is in effect held in trust for the whole of the supply chain and prevents a receiver seizing the proceeds of the account. An example of a trust is given in the OGC guide.

- *The selection of suitable projects*
  In principle PBAs can be applied to any size of project whether one off schemes or part of an ongoing programme of work. However, in light of the costs involved they are better suited to a programme of work or a larger project. PBA's can be applied to traditional lump sum and open book arrangements, although in view of the differing degrees of client visibility authorisation arrangements will be different.

- *Training the client's team*
  Training of client's staff on the operation of a PBA is a key to it's successful adoption. This training should cover roles and responsibilities, the rationale for its use, the benefits to the supply chain etc.

- *Selecting and appointing a bank*
  The selection of the correct PBA will be dependent on the type and value of project. For a programme of works a call-off arrangement with a selected bank needs to be established, after initial trials, in accordance with an agreed protocol.

- *Changes to the tender invitation and contract documentation*
  Standard tender documentation will need to be modified to accommodate a PBA. Changes will include mandating the use of the PBA, defining payment processes and the notice of payment provisions. Further amendments will need to cover the scale of bank charges, tenderer awareness training, amendments to the marking regime, post award training etc.

- *Arrangements for supply chain members outside the PBA*
  OGC recommend that the PBA is adopted on larger contracts initially, in view of the costs associated with their initial establishment. The OGC envisage that over time it will, however, be possible to include most levels of the supply chain, accepting that there will be projects, which are too small or for other reasons are not suited to the PBA arrangements.

- *Briefing tenderers*
  Tenderers must be appraised of the PBA arrangements during the tender process including the process for setting up the account, how it is to be operated, what charges will be levied and how interest will be dealt with.

- *Training successful contractors and their supply chain*
  OGC recognise that there is likely to be concern that PBAs are a means of attacking contractor margin and training (at all levels) is therefore considered an essential part of the adoption process to highlight the long term benefits that can be derived through lower tender prices, greater collaboration and cooperation.

- *Finalising payment arrangements*
  Although the operation of the PBA is standardised, the detail of payment arrangements may vary from client to client and project to project eg monthly payments versus milestones and the levels and degree of authorisation.

- *Activation of the account;*
  Some clients may wish to open the PBA themselves while others may ask their appointed contractors to do so.

- *Operation of the account*
  Interim payments are agreed in the normal way, including the review and evaluation of the payments due to each member of the project supply chain by the contractor. The agreed interim payment is authorised by the client team and money is transferred directly into the PBA by the client's bill paying department. The client and main contractor then jointly authorise payment transactions by pre-registered contractor or client representatives.

A2.7 Case Study, Channel Tunnel Rail Link

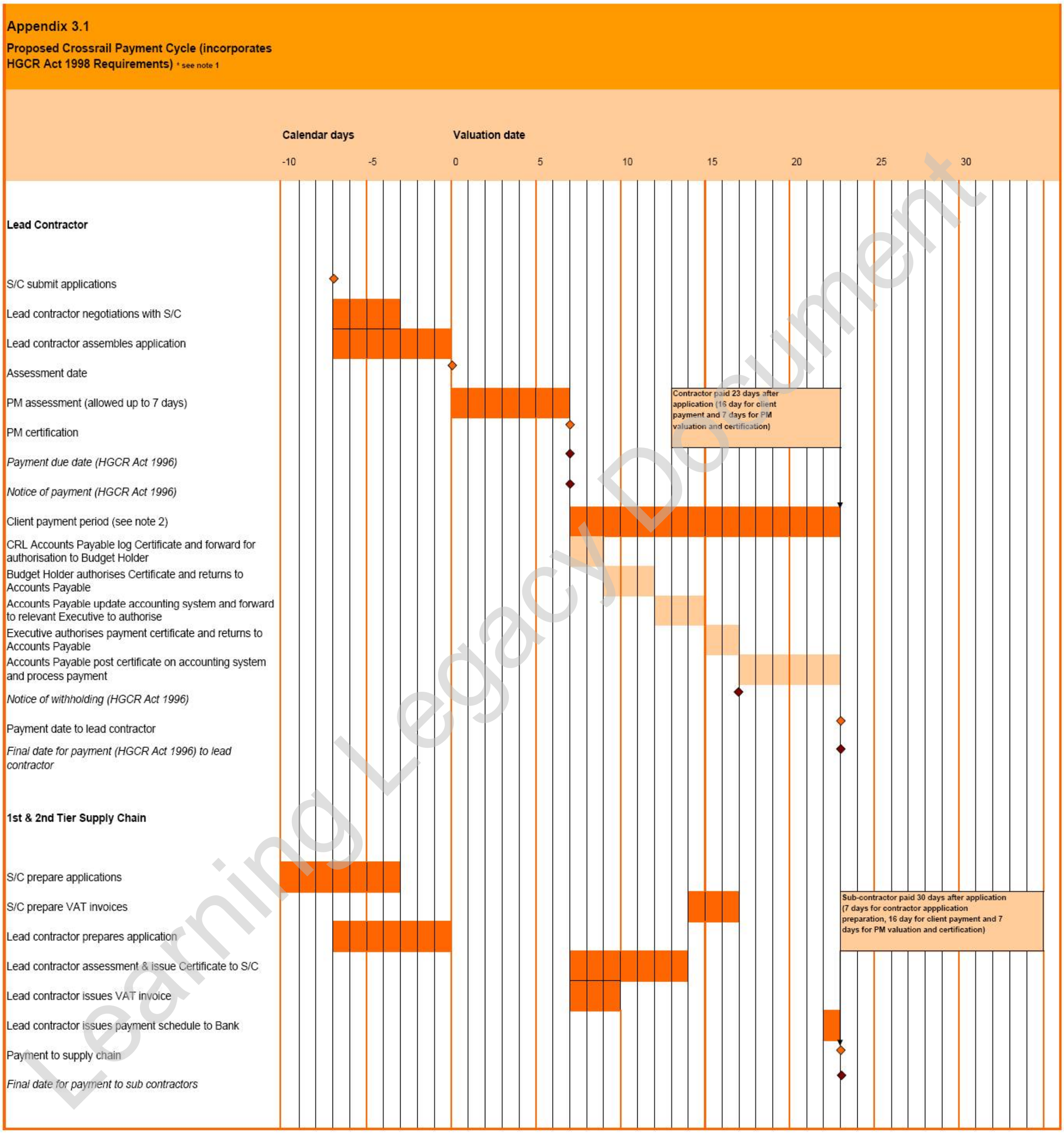
- CTRL established a form of project bank account through which it made all contract payments.
- Each of the main contracts (15 at peak) had a requirement for the contractor to set up a project bank account. Each contract had its own bank account. These accounts were set up through the usual high street banks (Lloyds, Barclays etc).
- The initiative was established to reduce contractor related finance charges (based on the premise that the client could borrow money more cheaply) and to improve payment periods and predictability.
- Interest gained on the account rested with the client.
- The account was geared to ensure contractors had a neutral cashflow.
- The account was widely regarded as saving the client in the region of 3% of its main works costs.

- The balance maintained within the account was based on actual and projected expenditure over the following period.
- CTRL adopted a 28 day certification/payment cycle.
- The look ahead period was initially seven weeks.
- The projected expenditure was adjusted to reflect actual spend in the previous period against forecast.
- It was possible for the client to certify negative payments and under these circumstances the contractor could be required to fund the account to cover any amounts due.
- The tier 1 supplier could draw down on the account without client authorisation and at anytime. All payments of Actual (Defined) Cost were made from the PBA.
- Sub contract invoices were based on contractor's certified values.
- The account was subject to client audit to ensure only allowable amounts were drawn from the account.
- Contracts were based on NEC2 option C (or in the case of sub contracts option A), with an open book approach allowing greater transparency of supply chain payments beneath tier 1.
- NEC2 wording regarding the definition of cost of works to date (along the lines "of payments made to sub contractors"), was preferred to the wording now adopted in NEC3 (along the lines of "sums forecast to be due").
- The account was established in joint names.
- A number of contactors chose to use cheques as their preferred method of payment to address internal payment authorisation issues, but the use of new electronic banking procedures would have been viable had they existed at the time.
- The PBA was not set up as a trust.

The principal differences between the OGC model and the CTRL model would appear to be:

- Client authorisation before payments are made from the account.
- Monthly payments by the client from the PBA based on certified amounts versus withdrawals by the contractor as and when required in relation to the project (in parallel with the normal contractual processes).
- The trust status of the account.

APPENDIX 3 – Detailed Payment Cycle



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