SECURITY OF PAYMENT ACT 1999 (NSW) —A REMINDER OF ITS CONSEQUENCES

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The recent decision of the Supreme Court of New South Wales in *Walter Construction Group Ltd v CPL (Surry Hills) Pty Ltd* [2003] NSWSC 266 has raised awareness about the *Building and Construction Industry Security of Payment Act 1999* (NSW) ('the Act').

In that case, Justice Nicholas held that Walter, the contractor, was entitled to summary judgment of $13,962,904 against CPL, the principal, because CPL had failed to provide a payment schedule to Walter in reply to Walter's payment claim made under the Act.

WHY IS THE DECISION SIGNIFICANT?

Decisions like the *Walter* decision are assisting participants in the construction industry to realise that the Act is creating a more level playing field in situations where payment is in dispute, and has been helpful in clarifying aspects of the Act's interpretation.

The decision demonstrates the consequences of failing to comply with the provisions of the Act, and has prompted much legal and construction industry commentary in relation to the Act's scope and ramifications.

Certifiers, principals, contractors and consultants are on notice that if they intend to withhold money or reject progress claims, they need to be diligent in their administration of the requirements of the Act.

It is important to note that Walter's payment claim was made prior to the amendments to the Act, namely the *Building and Construction Industry Security of Payment Amendment Act 2002* (NSW), which commenced on 3 March 2003. Those amendments further strengthen the means and entitlements to recover unpaid amounts claimed under the Act.

BACKGROUND

CPL was a special purpose vehicle which owned a property at Glebe Point. Walter agreed to design and construct 46 residential apartments on the property for CPL. The contract incorporated an amended AS4300-1995.

In December 2002, Walter submitted a progress claim under the contract to the Superintendent in the amount of $14,915,255. On the same date Walter separately served a payment claim under the Act on CPL, as the party liable to make payment, for the same amount.

While the Superintendent issued a progress certificate under the contract assessing Walter's progress claim to be $952,351, CPL did not issue a payment schedule under the Act. The Superintendent's certificate did not meet the requirements of a payment schedule under the Act and in any case was not provided within the required ten business days after the payment claim was served.

Walter subsequently suspended the carrying out of works in reliance upon sections 15(2)(b) and 27 of the Act. Walter also commenced proceedings in the Supreme Court and immediately applied for summary judgment of the unpaid portion of the amount claimed, namely $13,962,904, as a debt due pursuant to section 15(2) of the Act.

CPL contended that the payment claim was not a valid claim within the meaning of section 13 of the Act on four bases, namely that:

a) Walter had submitted its claim prematurely under the contract and therefore it was not entitled to serve a payment claim under the Act;

b) Walter was not entitled to serve a payment claim, pursuant to section 13(1) of the Act, until after it was 'entitled to a progress payment' under the contract and that such entitlement did not arise until the progress payment was due and payable under the contract;

c) Walter's payment claim included items that did not relate to 'construction work' or 'related goods and services' as defined in sections 5 and 6 of the Act as it claimed for things other than physical construction work; and

d) pursuant to section 7(2)(c) of the Act, the Act did not apply to the contract, being a lump sum contract, because the consideration payable is calculated otherwise than by reference to the value of the works.

CPL also brought a cross claim against Walter. The basis of the cross claim was that Walter intended to mislead or deceive CPL by failing to make clear that the claim was made under the Act.

WAS THE CLAIM PREMATURE?

The contract provided that progress claims were to be submitted on the 28th day of each month. Walter served its December progress claim (and its payment claim under the Act) on 20 December 2002.

CPL led evidence, which unsurprisingly was not challenged by Walter, that the parties had agreed that Walter could lodge its progress claim for December 2002 prior to Christmas. That the parties to a contract may agree on the date on which a progress claim can be made was recognised by Ipp J in *Brewarrina Shire Council v Beckhaus Civic Pty Ltd* [2003] NSWCA 4 where he said at para 53:

As the contract was entered into on 3 October 2001, it seems that the first claim for payment was made prematurely. It may be that the parties, by their conduct, accepted that claims for payment should be made at times different to the times specified in cl 42.1, or that the monthly periods were to be calculated in a way that differed from that required by the contract. But there was not evidence to this effect and this does not appear to have been an issue before Macready AJ.

Justice Nicholas found that the parties had agreed that the December 2002 progress claim could be submitted earlier and therefore held the payment claim under the Act was not premature.

WAS WALTER 'ENTITLED TO A PROGRESS PAYMENT'?

Section 13(1) of the Act (prior to the amendments to the Act) provided that a party who is 'entitled to a progress payment under a construction contract' may serve a payment claim under the Act. CPL contended that section 13(1) of the Act meant that Walter must first be entitled to payment under the contract before it was entitled to serve a payment claim under the Act. On CPL's view, Walter would not be entitled to serve a payment claim under the Act until its progress claim had been assessed by the Superintendent or the period for payment under the contract had lapsed.

Macready AJ in *Beckhaus Civic Pty Ltd v Brewarrina Shire Council* (2002) NSWSC 960 considered the same submission that unless a progress payment submitted under a contract is due and payable under the contract, then there is no statutory entitlement to serve a claim under the Act. Macready AJ considered that reference to entitlement in section 13(1) of the Act must be reference to the statutory entitlement (created in the previous sections) not the contractual entitlement. In rejecting the submission His Honour stated 'there is no reason why he [the claimant] cannot make the statutory claim at the same time as his contractual claim' (at para 61).

Justice Nicholas agreed with the analysis of Macready AJ and noted that it was consistent with the opinion of Heydon JA (as he then was) in *Fyntray Constructions Pty Ltd v Macind Drainage and Hydraulic Services Pty Ltd* (2002) NSWCA 238 at para 51. His Honour held that, it being agreed that the date for making a claim for December was 20 December 2002, Walter was entitled to a progress payment within the meaning of section 13(1) of the Act and was therefore entitled to serve a payment claim under the Act on that date. The decision makes clear that it is not necessary to establish an entitlement to payment under the contract to make a claim under the Act.

Walter put forward an alternative submission that the payment claim was not invalid if submitted before time under the contract by reason of clause 42.1 of the contract. That provision relevantly states:

If the Contractor submits a payment claim before the time for lodgement of that payment claim, such early lodgement shall not require the Superintendent to issue the payment certificate in respect of that payment claim earlier than would have been the case had the Contractor submitted the payment claim in accordance with the Contract.

Accordingly, Walter argued that where the contract allows for early lodgement of a progress claim, the validity of a claim under the Act made prior to the stated date in the contract will be unaffected.

Justice Nicholas however found that a statutory entitlement to make a claim under the Act was to be calculated by having regard to the reference date as defined in section 8(2)(a)(i) of the Act and held that, but for the agreement to change the date to 20 December 2002, Walter was not entitled to make a claim under the Act on that date, notwithstanding that the contract allowed for early lodgement of a progress claim under the contract.

Justice Nicholas also commented that it is irrelevant that an item which was a component of the payment claim was disputed. The decision makes clear that payment claims are still valid under the Act even if they include items which may be disputed or if the entitlement is yet to be established under the contract.

DID THE CLAIM IDENTIFY THE CONSTRUCTION WORK (OR RELATED GOODS AND SERVICES)?

The contract provided that Walter could claim delay or disruption costs. Under the contract however Walter was not entitled to payment of such costs unless it had been granted an extension of time. The Superintendent under the contract did not grant Walter extensions of time. Notwithstanding, Walter included in its payment claim a consolidated claim for extensions of time previously made, a 'Further Entitlements claim' related to delay or disruption costs under the contract and a 'Special Measures claim'.

Section 13(2)(a) of the Act requires that a payment claim must identify the construction work (or related goods and services). CPL argued that the above items claimed did not relate to 'construction work' or 'related goods and services', as defined in sections 5 and 6 respectively, and therefore could not constitute a claim under the Act.

Justice Nicholas commented that CPL's argument misconceived the requirements of the Act and that the payment claim adequately identified the work (or related goods and services) to which the payment claim related. His Honour held therefore that Walter's payment claim was valid under the Act.

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The Court was of the view that if CPL took exception to the matters claimed in the payment claim then it had the opportunity to dispute the inclusion of such items in the payment claim and that the time for raising such argument was in a payment schedule.

DOES THE ACT APPLY TO LUMP SUM CONTRACTS?

Section 7(2)(c) of the Act provides that the Act does not apply to a contract under which it is agreed that the consideration payable for construction work carried out is to be calculated otherwise than by reference to the value of the work carried out or the value of the goods and services supplied.

Philip Davenport in *Adjudication in the NSW Construction Industry* said in relation to section 7(2)(c) of the Act that:

This exemption is particularly relevant to what are called BOOT and BOT schemes. They are contracts where the contractor carries out work in return for a lease or the right to operate the facility for a period. Examples are toll roads, the Sydney Harbour Tunnel, private prisons and privately run water treatments plants where the contractor's remuneration is based upon the output of the plant.

He cites other examples of the exemption in section 7(2)(c) of the Act as a lease agreement whereby the landlord or tenant agrees to carry out painting or repairs or to complete a fit out of premises, an agreement whereby an advertiser constructs a sign on a building and pays the owner for the right to do so and a contract for sale where the vendor agrees to complete some work or install some fitting either before or after settlement.

CPL contended that the Act did not apply to a lump sum contract pursuant to section 7(2)(c) of the Act, because the consideration payable was calculated otherwise than by reference to the value of the works. Justice Nicholas rejected this argument and found that the lump sum agreed upon was

calculated by reference to the value of the work undertaken and therefore fell outside the exclusion in section 7(2)(c) of the Act.

MISLEADING AND DECEPTIVE CONDUCT

The Act requires the payment claim to state that it is made under the Act and must be clear on the face of the document that it purports to be a payment claim under the Act. The Act does not specify the location of the words, size of print or that it should be brought to the attention of the recipient of the claim.[1]

CPL contended by way of cross claim, as a further basis of opposing an order for summary judgment, that the payment claim was ambiguous or so lacking in clarity as to its true nature and effect that by serving the payment claim in the form in which it was, Walter had engaged in conduct which was misleading and deceptive in contravention of section 52 of the *Trade Practices Act*.

Justice Nicholas quickly dispensed with CPL's argument and found that CPL should have had no difficulty in identifying the payment claim and in realising that it constituted a claim made under the Act.

DOES THE ACT WORK?

The Act is intended to provide a fair means of ensuring timely interim payment for work done under a construction contract.

Some industry commentators have suggested that the Act was never intended to apply to such large sums of money as was involved in this case. Arguably it is even more important where large sums of money are involved. After all, as the Court itself has acknowledged 'cash flow is the "life blood" of the contract'.[2]

In the words of Phil Armessen, Manager of Policy at the NSW Department of Commerce:

This Act is all about getting cash flow in the industry. Disputes can drag on. In the meantime the Act provides a fair mechanism whereby a payment can be made to the person who has done the work.[3]

The *Walter* case demonstrates that the Act is powerful and provides an effective mechanism to assist with cash flow to contractors in the industry.

REFERENCES

1. *Jemzone Pty Ltd v Trytan Pty Ltd* (2002) NSWSC 395 per Austin at [46].

2. The purpose of progress payments in construction contracts was explained by White J in *Egan v State Transport Authority* at p.537. His Honour said:

Payments have long been recognised as being merely agreed instalments in reduction of the lump sum price, made on that account to keep the building contractor on the job. The purpose of instalment payments is not to pay for the materials in the sense that a purchaser of land or of specific goods pays money for or towards the purchase price. Instalment payments are made in contracts like this as a practical measure to enable the contractor to keep working under the contract; they are made also in reduction of the lump sum contract price. Such payments have been described as the 'life blood' of the contract.

3. *Building Sciences Forum* 25 June 2003.