

SECURITY OF PAYMENT IN NSW—SIGNIFICANT CHANGES

Philip Davenport
Solicitor

The *Building and Construction Industry Security of Payment Amendment Act 2002* (NSW) to commence on a date to be proclaimed, will have most important implications for all who have carried out construction work or who have the supplied goods or services in relation to construction work and have not been paid in full. The amendments affect existing contracts as well as future contracts and, even if litigation has been commenced to recover an amount due for or in relation to a construction work, the amendments could provide a most important additional remedy.

The ten most important changes are:

1. The option to lodge security instead of paying the adjudicated amount has been repealed.
2. Procedures for obtaining judgment for the statutory debt have been enhanced.
3. A minimum rate of interest applies to all progress payments claimed under the Act.
4. All applications for adjudication must be lodged with an authorised nominating authority.
5. Authorised nominating authorities will be able to charge for their services;
6. Adjudicators will have a discretion to decide which party pays what proportion of the fees and expenses paid to an authorized nominating authority and the adjudicator.
7. There is provision for an optional adjudication.
8. The times for lodging an adjudication application and for paying the adjudicated amount have been extended.
9. The number of payment claims which can be made under the Act is limited.
10. A claimant has a lien for unpaid amounts.

The amendments do not apply to a payment claim made under the Act before the amending Act commences. Usually a claimant will be able to obtain the benefit of the amendments to the Act by lodging a payment claim or a further payment claim after the amending Act commences. For this reason, claimants who have finished or are about to finish a project should consider the possible benefits of postponing the making of the final progress claim under the Act until the amendments commence. *Beckhaus Civil Pty Ltd v The Council of the Shire of Brewarrina* NSWSC 55025 of 2002 provides valuable guidance on making a payment claim under the Act in respect of previously unpaid progress claims. The amended Act specifically provides that a payment claim under the Act can include a claim for the final payment [section 4(c)]. Claims against a person who resides or proposes to reside in the premises the subject of the construction work are still outside the scope of the Act [section 7(2)(b)].

The amended Act requires the respondent to pay the claimant the adjudicated amount. The option of lodging a bank guarantee or paying the adjudicated amount into a designated trust account has been repealed. This makes use of the Act much more attractive to claimants. The amended Act has provision for obtaining an expedited judgment without the need to issue a summons. An adjudicator's determination is more easily enforced than an arbitrator's award. It would be a rare instance where a party who has not been paid for construction work related goods or services would not be best advised to pursue an adjudication under the Act before or concurrently with litigation to recover payment. The fact that litigation has already commenced is no bar to pursuing proceedings through the Act and

obtaining a judgment for the debt due under the Act.

The amount paid pursuant to the judgment under the Act is payment on account and, in other proceedings, an award of a court or arbitrator can require repayment of the judgment debt or any portion thereof. However, a payment on account can be very valuable to the claimant and might even be necessary to enable the claimant to finance the other litigation. Sometimes, the reason why a respondent fails to pay is because the respondent is using the claimant's money to finance the respondent's defence or to preserve the respondent from bankruptcy. If, before finalisation of arbitration or litigation, the respondent has to pay the whole or a substantial part of the claim, the respondent may be unable to continue the arbitration or litigation. At least, the incentive to commence or continue arbitration or litigation may be reduced.

Litigation or arbitration in respect of construction claims tends to be complicated and to take a long time between commencement and judgment. A claimant who has not been advised of the concurrent right under the Act to obtain a payment on account pending the final resolution of the dispute may be justifiably concerned. Imagine a subcontractor who claims to be owed \$35,000 for work done. The subcontractor can sue in the Local Court and, after some considerable time (maybe 12 months or two years) and a hearing of cross claims and defences such as that work was defective, the subcontractor may get judgment for the \$35,000. The subcontractor's legal costs may even exceed \$35,000 but usually not all those costs are recoverable. If the construction contract includes an arbitration clause, the subcontractor will probably first have to go to arbitration. The legal and arbitration costs are then likely to be considerably more.

Before, concurrently with or instead of the Local Court proceedings the subcontractor can, by using the Act, obtain a determination by an adjudicator. Because of the strict time limits under the Act, this determination can be obtained in approximately four or five weeks after the payment claim under the Act is made. If the adjudicator determines that the subcontractor is entitled to the \$35,000, the adjudicator can determine that the respondent must pay the costs of the adjudication. In that event, the adjudication may cost the subcontractor nothing. Otherwise, the costs of adjudication will usually be shared equally by the parties. Then the cost to the subcontractor of the adjudicator's fees and the fees of the authorized nominating authority are likely to be approximately \$1,000 to \$2,000. The subcontractor can immediately apply to the Local Court for judgment for the adjudicated amount. To that application for judgment, the respondent cannot raise a cross claim or defence relating to matters arising under the contract. Moreover, if the respondent wishes to challenge the judgment the respondent must first pay into court the amount of the judgment.

Once the subcontractor has obtained judgment under the Act for \$35,000, the respondent must pay the \$35,000 even though concurrent proceedings in arbitration or the Local Court have not reached finality. It will be the respondent who is out of pocket \$35,000 while the litigation drags on. Having paid out \$35,000 the respondent may be less keen to pursue the other proceedings. If the claimant first recovers the \$35,000 under the Act, the claimant will probably not wish to instigate arbitration or litigation. It would then be up to the respondent to sue to recover the \$35,000.

The amending Act facilitates the obtaining of judgment for the statutory debt under the Act. Where the statutory debt arises under section 15 (because the respondent has not within the prescribed 10 business days served upon the claimant a payment schedule and has not paid the full amount claimed) or under section 16 (because the respondent has failed to pay the scheduled amount), the claimant can sue in a court for the statutory debt but now the Act will bar the respondent from lodging any cross claim or any defence in relation to matters arising under the contract. This should make it much easier for the claimant to obtain summary judgment.

If the claimant proceeds to adjudication and the adjudicator decides that the claimant is entitled to a progress payment then the method of obtaining judgment is much easier and faster. The claimant only has to obtain an adjudication certificate from the authorised nominating authority which nominated the adjudicator and to file that certificate, and an affidavit as to the outstanding amount, in a court of appropriate jurisdiction. The claimant is then entitled to judgment forthwith without the need for a summons or an appearance before a magistrate or judge. The adjudication certificate can also certify the interest, fees and expenses to which the claimant is entitled and the judgement will include those amounts.

The concept of a judgment for and payment on account of the amount in dispute before the final determination of the issues between the parties and final judgment is most unusual. For this reason, claimants have had some difficulty persuading courts to grant summary judgment for the debt due under the Act and to strike out defences in relation to matters arising under the contract and cross

claims. To overcome this problem the amendments provide for summary judgment without a hearing. As well as being unable to raise any defence in relation to matters arising under the contract or a cross claim, the respondent who applies to have the judgment set aside is prohibited from challenging the determination of the adjudicator and must pay into court as security the unpaid portion of the adjudicated amount. This will make it very difficult for a respondent to use litigation to delay or withhold payment. The unfair advantage which a respondent has traditionally had over a claimant has been overcome. Now the playing field is level and the adjudicator is umpire. Either party can try to have the umpire's decision overturned by a court or, if the contract permits or the parties agree, by an arbitrator. But pending the final decision, if any, the respondent must abide by the umpire's decision.

If a respondent fails to serve upon a claimant a payment schedule within time and to pay the adjudicated amount or serves a payment schedule within time but fails to pay the scheduled amount, the amendments give the claimant the option of issuing a summons for the debt due or initiating an adjudication. If the claimant exercises the adjudication option and the respondent has not served a payment schedule within time, the claimant must give the respondent another opportunity to serve a payment schedule [section 17(2)]. For exercise of the option there are time limits which cannot be extended. The advantage of exercising the adjudication option is that judgment can be obtained without the need for a summons and the time allowed for a defence. There is also the advantage that the respondent who wants to challenge judgement based upon an adjudication must first lodge with

the court as security the amount of the judgment.

Henceforth payment claims under the Act must be lodged with an authorized nominating authority. The authority can charge a fee. However, the adjudicator can decide that the fee or portion must be paid by the respondent and the amount payable by the respondent can be included in the adjudication certificate and the judgment based upon the certificate. The parties can no longer agree upon and appoint their own adjudicator but there is nothing to stop a party or parties suggesting to the authorised nominating authority a person or persons who would be appropriate appointments. The authorized nominating authority can no longer be specified in the construction contract.

An adjudicator can withhold publishing the adjudication determination until the adjudicator has been paid [section 29(5)(a)]. In the past, when the parties were each liable to pay half the adjudicator's fee, the respondent would sometimes refuse to pay the respondent's share. This meant that to obtain the determination the claimant had to pay the respondent's share and endeavour to recover it. Now recovery has been made easier. The authorised nominating authority can include the amount in the adjudication certificate and it becomes part of the adjudicated amount and the judgment debt [section 24(5)].

The amendments provide for interest on unpaid progress payments at the rate under the contract or the rate applicable to unpaid judgments of the Supreme Court, whichever is the greater. The amendments also entitle the claimant to a lien in respect of the unpaid amount. The lien is over any unfixed plant or materials supplied by the claimant for the use of the respondent in connection with the carrying out of the construction

work. The lien does not give the claimant priority over a third party's interest in the unfixed plant or materials.

Some lawyers and courts have had difficulty with the concept that a progress claim can be made in respect of a contract which provides for a single payment on completion and in respect of the final payment under a contract. To resolve this problem the Act now specifically provides that a progress claim can be made in respect of a single or one off payment, milestone payments and the final payment [see definition of 'progress payment' in section 4].

The amendments not only enhance the rights of claimants. They also provide important additional protections for respondents. For example, limits have been placed upon the number of payment claims which can be made under the Act. Only one payment claim can be made in respect of each reference date [section 13(5)] and a payment claim cannot be made after the period prescribed in the contract or 12 months after the work was last carried out or the goods or services were last supplied, whichever is the later [section 13(4)] but a payment claim can include amounts previously claimed [section 13(6)]. Where a reference date is not prescribed in the contract, it is now the last day of each month [section 8(2)].

The new section 22(4) is designed to stop 'adjudicator shopping'. This is where a claimant dissatisfied with the value given by one adjudicator to construction work or related goods or services seeks, to have a subsequent adjudicator give the work, goods or services a greater value. Henceforth, if a previous adjudicator has determined the value of work, goods or services, in any subsequent adjudication, the adjudicator must give the work, goods or services the same value as the previous adjudicator

determined unless the claimant or respondent satisfies the adjudicator that the value has changed since the previous determination.

The *Contractor's Debts Act 1997* is amended to provide that if an adjudication certificate has been filed as a judgment debt, the registrar of the court can issue a debt certificate under the *Contractor's Debts Act 1997* [schedule 2]. This can be a quick and efficient method of obtaining payment of the judgment debt from the principal who owes money to the judgment debtor in respect of the construction work.

A number of other amendments have been made. These and the amendments discussed have important implications for anyone drafting a contract for construction work or a contract for the supply of related goods or services. This includes contracts for architectural, engineering or surveying services. Particular care must be given to the dates for progress claims, the valuation of work for progress payments and the serving of payment schedules. Many standard form contracts have outdated provisions for progress certificates and ignore the fact that the once common progress certificate from an independent certifier is not the payment schedule required under the Act. The 'no contracting out' provisions of section 34 have been expanded to prohibit a contractual provision that may be construed as an attempt to deter a person from taking action under the Act. This is aimed at stopping the practice of some developers and head contractors of inserting contractual provisions aimed at deterring contractors and sub-contractors from making payments claims under the Act or instituting adjudications.

The NSW concept of rapid adjudication of a claim for payment on account is gaining favour in many jurisdictions. Victoria has

enacted legislation very similar to the NSW Act as it was before the amending Act. New Zealand has just introduced the concept in the *Construction Contracts Act 2002*. Queensland and Western Australia are actively considering legislation.

The implications for adjudicators will be the subject of a separate article by the author, updating *Adjudicators—Their Role and Functions under the Building and Construction Industry Security of Payment Act 1999 NSW* published in 1999 #68 ACLN pp6–24.