

## Advisory Note: Finance No 2 Bill 2021 – Red Diesel Reform

From 1 April 2022, the construction industry, along with many others, will face a serious blow from the new restriction on the use of “red” diesel introduced by the Finance No 2 Bill 2021. Users of off-highway applications will soon need to make the transition to white diesel, at an extra 46.81 pence per litre. While this may have a positive impact on the environment, with the encouragement of cleaner alternatives, many in the construction industry are questioning how they will be affected by the changes in light of ongoing or future construction contracts.

We set out below some commentary about the position under some standard form building contracts, but it is crucial to note that many contracts have been amended using schedules of amendment or “Z Clauses”. It is very important to review each contract individually to ascertain the effect, if any, of any change in the law.

### JCT

In relation to JCT Design & Build 2016, we advise looking at the relevant provision concerning the exercise of any statutory authority which directly affects the works. Firstly, it is important to note that JCT standard form includes a “Base Date”, being the date after which changes in the law might be relevant to the contract.

Under Clause 2.26.12 of the JCT Design and Build Contract, a Relevant Event (being an event, the occurrence of which might entitle contractors to additional time) is “*the exercise after the Base Date by the United Kingdom Government or any Local or Public Authority of any statutory power that is not occasioned by a default of the Contractor or any Contractor’s Person but which directly affects the execution of the Works*”. Under this provision, contractors will be entitled to claim that a Relevant Event has occurred if the law has changed after the contractual Base Date. However, one must query how useful an entitlement to additional time will be in relation to transitioning away from red diesel. Will it be possible to put forward a legitimate, critical path-based time claim as a result of this law change?

Changes in the law under JCT give entitlement to time, but not money. Entitlement to money must fall under a Relevant Matter as per Clause 4.21, which can include Changes under Clause 5.1. However, the wording of the contract does not provide for a change in the law amounting to a Relevant Matter or a Change. This will inevitably be frustrating for contractors as, given the increased costs of using white diesel, money is perhaps more pivotal in relation to the change in law on red diesel.

## **NEC**

In the context of NEC contracts, X2 is an optional additional clause which parties may have selected and, if included within a contract, provides, in broad terms, that any change in law after the Contract Date is a Compensation Event. Without the selection of X2, the Contractor accepts the risk of any changes in the law and therefore will not be able to recover any costs or time.

*Option X2 provides that “a change in the law in the country in which the Site is located is a Compensation Event if it occurs after the Contract Date. The Project Manager may notify the Contractor of a Compensation Event for a change in the law and instruct him to submit quotations. If the effect of a Compensation Event which is a change in the law is to reduce the total Defined Cost, the Prices are reduced”.*

It is important to note here that the change must be in the law where the site is located. Sites affected by the Bill must therefore be in the UK/NI. Furthermore, the change in the law must occur after the contract date to trigger a Compensation Event. Despite X2 indicating that the Project Manager may notify the Contractor of the change of law, the contractor could, indeed should, also notify the Project Manager as per Clause 61.3, otherwise contractual entitlement to time and for money will be lost.

Disputes may ensue regarding when the change in the law occurred. The specific provision on the restriction on red diesel will come into force on 1 April 2022, however there may be scope to argue that the law changed when the Finance Bill 2021 becomes law. See below.

We urge parties to remember that X2 is often amended to exclude any changes in the law that the parties should have been aware of prior to the Contract Date even if the change happens at a later date. This could have detrimental consequences for the potential recovery of monies or time.

Interestingly we are seeing Employers being reluctant to include X2 because of the experience they have had in recent years following significant changes in the legal landscape e.g. Brexit, Covid-19 and now, red diesel.

### **The Finance No 2 Bill 2021**

Bills must be agreed by both Houses of Parliament and receive Royal Assent from the Queen before it can become law and an Act of Parliament.

The Finance No 2 Bill 2021 is still some bit away from achieving Royal Assent. It is currently, at the time of this note, at the committee stage in the House of Commons.

Therefore, the change in the law will happen when it comes into force. It is important to note the Contract Date, as per X2, a Compensation Event must occur after the Contract Date. Contract Dates after 1 April 2022 will not avail of a Compensation Event under X2, only those dated beforehand will. Similarly, under JCT, the change in the law must come into force after the Base Date.

What does this mean for entering contracts now given that the change is due in April? We would advise that NEC X2 and JCT Clause 2.26.12 cover changes in the law, including that in April, but parties can also provide more clarity by introducing bespoke amendments to deal with the red diesel change specifically. However, contracts being drafted now should be wary of including specific reliance on future legislation changes and dates, as we have seen delay time and time again within Parliament, especially given the current pandemic situation.

If entering contracts now, with knowledge of the change in law in April, will contractors still be entitled to a claim? Theoretically, yes, however that is why we advise specific and bespoke inclusion for such an event. Employers entering contracts at this stage may choose to omit X2 given its scope come April and this will have a detrimental effect on any claim a contractor may wish to bring upon the red diesel ban.

### **Going forward**

We advise that when entering new NEC contracts prior to the Finance Bill being passed, it is wise to agree, where possible, a bespoke Compensation Event which deals specifically with the red diesel issue. Both parties are aware of the issue so they should discuss it and agree with one another what impact it will have contractually. This will allow clarity and certainty around the matter. Further detail can be included that the Contractor/Sub-Contractor can recover additional costs resulting from the use of red diesel. Similarly, under the JCT umbrella, we advise to consider including new Relevant Events which can be used to specifically provide time relief for having transitioned to white diesel.

Regarding existing contracts containing X2, we envisage it being hotly debated as to when the event should have been notified, both as an Early Warning and a Compensation Event. We advise that the “safest” approach is to issue Early Warning and Compensation Event Notices now on the premise of what is expected to happen. This notice can include that the change applies from 1 April 2022, and if this date is changed, it can be updated by issue of an updated Compensation Event notice.

Moreover, under JCT, given that an extension for time claim is the only relief available to contractors, it must be noted that despite time being granted, eventually the new legal provisions will catch up, and so, putting measures in place in advance would be wise to avoid any issues. Employers under JCT will benefit from no contractor entitlement to money in light of the change of the law, however, employers must bear in mind the financial implications this may have for some contractors, especially given the current climate. Whilst red diesel restriction alone may not be enough to put a contractor’s lights out, couple this with Brexit, Covid-19, material costs and

availability, many contractors may fold under the pressure. Employers should therefore be wise to the financial implication at play here and assess this when tendering new projects or managing current ones.

It is clear that all parties must be aware that Relevant Event and Compensation Event claims based on the provisions discussed above are likely to become more common as a result of legislative change.

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