



## Précis Paper

### Building and Construction Industry Security of Payment Act

We have broadcast several discussions on security of payment legislation with reference to particular cases. This 50 minute discussion is about the framework of the legislation by Frank Hicks of counsel. It is very useful indeed. Frank's analysis and comments are a fine introduction.

#### Discussion Includes

- What is the regime established by the *Building and Construction Industry Security of Payment Act*?
- What is the policy of the Act?
- Does this regime make a substantial difference from the common law that would otherwise apply?
- Who does that regime apply to?
- What sort of errors by an adjudicator constitute jurisdictional errors?
- What natural justice obligations do adjudicators have?

## Précis Paper

### Building and Construction Industry Security of Payment Act

1. In this edition of BenchTV, Frank Hicks (Barrister) and Ian Benson (Solicitor) discuss the *Building and Construction Industry Security of Payment Act 1999* (NSW) as well as some recent cases Mr Hicks has been involved in as a barrister: *Veer Build Pty Limited v TCA Electrical and Communication Pty Ltd* [2015] NSWSC 864 and *Lewence Construction Pty Ltd v Southern Han Breakfast Point Pty Ltd* [2015] NSWCA 288.

#### The Building and Construction Industry Security of Payment Act

2. The *Building and Construction Industry Security of Payment Act* (hereafter "the Act") was passed in 1999 but, according to Mr Hicks, only became an effective piece of legislation in 2002-3 when amendments were made to it which provided for claimants to recover progress payments rather than have those progress payments secured by a principal. The Act seeks to establish a regime whereby a party that undertakes to provide construction works or services have a capacity to obtain progress payments for those works/services, even if their contract does not provide for such progress payments to be made. The Act enshrines a statutory regime whereby progress payments may be sought and recovered, principally through a process called adjudication. The adjudication process involves the submitting of a payment claim, the answering of that claim with a payment schedule and an adjudication of any issues which arise by reference to the contentions raised by the claim and the schedule where they have been identified.

#### Changes to the Common Law Position

3. The Act provides significant changes to the common law position. Ordinarily, under the terms of a contract, a party may submit a claim for payment which may be refused by a respondent builder or principal. Usually, under common law, in order to recover the money said to be due and payable, a claimant would have to proceed through the ordinary court process by filing a statement of claim or summons and then prove their claim substantively before a judge or arbitration. The Act has an object of ensuring those entitlements to payment are dealt with quickly and on a "pay now and argue later" basis. Entitlement to receive a progress payment exists as a matter of statute following the process which is available under the Act, however this entitlement and the adjudication that one is entitled to a progress payment is not determinative of the substantive rights of the parties under the terms of the contract or by reference to other legal provisions which may apply, such as the *Australian Consumer Law* or the common law. The Act thus facilitates progress payments on an interim or on account basis for the benefit of contractors who have undertaken to perform construction work or to provide related goods and services.

4. The Act has also been held in some cases to change the risk of insolvency by moving the onus or the risk of insolvency away from the contractors who have performed the work and are awaiting payment and putting it on to the party which is obliged to make payment on an on account basis.

### The Object of the Act

5. The object of the Act is stated in s 3 of the Act:

#### **SECTION 3:**

##### ***Object of Act***

- (1) The object of this Act is to ensure that any person who undertakes to carry out construction work (or who undertakes to supply related goods and services) under a construction contract is entitled to receive, and is able to recover, progress payments in relation to the carrying out of that work and the supplying of those goods and services.*
6. It was observed in the second reading speech of the Act by the Minister Morris lemma that cash flow is the 'life-blood' of the construction industry and the failure to obtain cash flow when margins are often very narrow on construction projects can be very detrimental for contractors. The object of the Act is thus to ensure that the cash flow keeps flowing and contractors, particularly smaller contractors, are more likely to stay afloat.

### Impact and Success of the Act

7. In Mr Hick's view, the Act has been largely successful and has certainly made a difference in regards to its objects. The Act has changed the landscape for the ability of contractors to recover money and get paid for works along the way and has somewhat changed the mindset of the industry, with the reduction of disputes at the end of projects over payments. Additionally, several matters or disputes which would not have been settled, if ever, but for a significant process or litigation have resolved at a much earlier stage. It is often recognised on a commercial basis at least that it is often better to resolve a matter and move onto the next project rather than having ongoing disputes.

### Structure of the Act

8. The Act is effectively split into three parts. The first part is described as preliminary and identifies the objects of the Act (s 3) and various definitions. Additionally, s 7 identifies to whom the Act is applicable and provides some specific exclusions. Part 2 sets out the principle entitlements under the Act, that is the entitlement to a progress payment on and

from a reference date and how that progress payment is to be assessed. Part 2 also includes a prohibition described as a "pay when paid clause". Lastly, Part 3 sets out the process by which the entitlement to the progress payment may be claimed, the adjudication process that can be engaged and the enforcement of the entitlement to a progress payment either following the issue of a payment claim which is unanswered by a payment schedule or following an adjudication determination. There are a series of rights including the entitlement to seek judgment, suspend works and to otherwise seek recovery of monies which are specified in Part 3 of the Act.

#### Procedure of the Act

9. The procedure under the Act involves the submission initially of a payment claim. A party who claims to be entitled to a progress payment, set out in s 8 of the Act, may make a claim under s 13 of the Act, which specifies what a valid payment claim must set out and contains particular prohibitions about the time frame for the submissions and against the making of multiple payment claims. The payment claim, to be valid, must specify the amount that is claimed and the construction work to which it relates. The recipient of the claim is then obliged to issue a payment schedule within a strict time frame.
10. If a payment schedule is not issued in answer to a payment claim, the claimant effectively has two options. Firstly, it can move immediately to recover the amount of the claim as a debt due pursuant to s 14(4) of the Act by seeking judgment in a court of appropriate jurisdiction under s 15(2) of the Act. Alternatively, the claimant can seek to engage the processes of the Act by issuing a notice under s 17 of the Act informing the respondent that it proposes to seek adjudication and providing the respondent a further opportunity to then provide a payment schedule.
11. Assuming a payment schedule has been provided, either initially or following the s 17 notice, the matter is then referred to adjudication by reference to s 17 of the Act. The adjudicator is charged with determining the issues, particularly what amount, if any, is due by way of a progress payment pursuant to s 22(1) of the Act. In reaching that determination, the adjudicator is required to consider specific matters relating to the Act, the construction contract, the payment claim, the payment schedule, together with any submissions duly made pursuant to s 22(2) of the Act. There are further matters which apply to the adjudication including the relevance and the binding effect of prior determinations by earlier adjudicators where they are of significance.

#### Debate and Jurisdictional Errors

12. There has been considerable debate about whether there are other essential requirements for the making of a payment claim including the extent to which s 13(5), which is a prohibition

on making a second payment claim, effects the validity of the claim and, indeed, the adjudication process. There has also been consideration in cases about whether or not it is necessary that a reference date exists in order to found the payment claim.

13. A question which can often arise, in particular where one has an adjudication process, is the extent to which the courts can review what the adjudicator has done and assess whether or not the adjudicator was relevantly right or wrong. This often requires consideration of administrative law principles like jurisdictional error as non-jurisdictional error, for example regarding the construction of a contract term, will not invalidate the adjudication for the purposes of entitlement that arises for a progress payment. A number of cases have considered the extent to which an adjudicator's determination is either within power, in which case it cannot be challenged at this stage since substantive rights and entitlements continue to exist, or outside of power, in which case the adjudication itself is void and the processes and procedures of the Act which allow enforcement cannot be engaged.
14. The finding of jurisdictional errors has varied in the case law. An error with respect to a prohibition has been found to be a jurisdictional error, for example an adjudicator finding that a construction contract exists may be capable of challenge if the court is satisfied that no construction contract exists. Moreover the prohibition on submitting a payment claim pursuant to s 13(5) where it is in fact a repeated claim using a reference date that has already been utilised for a payment claim has been said to engage the provisions of the Act such that there is a jurisdictional error if the adjudicator determines the matter incorrectly. It has also been held that the making of a valid payment claim which gives rise to a valid adjudication does not require the existence of a reference date and the question of whether a reference date exists is a question for the adjudicator. Fraud or bad faith, however, will automatically vitiate any adjudication.
15. A failure to afford procedural fairness or natural justice may also constitute jurisdictional error. There is a requirement for adjudicators to give a fair hearing and allow both parties to be heard. Issues may arise where one party's submissions appear to be disregarded or ignored or where an adjudicator makes a finding based on an argument, contention or issue where the parties have not been given an opportunity to offer any submissions on the matter. It can be difficult to establish that there has been jurisdictional error on the part of an adjudicator in considering submissions which are duly made for two main reasons. Firstly, where respondents are concerned, s 20(2B) of the Act provides that unless a matter is raised by way of a payment schedule it cannot be raised subsequently in the adjudication process and secondly, specific submissions might not be dealt with in the terms of the adjudication determination. The adjudication is required to be given in writing and the adjudicator is required to give reasons. Sometimes complaints are of real substance because there are clear matters that have been raised that have not been dealt with by the adjudicator, but other times this is not as clear. It is a more significant matter where an adjudicator proceeds

to determine a matter on a basis that neither party has advanced or been given an opportunity to make submissions about. Where the adjudicator has a thought which informs their decision, they are duty-bound to give the parties the opportunity to make submissions about that matter and if they do not then it is often the case that they will fall into jurisdictional error. It can also be argued that an adjudicator is biased, but there are very few cases on which that allegation has been raised. Mr Hicks notes that it would be a very rare case where it could be argued that an adjudicator is biased by reference to an earlier determination, however it might be argued that an adjudicator is biased by reference to an earlier commercial relationship which has not been disclosed to the parties, for example, if the adjudicator acted as a solicitor for one of the parties in a previous matter.

16. The question of jurisdictional error is often determined by reference to the High Court decision in *Craig v South Australia* [1995] HCA 58; 184 CLR 163 concerning the obligation of someone exercising jurisdiction to do so having regard to the proper exercise of power and to consider all of the relevant matters as specified by the Act. It should be noted that it is within the power of an adjudicator to determine matters incorrectly having regard to the construction contract or other matters. Mr Hicks notes that, having regard to the short time frame of 10 days that an adjudicator is given to make their decision and the large volumes of material adjudicators are often faced with, it is not unusual that errors will be made along the way. The question of whether considering an irrelevant matter or wrongly considering a matter that is required to be addressed affects jurisdiction is usually a fairly narrow one and it would need to be identified that the consideration of the matter was indeed so removed from what the adjudicator was bound to consider having regard to the provisions of the Act that it did affect their exercise of jurisdiction to the extent that what had been done was not a proper exercise of statutory function.

#### Reference Date

17. The reference date is the date on and from which a party may be entitled to a progress payment. Section 8 of the Act specifies the reference date and it is the basis upon which the importance of the reference date arises.

#### **SECTION 8:**

##### ***Rights to progress payments***

- (1) *On and from each reference date under a construction contract, a person:*
  - (a) *who has undertaken to carry out construction work under the contract, or*
  - (b) *who has undertaken to supply related goods and services under the contract,**is entitled to a progress payment.*
- (2) *In this section, "reference date", in relation to a construction contract, means:*

- (a) *a date determined by or in accordance with the terms of the contract as the date on which a claim for a progress payment may be made in relation to work carried out or undertaken to be carried out (or related goods and services supplied or undertaken to be supplied) under the contract, or*
- (b) *if the contract makes no express provision with respect to the matter-the last day of the named month in which the construction work was first carried out (or the related goods and services were first supplied) under the contract and the last day of each subsequent named month.*

18. The reference date is determined either pursuant to the terms of the construction contract where the reference date may be identified as a particular date or by reference to the completion of certain obligations or milestones in the construction contract. If the construction contract does not specify the reference date by a calendar-based or activity-based date, the Act itself provides that the relevant reference date is the last date of each month in which work has been performed.

*Veer Build Pty Limited v TCA Electrical and Communication Pty Ltd [2015] NSWSC 864*

19. In the case of *Veer Build*, there were issues between the parties as to whether certain documents were in fact valid payment claims having regard to the history of communications between the parties. Towards the end of the project there were a series of dealings between the parties whereby a claim document was submitted but later rejected or sought to be withdrawn, then redrafted and submitted for consideration, being the subject of certain communications and correspondence, and then finally submitted in a particular form on a certain date. The sequence of events was such that most of the work was done in or about October 2014. There was then some further work done in November 2014 and also in December 2014. The issues which arose were related to the performance of most of the works by October 2014 and whether there was a reference date that had been used as at October 2014 or whether it was open and available to be used by the subsequent documents that were issued.
20. It was held in the case of *Veer Build* that since the initial claim was submitted but then withdrawn by agreement, the October 2014 reference date remained available to support any subsequent payment claim. What occurred throughout November was a series of communications where drafts were submitted for consideration and reasonable commercial endeavours were exercised on both sides to try to reach an agreement as to the amount of the progress payment to which the contractor was entitled. Those processes were finally concluded by about December 2014. On the 1<sup>st</sup> of December 2014, although no final agreement had actually been reached, a claim was submitted by the claimant to the respondent. The claimant sought to argue that that claim was related to the reference date

of October 31 2014 which had gone unused as a result of the withdrawal of the earlier payment claim. The respondent argued that if the 31<sup>st</sup> October reference date remained unused then it was left unused and the December 1 2014 claim in fact utilised the reference date of 30 November 2014 even though on its face the claim related to work that was undertaken in October 2014. The judge agreed with the respondent's characterisation.

21. Subsequently, the December 1 2014 payment claim was not paid and on the 7<sup>th</sup> of January 2015 the claimant issued another payment claim which was in substantially the same terms as the earlier payment claim. The respondent argued that because of the issue of the claim on the 1<sup>st</sup> of December 2014 which utilised the reference date of 30 November 2014 there was no available reference date for the payment claim of the 7<sup>th</sup> of January 2015 because that claim largely replicated the earlier works which were unpaid. However, a small amount of work had in fact been done in December 2014, for which no claim was made. The respondent argued that because no claim was made for that work, no reference date arose by reference to that work. The judge disagreed and found that even though no claim was made for the work, that was a matter for which the claimant could choose whether or not to pursue, but having performed work in December 2014, another reference date arose on the 31<sup>st</sup> of December 2014 and that reference date was sufficient to support the payment claim made in January 2015. The matter proceeded to adjudication where the adjudicator largely upheld the claim and required the claimant to be paid by way of a progress payment.
22. The lessons to be learnt from this case are that whilst it is always important to try to reach a commercial resolution of claims with respect to the security of payment and otherwise, it is also very important to bear in mind that reference dates, if they are not specifically provided for in the construction contract, can be lost or exhausted and that if claims are not submitted in accordance with the provisions of the Act, inadvertently one might find themselves in the position of having lost the benefit of a claim and reference date because of the doubtless best endeavours to try to reach some agreement. The overarching lesson that must be borne in mind for the Act is that the time frames are strict and they have effect whether or not there is intent or otherwise. Thus, it is always important to note the operation and effect of the time frames, particularly when one is engaged in commercial negotiations.

*Lewence Construction Pty Ltd v Southern Han Breakfast Point Pty Ltd [2015] NSWCA 288*

23. In the case of *Lewence Construction*, the parties had entered into a construction contract and had fallen into a significant dispute which was so extensive that Southern Han had issued notices under the terms of the construction contract and taken the works out of the hands of Lewence Construction. Lewence Construction responded by saying those notices were invalid and constituted repudiation. After the notices had been issued, a payment claim was submitted by Lewence Construction for works performed but Southern Han rejected the payment claim and asserted that there was no available reference date for it because of the



circumstances in which the construction contract had come to an end. The matter went to an adjudication and the adjudicator found in favour of Lewence Construction.

24. The matter then proceeded to the NSW Supreme Court where Ball J considered the question of whether a reference date was a jurisdictional element in respect to the payment claim process, the right to an adjudication determination and the enforcement of any determination that arose by reference to that process. His Honour found that the reference date was an essential element and that s 8 of the Act necessitated there being a reference date in order for one to submit a valid payment claim.
25. The matter then went to the Court of Appeal and the Court of Appeal disagreed with Ball J, stating that s 13 did not require the existence of a reference date and, in particular, the wording of s 13 to the effect that a person who is or who claims to be entitled to a progress payment may submit a payment claim necessarily set out the only matters which were requisite for a valid payment claim to be submitted. While s 8 established the entitlement or basic object and statutory position, the process under Part 3 and s 13 of the Act was a separate matter and the adjudication process and the existence or otherwise of a reference date was something that an adjudication could deal with.
26. The most important lesson to take from this case is that, while jurisdictional issues may be thought to arise by reference to earlier parts of the Act like Part 2, the actual process or practice for the assessment is set out in Part 3 of the Act and one may have a valid claim or process which gives rise to the provisions of the Act in terms of entitlement and recovery of an interim progress payment even where it is contested that a reference date may or may not exist. It is important to note in that case that the object and scheme of the Act is twofold:
  1. To afford interim progress payments on account in favour of those who have undertaken construction work and
  2. To afford a swift mechanism for determining disputes about those matters.The court is very mindful of these two objects and it should involve itself as little as can be reasonably expected by reference to the terms and structure of the Act in contested issues about determination and the entitlement for interim progress payments.

#### Advice when Drafting Construction Contracts

27. The principle areas where a construction contract informs the provisions of the Act is in identification and definition of a reference date and the assessment of the value of a payment claim. Where those matters are the subject of express provisions of the construction contract, the Act incorporates the construction contract as between the parties as determinative of those matters. This gives the parties control in terms of how the adjudication process is to be undertaken, firstly by reference to the reference date and secondly by identifying what is to be assessed when addressing the quantum of the claim, for example, whether defects or liquidated damages will be taken into account. Where the construction

contract is silent about those matters, then the Act will provide its own position in terms of a reference date by identifying the last date of each month in which construction work was performed and examining the question of quantum by having regard to ss 9 and 10 of the Act.

#### Advice when a Dispute Arises

28. The main areas that need to be addressed when there is a dispute on a construction project, whether relating to the Act or not, are how the Act is going to affect the dispute and what obligations may arise pursuant to the Act. It should be noted that the Act does not determine the substantive rights and entitlements between the parties. The parties are still entitled to exercise their substantive rights under the terms of the contract or the common law by reference to the conduct of either party and, indeed, they may be entitled to recover by way of restitution monies paid or over paid pursuant to an adjudication under the Act.
29. Where claims are being made or payment schedules are being issued, the principal issue is to concentrate on the question of time frames and what has to be done, because the failure to meet a particular time frame or the failure to issue a notice as is required by the Act can have dire and final consequences in terms of the obligations that arise. Principally, if a payment schedule is not issued in answer to a payment claim within the specified time period, then that immediately gives rise to a statutory debt that can be enforced in any court of competent jurisdiction. Thus, it is essential when matters might become contested in terms of the alleged entitlements that those time frames are addressed and kept in mind.
30. It should also be clearly recalled that the Act is concerned with interim progress payments for works pursuant to a construction contract and it is not a mechanism by which one can claim damages for breach of contract. If one wishes to make an assertion of entitlement, for example for delay costs, it has to be shown that there is an entitlement to receive delay costs under the terms of the construction contract. Any claim which is founded simply on a term which has been breached when submitted pursuant to a payment claim should be rejected because the Act does not allow the recovery of damages.

#### Contracting out of the Act

31. Section 34(2) of the Act provides that it is not possible to contract out of the Act.

#### **SECTION 34:**

##### ***No contracting out***

- (1) *The provisions of this Act have effect despite any provision to the contrary in any contract.*
- (2) *A provision of any agreement (whether in writing or not):*

- (a) *under which the operation of this Act is, or is purported to be, excluded, modified or restricted (or that has the effect of excluding, modifying or restricting the operation of this Act), or*
  - (b) *that may reasonably be construed as an attempt to deter a person from taking action under this Act,*
- is void.*

32. Section 34 provides very strong protection for the processes and procedures which are set out for the purposes of obtaining a progress payment or at least seeking to make a claim for a progress payment. If any contract or principal was to refuse to make payment by reference to either a payment claim which was not answered by a payment schedule or an adjudication determination where such a determination had been issued, would be faced with action in a court of competent jurisdiction. It would be impossible in those circumstances, other than by challenging the adjudication decision itself or by alleging that the payment claim is somehow invalid whether by reference to a prohibition or otherwise, to resist judgment being entered and for the weight of the rights which exist for the enforcement of judgment to then be deployed for the purposes of recovering those monies, including garnishee orders and levies on property.

### Dangers

33. There is always a danger of being drawn into expensive litigation, particularly when dealing with recalcitrant or obstinate respondents. It is not uncommon for a respondent to assert that the claimant is not entitled to the payment because the works are defective. If that is the case and the cost of remedying defective works is at least in the mind of the respondent not adequately accounted for in the adjudication determination, it can be the case that the respondent is dissatisfied with having to pay the amount to the claimant because it feels that the claimant has received more money than it is entitled to having regard to the quality of the work performed. Consequently, that respondent may take action against the claimant by reference to those defects in order to recover the monies that have been paid on account by reference to the provisions of the Act and a claim of restitution. Mr Hicks notes that these risks always exist with litigation and contract disputes and should be weighed accordingly.

## **BIOGRAPHY**

### Frank Hicks

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Frank Hicks practises primarily in technology and construction disputes concerning large residential, commercial, industrial and infrastructure projects. He has been published in the Building and Construction Law Journal and, in 2006, updated and edited the Halsbury's Laws of Australia Building and Construction title. In September 2011, he presented an assessment of the law and risks associated with Coal Seam Gas exploration and extraction (fracking) for the NSW Claims Discussion Group, an insurance industry association.

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*Veer Build Pty Limited v TCA Electrical and Communication Pty Ltd* [2015] NSWSC 864

*Lewence Construction Pty Ltd v Southern Han Breakfast Point Pty Ltd* [2015] NSWCA 288

### Legislation

*Building and Construction Industry Security of Payment Act 1999* (NSW)

*Competition and Consumer Act 2010* (Cth) Schedule 2 - The Australian Consumer Law

### Other

Morris lemma, New South Wales, Legislative Assembly, Parliamentary Debates (Hansard), 8 September 1999, at 103