JOINT STANDING COMMITTEE ON SMALL BUSINESS

REPORT

SECURITY OF PAYMENT FOR THE NEW SOUTH WALES BUILDING INDUSTRY

4/51 **September 1998**

This report was prepared and published by:

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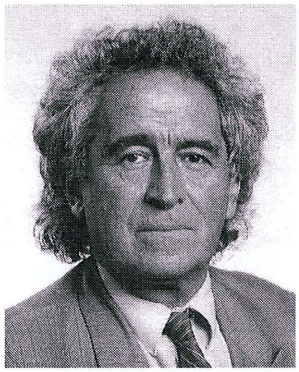

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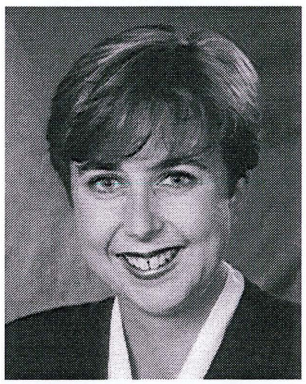

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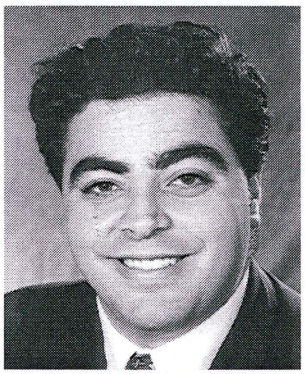

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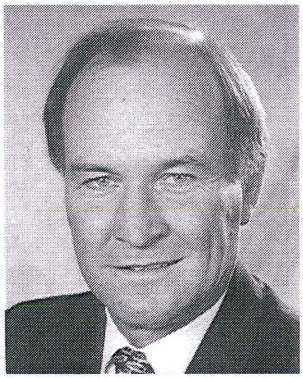

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Glossary

Adjudication	The proposed process by which disputes between parties are resolved.
Adjudication Order	An order given by an Adjudicator (within seven days of appointment).
Adjudicator	An accredited person appointed by the BRA to adjudicate a dispute.
Attachment Order	An order issued by a Court on application by a person claiming to be owed money (the claimant) that another person retain the sum of money nominated in the attachment order or be liable for its future payment. (Refer s.14 Contractors Debtors Act 1997)
BRIS	Building Registration Information System
BRA	Building Registration Authority
BR/LA	Building Registration/Licencing Authority (Superseded title used in Discussion Paper, now the BRA)
Building Entities	Entities engaged in the commercial, industrial or residential building and construction industry who will be required to register with BRA (includes contractors, subcontractors, project managers, owner-builders and certain owners and principals).
Client	Owner of property or a project giving rise to building work.
Complex Adjudication	The third tier in the proposed sessional structure of adjudication
Head Contractor	Contractor with a single contract with the Client for all building work on one site.
Intermediate Adjudication	The second tier in the proposed sessional structure of adjudication
MSPI	Mandatory Security of Payment Insurance
Notice of Intent to Revise Payment	A notice sent from the debtor to the creditor, after receipt by the debtor of the creditor's invoice, prior to the invoice being due and payable and within 7 days of receipt.
Notice Requiring Adjudication	A notice sent by the creditor to the debtor after receipt of a Notice of Intent to Revise Payment in the event that payment of an invoice is being withheld, delayed and/or is incomplete.

Notice to Suspend Work	A notice sent in any of 3 sets of circumstances: (1) from the creditor to the debtor: in the circumstances where the creditor has sent an invoice and no notification of Intent to Revise Payment has been received and there has been incomplete payment of the invoice by the debtor on or by the express or implied payment date. (2) from either the creditor or the debtor : in the circumstance where there is a failure to comply with an adjudicator's order; (3) from either the creditor or the debtor: if insolvency proceedings are commenced in relation to the other party.
Notice of Intent to Litigate	A notice sent by either party involved in a dispute following receipt of an order from an adjudicator.
Notification	Serving of a Notice
Registered Entities	Building entities registered with the proposed BRA
Principal	1) Owner of unincorporated contracting business 2) Representative of client
Standard Adjudication	The first tier in the proposed sessional structure of adjudication
The "Code"	Building Code of Conduct A Code which is proposed to be established under new legislation which would require all registered entities to utilise written contracts for building work. The Code is proposed to require contracts for building work include minimum standard contract terms governing notifications, adjudication and utilisation of designated trust accounts.
[sub.nn]	Refers to a numbered submission from the public

Foreword

Security of payment for subcontractors and suppliers in the building industry has long been a concern of Government and the industry. Over the past decade, there have been many reports written on security of payments and the state of the building industry in New South Wales. Yet the problem of security of payment remains.

The Joint Standing Committee on Small Business decided to investigate the issue following continued reports of subcontractor difficulties in securing payment when head contractors became insolvent and in receiving prompt payment for labour and materials supplied.

This Report contains the most far-reaching recommendations for reforms in the building industry since the Royal Commission into Productivity in the Building Industry in New South Wales in 1992.

These recommendations arose after a comprehensive process of consultation with all sectors of the industry. Based on the submissions received from professional bodies and associations representing the contractors and subcontractors in the industry the reform package has achieved a remarkable level of consensus.

This level of consensus was in stark contrast to the Committee's early experiences which focussed on a proposal put forward by the Construction Payments Group for legislation establishing a regime of cascading deemed trusts.

Despite extended consideration of the proposal, the Committee was of the opinion that deemed trusts did not have the level of support required for the successful reform of the payment culture in the building industry.

The Committee's Discussion Paper on Security of Payments released in August 1998, outlined a proposal which combined a number of regulatory and contractual reforms.

The key features of this proposal were a streamlining of existing dispute resolution processes in the building industry:

- to establish industry wide registration;
- to create a mandatory Building Code of Conduct; and
- to establish a mandatory Security of Payment insurance regime, which would be introduced after the other reforms had an opportunity to change industry behaviour.

Submissions from the industry groups and the public were extremely helpful in refining and fine tuning the Committee's proposals and led to a number of enhancements which have improved the equity and effectiveness of the reforms proposed.

The concerns expressed about the potential cost of the mandatory insurance regime have also been noted and resulted in the Committee identifying and recommending additional safeguards prior to any implementation.

During the course of the inquiry, the Committee held extensive consultations with

representatives from all sectors of the building industry. In addition, the Committee consulted with, and sought the advice of NSW Government Departments, financial institutions and the insurance industry.

The Committee has been assisted by many individuals and organisations whose input and contributions made this Report possible The Committee would like to place on record its appreciation for those efforts, which led to a better understanding of the issues and a clearer vision for the future.

The Committee would like to make particular mention of the following people:

Mr George Cepak (Director), Mr Chris Denney (Research Officer), Ms Susan Want (Research Officer) and Mr Bruce Gordon (Consultant to the Committee).

While all committee members were instrumental in the finalisation of this Report, special mention must be made of the contributions of Mr Joe Tripodi MP, Ms Reba Meagher MP, the Hon Joe Schipp MP and the Hon Mark Kersten MLC who devoted so much of their time to the sub-committee on this issue of Security of Payment.

The Hon Edward M Obeid OAM MLC
Chairman

Executive Summary

Legislative Provisions

The Report outlines that legislation be introduced to provide for the establishment of a Building Registration Authority (BRA) and a Building Code of Conduct (The Code). This registration requirement would apply to all contractors engaged in building activities as head contractors, sub contractors, trade contractors and in certain circumstances owners, principals and project managers, while the Code would apply to all registered entities which contract for commercial, industrial and residential building work.

The Report also states that there be a legislated requirement that all contracts for work on building projects be in writing and contain certain terms.

As part of the reforms, the Committee is of the opinion that the Contractors Debts Act 1997 be amended to provide a court with the power, additional to its current power to make an attachment order against a principal, to also make an attachment order against a defaulting contractor.

In the event of the implementation of such provisions as the BRA and the Code, the Committee believes that jurisdiction be conferred on the Commercial Tribunal or its successor bodies to hear prosecutions for breaches of the Code or appeals in relation to registration decisions made by the BRA.

To increase the number of parties who can access dispute resolution in the Small Claims Division of the Local Court, that the jurisdictional limit in the Small Claims Division of $3,000 be increased to $10,000.

Building Registration Authority (BRA)

The Committee proposes that the BRA be responsible for:

- registration of all commercial, industrial and residential building entities;
- prosecution of breaches of the Act and Code;
- monitoring compliance;
- accreditation of those private sector bodies which will nominate adjudicators;
- recording of adjudicator decisions;
- accreditation of impartial adjudicators.

It is anticipated that, after its establishment, the BRA be a self funding and revenue neutral agency, with registration fees set at levels which recoup the running costs of the organisation.

The Building Code of Conduct (The Code)

The Committee believes that a Mandatory Building Code of Conduct for registered entities be introduced which would require:

- that all contracts be written and contain certain features;
- that creditors notify debtors of intention to revise payment within a specified time;
- that the BRA be notified of disputes;
- that a prescribed dispute resolution process be adopted;
- that a designated trust account (DTA) be establish to keep disputed monies while the dispute is settled;
- that all parties abide by the adjudicators' decisions; and
- that all registered entities secure mandatory security of payment insurance when these requirements are proclaimed.

The Code would specify standard terms for payment, notification, dispute resolution and suspension of work in the event that these were omitted from the written contract.

The Code terms would apply equally to the registered entity and the other party to the contract if unregistered eg principal.

Standard Contract Terms

The Committee is of the opinion that standard contract terms be adopted and include:

- a clear statement of scope of work to be performed;
- details of payment and notification terms;
- dispute resolution and adjudication provisions; and
- the right to suspend work in three specified circumstances.

The Committee also proposes that as part of the standard contract terms, the following clauses be precluded:

- 'pay if paid' and 'pay when paid' clauses; and
- 'contracting out of the provisions of the Code' contract clauses.

If either payment, notification, adjudication or suspension of work clauses are not specified in the written contract, the standard terms stipulated in the Code for any clause omitted will be applied to such contracts.

Contract variations will be subject to the same condition as the original contract unless there is a change specified in the variation and signed by both parties. Set-off claims are subject to the conditions of the contract and require notification in writing. They may trigger a dispute

in conjunction with a payment demand or on a stand alone basis.

Adjudication

The Committee believes that there is a requirement for an adjudication process to be established under the Building Code of Conduct.

As such, all contracts for building work or the supply of building materials or services specific to building related activity such as design, will require the inclusion of a mandatory clause specifying that either party to a contract involving a registered building entity may, after the exchange of notifications, refer a dispute to adjudication.

It is anticipated that legislation will provide for the appointment of impartial adjudicators by an appropriate private sector body. The adjudicator nominating body and the impartial adjudicator will both require accreditation with the BRA.

The role of the impartial adjudicator is to provide the dispute parties with an order within seven days of appointment.

The order is to be based on:

- information provided by either party about the dispute,
- conditions set out in the contract between the disputing parties, and
- any further material considered relevant to the resolution of the dispute.

When an adjudicator is unable to complete the resolution of the dispute within 7 days, the adjudicator is able to obtain an extension to the adjudication or to provide both parties with an interim order. This order is to include a specification of the amount of money to be placed in a DTA pending the resolution of the dispute and the date money is to be deposited.

An adjudicator may take into consideration a dispute at another point in the contract chain, where there is evidence that monies have been put into a DTA, in framing the order on the current matter provided that there is clear overlap of the Scope of Works.

An adjudicator's order can be enforced by registration of that order with a court of competent jurisdiction.

The costs of the adjudication will be born equally by the parties to the adjudication except in special circumstances.

Designated Trust Account

The Committee proposes that registered entities and any party contracting with a registered

entity will be required to establish a Designated Trust Account (DTA) in the circumstances where a dispute arises.

All monies in dispute are to be lodged into a Designated Trust Account (DTA) subject to:

- the monies being due and payable under the conditions of contract;
- the adjudicator specifying the amount to be paid or placed in trust in an order.

In the event that either party notifies their intent to litigate or proceed to utilise other dispute resolution clauses in the contract, all monies ordered for payment by the adjudicator are to be placed immediately into the DTA as a prerequisite to proceeding. The monies will remain in trust until the conclusion of the litigation or dispute resolution. Payments from the DTA will be made in accordance with the orders issued.

The Report outlines that appropriate unconditional undertakings in the form of bank guarantees or payment bonds may serve as substitutes for monies lodged into a DTA.

Mandatory Security of Payment Insurance

The Committee proposes that all registered entities be required to take out Mandatory Security of Payment Insurance (MSPI) to guarantee the payment of all parties who have a contract for building work on a site in the event of contractor insolvency. These parties would include subcontractors, material suppliers and other service providers. This will provide added assurance for continuity of payments to the employees of all organisations.

It is anticipated that under the reforms all unregistered entities or specialist suppliers be exempted from the requirement to effect MSPI unless some provision of the legislation requires them to become registered entities.

The Committee believes that it would be beneficial for the introduction of MSPI to be deferred for a period of twelve months pending the implementation of other reform measures recommended.

The Committee proposes that legislation for the introduction of MSPI be proclaimed after receipt by the Minister of a satisfactory assessment from a working party advising on the financial feasibility of the scheme.

That MSPI would then be phased in over a period of a further two years commencing with contracts exceeding $5 million. This contract limit would be reduced after 12 months to $1 million and then eliminated so that MSPI would apply to all contracts. The Committee also acknowledges that the working party advising the Minister should be free to recommend a further alternative for consideration.

Recommendations

General Recommendations

1. The Committee recommends that the Minister for Public Works and Services be responsible for the introduction of new or amended legislation providing for security of payment reforms proposed in this Report.

2. The Committee recommends that the Department of Public Works and Services be responsible for the implementation, administration and auspicing the legislation and overseeing any new agencies such as the Building Registration Authority (BRA).

3. The Committee recommends that a BRA be establish to operate as the coordinating body for the security of payment reforms outlined in this Report.

4. The Committee recommends that the BRA monitor industry behaviour and breaches of the Building Code of Conduct.

5. The Committee recommends that the Building Code of Conduct incorporate minimum standard contract terms covering payment, notification, dispute resolution and suspension of work which would operate as implied terms if they were not expressly contained in the written contract for building works.

Legislative Provisions

6. The Committee recommends that legislation be introduced to establish the BRA.

7. The Committee recommends that legislation be introduced to establish a mandatory Building Code of Conduct (the Code) governing payment and notification behaviour in the building industry.

8. The Committee recommends that the Contractors Debts Act 1997 be amended to include provision for an attachment order to be made against a defaulting contractor.

9. The Committee recommends that jurisdiction be conferred on the Commercial Tribunal or its successor bodies to hear prosecutions on breaches of the Code and appeals in relation to registration decisions made by the BRA.

10. The Committee recommends that the monetary jurisdictional limit of the Small Claims Division in the Local Court be increased from $3,000 to $10,000.

Building Registration Authority

11. The Committee recommends that the BRA be responsible for:

- registration of entities engaged in commercial, industrial and residential building work;
- prosecuting breaches of the legislation and Code;
- monitoring compliance; and
- accrediting dispute resolution bodies and adjudicators.

12. The Committee recommends that the BRA be responsible for processing all applications by building entities for registration and registration renewals.

13. The Committee recommends that all contractors and subcontractors (and in certain instances owners, principals and project managers) who are engaged in contracts in commercial and industrial building be required to register with the BRA.

14. The Committee recommends that all contractors who currently hold Residential Building Licences be automatically registered by the BRA.

15. The Committee recommends that a separate registration category for specialist suppliers be created.

16. The Committee recommends that the registration of specialist suppliers be optional for all suppliers, hirers, and professional service providers who supply materials or services which are utilised in the planning, design or construction of a building.

17. The Committee recommends that owners, principals, and project managers who assume the role of the head contractor in a relationship with subcontractor trades be required to register.

18. The Committee recommends that information relating to the performance of registered entities be available to the public.

19. The Committee recommends that the Department of Fair Trading Residential Building Licensing Database be utilised as the basis for the Building Registration Information System (BRIS).

Building Code of Conduct

20. The Committee recommends that a mandatory Building Code of Conduct for registered entities be introduced with the range of requirements already specified and standard implied terms of payment, notification, adjudication and suspension of work in the event these are not expressly contained in a written contract.

21. The Committee recommends that minimum standard contract terms outlined in the Code apply equally to the registered entity and any other party to the contract for building work if unregistered.

22. The Committee recommends that consistent breaches of the Code result in the suspension of a registered entities' registration.

23. The Committee recommends that the BRA have the power to suspend the registration of any registered entity associated with the principals, directors and operational managers of a registered entity under investigation, for a period of up to 60 days.

24. The Committee recommends that the BRA collate dispute data and breaches of the Code.

Standard Contract Requirements

25. The Committee recommends that all written building contracts include the following general terms:

- registered entity's registration number;
- detailed statement of scope of works to be performed;
- the work completion date;
- details of payment terms;
- details of notification terms;
- dispute resolution and/or adjudication provisions; and
- right to suspend work without penalty in three specified circumstances.

26. The Committee recommends that in relation to contracts for building work, legislation prohibit :

- 'pay if paid' and 'pay when paid' contract clauses ; and
- 'contracting out of the provisions of the Code' contract clauses.

27. The Committee recommends that in the event that a written contract for building work does not include minimum standard contractual terms, then the Code's terms for payment, notification, adjudication and suspension of work will be incorporated into the contract as implied terms.

28. The Committee recommends that a 14 day (from receipt of invoice) payment term, be required by the Code to operate as an implied term in the event that a written contract does not expressly stipulate payment terms.

29. The Committee recommends that a 7 day notification term, from the receipt of invoice or any subsequent notice, be required by the Code to be a non-excludable implied term in all written contracts for building work.

30. The Committee recommends that a 7 day adjudication term, from the date of Notice Requiring Adjudication be required by the Code to be a non-excludable implied term in all written contracts for building work.

31. The Committee recommends that any variations to a written building contract involving a registered entity :
    - be in writing; and
    - possess or refer to the basic terms and conditions of the original contract, unless these terms and conditions are expressly altered in the variation documentation.

32. The Committee recommends that if a registered entity enters into an unwritten contract for building work there should be no be no minimum standard implied terms applicable to such contract and hence no protection from the proposed reforms.

33. The Committee recommends that the Code require every written building contract incorporate the Code's suspension of work term as non excludable implied term.

34. The Committee recommends that the right to issue a notice of *Intent to Suspend Work* **without penalty** be required by the Code to be a non excludable implied term in every written building contract for building work in three circumstances:
    1. In the event that payment to a creditor has been withheld, delayed and/or is incomplete beyond the due date without prior *Notice of Intent to Revise Payment.*
    2. If either party fails to comply with an order issued by an adjudicator.
    3. If insolvency proceedings commence in relation to either party.

Adjudication

35. The Committee recommends that the BRA be responsible for the development and maintenance of an accredited network of appropriately qualified adjudicators and accredited professional bodies and institutes.

36. The Committee recommends that the appointment of an adjudicator be subject to the following statutory requirements (which would operate as non-excludable implied terms in every written contract for building works covered by the Code) :

    - that the adjudicator be independent, accredited by the BRA and be appointed by a body which is accredited by the BRA for the nomination of adjudicators.
    - that the BRA be advised within 7 days of the notice of *Intent to Revise Payment.*
    - that the adjudicator provide an adjudication order within 7 days of being appointed.

37. The Committee recommends that an adjudicators order, if not appealed within 7 days be enforceable in a court of law.

38. The Committee recommends that the Code adopt a sessional structure of fees according to the complexity of the dispute. The sessional structure would be classified into 3 categories: standard, intermediate and complex.

39. The Committee recommends that adjudicators not be held liable in respect of anything done or omitted to be done during any part of the adjudication proceedings apart from liability for fraud.

40. The Committee recommends that legislative provisions be implemented which ensure that the adjudicator cannot be subpoenaed to provide evidence in any subsequent litigation or alternative dispute resolution process.

Designated Trust Account

41. The Committee recommends that a designated trust account be used for the lodgement of monies following an adjudication or the receipt of an attachment order.

42. The Committee recommends that in the event that either party notifies their intent to litigate or to use other dispute resolution clauses specify as stated in the contract, all monies ordered for payment by the adjudicator are to be placed into a designated trust account as a prerequisite to proceeding.

43. The Committee recommends that the use of unconditional undertakings, such as bank guarantees and insurance bonds, be allowed for the purpose of securing monies in dispute.

44. The Committee recommends that any registered entity required to deposit monies into a designated trust account also act as the trustee.

45. The Committee recommends that failure by a registered entity to deposit monies into a designated trust account as ordered, warrants the issuing of a demand by the BRA for a certification of solvency to be signed by the entities Principals and Chief Financial Officer on the first offence. Any subsequent breaches of this type could result in the BRA demanding an independent certification of solvency.

Mandatory Security of Payment Insurance

46. The Committee recommends that all registered entities who contract be required to take out mandatory security of payment insurance to ensure the payment of all parties who have a contract for building work on a site.

47. The Committee recommends that legislation for the introduction of mandatory security of payment insurance only be implemented after receipt by the Minister of a satisfactory

assessment from an industry working party advising on the feasibility of the scheme.

48. The Committee recommends that the assessment of the working party be referred to the Joint Standing Committee on Small Business or another relevant Committee of the Parliament for further review and advice to the Minister for Public Works and Services..

49. The Committee recommends that, if introduced, mandatory security of payment insurance be deferred for a period of 12 months.

50. The Committee recommends that the implementation of mandatory security of payment insurance then be phased in over a further period of 2 years commencing with contracts exceeding $5 million. This contract limit would be reduced after 12 months to $1 million and then eliminated so that mandatory security of payment insurance would apply to all contracts.

1. Introduction

The Joint Standing Committee on Small Business was established on the 27th November 1996, to inquire into issues affecting small business in New South Wales. The then Minister for State and Regional Development, the Hon Carl Scully MP stated that the Committee would:

> "have a brief to listen to the concerns of the small business sector and make recommendations to guide its future growth..." and "...enable the Government to become more attuned to the needs and problems of the dynamic small business sector."[1]

1.1 Terms of Reference of the Committee

The Terms of Reference of the Joint Standing Committee upon Small Business are:

> "That notwithstanding anything in the Standing Orders of both Houses, a Joint Standing Committee be appointed to inquire into and report upon Small Business in NSW with the following terms of reference:
>
> (1) The functions of the Committee are to report to Parliament on:
>
> (a) matters which reflect the importance of small business to the economy;
>
> (b) the streamlining of the provision of services to small business;
>
> (c) the reduction of regulatory control over small businesses;
>
> (d) the creation of employment opportunities within the small business industry;
>
> (e) the provision of assistance to small businesses in niche marketing;
>
> (f) the provision of assistance in the promotion of small business in regional development;
>
> (g) the provision of assistance to small business to become internationally competitive;
>
> (h) the provision of advice to persons intending to start a new business and to new starters in small business; and
>
> (i) any matters relating to or arising out of the above terms of reference.

[1] LEGISLATIVE ASSEMBLY Hansard Articles 51st Parliament, pg 6355

(2) The Committee is to consist of nine Members of both Houses, three being members of the Legislative Council (one supporting the Government, one Opposition and one Independent) and six being members of the Legislative Assembly (four members supporting the Government, one Opposition, one Independent and in the event that an Independent member is unavailable to serve on the Committee a member of the Opposition will be nominated instead). Members will be nominated in writing to the respective Clerks of the House.

(3) The quorum of the Committee is five Members, provided that the Committee meet as a joint committee at all times.

(4) The Chairman shall be a supporter of the Government.

(5) The Chairman or any Acting Chairman has a deliberative vote and, in the event of an equality of votes, a casting vote.

(6) The Committee has leave to sit during the sittings or any adjournment of either or both Houses, to adjourn from place to place; and to make visits of inspection within Australia and overseas."

The Committee members are:

Legislative Assembly

Mr J. Hunter	ALP
Ms R.P. Meagher	ALP
The Hon. J.J. Schipp	Liberal
Mr J.G. Tripodi	ALP
Mr J.A. Watkins	ALP
Mr A.H. Windsor	Independent

Legislative Council

The Hon. R.S. Jones	Independent
The Hon. R.S. Kersten	National
The Hon. E.M. Obeid	**ALP (Chairman)**

1.2 Definition of Small Business

Small businesses range from companies which operate on the international markets to self-employed people doing a few hours of word processing, family retailers, well established small manufacturers, rural and farm businesses, and franchises and agencies with varying levels of technical and marketing sophistication.

At a meeting held on the 22 April, 1997, the Committee agreed to adopt the following definition of small business:

1. **Managerial Characteristics:**

- they are independently owned and operated
- they are closely controlled by owner/managers who also contribute most, if not all, operating capital; and
- the principle decision making function rests with the owner/manager.

2. **Size component:**

- any size component should only serve as a functional addition to classification, rather than being of primary importance.

2. The Inquiry Process

Since October 1997, the Committee has adopted a comprehensive process of inquiry into the security of payments for subcontractors in the New South Wales building industry.

Initially, the Committee held briefings with representatives of contractor and subcontractor organisations in order to become familiar with all aspects of the security of payments debate. At this time it was decided that it would be appropriate for the Committee to facilitate a Round Table Discussion between the main organisations involved in the building industry.

Between November 1997 and March 1998, the Committee held three Round Table Discussions attended by representatives of 13 organisations:

The primary purpose behind the Round Table Discussions was to encourage agreement between all parties of the need to change the culture of delayed or non-payment of monies in the construction industry and develop a consensus on how that could be achieved.

The Committee then asked participants for submissions on measures which would improve payment performance. A Working Party was elected from the participants at the Round Tables and this group assisted with the assessment and screening of the proposals submitted.

In the absence of industry consensus concerning a trust based solution, the Committee proceeded with the construction of a Discussion Model for consideration by the building industry and the public.

The Discussion Model has drawn upon ideas which have emerged during the course of the Committee's inquiries. These ideas have focussed particularly on the proposed security of payment reforms in Queensland and on three items of recent legislation introduced in the United Kingdom under the broad title of Construction Contracts Legislation.

The Committee published a Discussion Paper which described the Discussion Model in detail and advertised for public submissions in the Sydney Morning Herald on Saturday 15 August 1998 and in a group of local and ethnic newspapers during the week commencing 31 August 1998.

The Committee received 31 public submissions from a broad spectrum of trade and professional associations in the building industry, insurance companies and several contractors.

These submissions were reviewed and based on the advice and opinions expressed in them a number of changes were made to the original structure of the Discussion Model. These revised reforms became the basis of the Committee's recommendations which are detailed in this Report.

3. Background to Security of Payment in the Building Industry

Security of payments for subcontractors in the construction industry has long been an issue of concern in New South Wales (NSW). The *Contractors' Debtors Act 1897* was introduced during the early days of the construction of railways in NSW in response to the problem of persons working on the railways not being paid wages due.

Data gathered by the Australian Bureau of Statistics creates a profile of the construction industry in New South Wales. In 1994-95, non-employing businesses accounted for 29,900 or 65% of all businesses in the construction industry. Small businesses with up to nine employees accounted for 14,500 or 31% of all businesses. This meant that while medium/large businesses accounted for 1,800 or 4% of the construction industry, the majority (96%) were classified as small.[2]

It has been the representatives of groups of subcontractors, suppliers and other service providers from this small business population, who have been advocating the need for a change in payment culture within the building industry over the past decade.

In May 1998, the *Contractors' Debtors Act 1897* was repealed and replaced by the *Contractors Debts Act 1997* to enable subcontractors to recover debts owed to them for work carried out and materials supplied by them. On its own, this Act is not intended to resolve all the problems of security of payment in the building industry. Rather, it is simply intended to be one of a number of measures that the Government is developing to address this complex problem.

It has been argued by representatives of subcontractor groups and associations that the *Contractors Debts Act 1997* does not resolve the main impediments to achieving security of payment. These remain, the extensive cost and length of time that a court-based solution imposes on subcontractors and the failure of the Act to ensure timely payments.

In response to this concern, subcontractor groups have put forward a number of options which have been analysed and refined over time but not acted upon. In more recent times, subcontractor groups have expressed their preference for a proposal for legislation establishing deemed cascading trusts through the contractor chain.

Over the past five years, a number of reports into security of payments have been commissioned by Government departments. These reports include:

- *Feasibility Study into the Proposal Prepared by the NSW Security of Payment Committee*, Anderson Consulting, May 1993.

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[2] ABS: *Survey of Employment and Earnings*; 1995/96.

- *Independent Assessment of the Viability of the NSW Security of Payment Proposal*, Coopers & Lybrand Consultants, August 1996.
- *Improving Security of Payment in the Building and Construction Industry*, Price Waterhouse, August 1996.
- *Security of Payment for Subcontractors, Consultants and Suppliers in the New South Wales Construction Industry*, Department of Public Works and Services, October 1996.

During the course of this inquiry, the Committee has been disturbed to discover that despite the extensive amount of time and thought spent on this issue, there is little statistical information about the extent of the security of payment problems in the construction industry.

4. Building and Construction Industry Statistics

4.1 The Cost of the Security of Payment Problem

The Green Paper titled "Security of Payment for Subcontractors, consultants and Suppliers in the New South Wales Construction Industry, October 1996, stated that there is no hard evidence available which quantifies the extent of the security of payment problem in monetary terms:

> Department of Public works and Services examination of data available to NSW government agencies over a 2 year period to July 1996 indicates that unpaid moneys, as a result of head contractor insolvencies on NSW government financed projects, is in the order of 0.15% ie., up to $10 million of the NSW Government's annual total capital expenditure of some $6 billion.
>
> However, losses from head contractor insolvency on government projects in the building sector of the industry are higher, averaging approximately 0.4 to 0.5% of total expenditure in that period. This is generally because of a greater use of subcontractors in building as against engineering works.
>
> Advice from industry associations and individual subcontractors and suppliers has been that the security of payment problem is generally more severe on private sector projects, as current Government initiatives have tempered behaviour on government projects.

The Construction Industry Development Agency (CIDA) in a report released in 1994 stated that:

> We believe it is an almost impossible task to meaningfully quantify the magnitude of the problem given the complexity of its interacting forces..

A report released by Australian Corporate Reporting (ACR) in April 1998 provides some insight into the number of insolvencies within the building and construction industry in New South Wales. The report states that insolvencies were three times higher in New South Wales than any other state in Australia.

Between October 1997 and February 1998, 61 building companies in NSW entered into some form of external administration. This compared to 20 in Victoria, 15 in Queensland, 5 in Western Australia, 3 in South Australia, 2 in the Northern Territory, 2 in the ACT and 1 in Tasmania over the same period.

It is generally claimed that 95% of the value of the labour spent on site is performed by subcontractors, and that in many cases these subcontractors find that they have little or no security over the monies owed to them if a contracting company goes into liquidation.

Of the little amount of information available on insolvencies in the building industry, it is apparent the examination of the costs to the industry of slow and deferred payments have not been undertaken.

4.2. Building Industry Statistics in New South Wales

In the period leading up to the year 2000, building and construction activity in New South Wales is expected to continue at the current high levels. The best available indicator of the construction activity was provided to the Committee by the Department of Public Works and Services.

Table 1: The New South Wales Building Industry

Activity - "Value of Work Done During the Financial Year"[3]

Constant Price 1989/90 $:	1996 $millions	1997 $millions	1998 $millions	1999 $millions	2000 $millions	2001 $millions
Total Private Residential Work	7,191.0	7,079.0	7,685.0	8,326.4	8,228.2	6,896.1
Total Private Residential Work	166.2	167.4	146.4	143.0	142.9	138.2
Total Residential Work	7,377.2	7,246.4	7,831.3	8,469.4	8,371.1	7,034.3
Total Non-residential Building	3,881.0	4,246.0	4,779.2	4,993.7	5,224.1	5,245.2
Total Building	11,258.2	11,492.4	12,610.5	13,403.1	13,595.2	12,279.5

Note: Years are financial years ending 30 June. Thus the year 2001 is the financial year 200/2001 or the year ending 30.6.2001.

As can be identified in Table 1, the value of total building work in New South Wales will continue to rise until the financial year ending in 2000 when it is estimated that the building industry will complete works valued at $13, 595.2 million. After this period it is expected that the total work undertaken by the building industry will fall by approximately $1,320 million for the financial year ending in 2001.

From analysis of the data contained in Table 1, it can be seen that the work undertaken by the non-residential sector of the industry is expected to comprise a greater percentage of all building works undertaken.

[3]National Institute of Economic and Industry Research, May 1998, for the NSW Department of Public Works and Services.

For instance, in 1998 non-residential building works are estimated to be $4,779.2 million or 33.7% of the total building work total of $12,610.5 million. In 1999, this figure is expected to rise to $4,933.7 or 36.8 % of the building work total of $13,595.2, in 2000 $5,244.1 or 38.0% of the building work total of $13,595.2 and in 2001 $5,245.2 or 42.7% of the total building work.

5. Security of Payment Reforms

5.1 Legislative Provisions

A Discussion Paper titled Security of Payment in the New South Wales Building Industry was published in August 1998 by this Committee. It proposed a number of legislative provisions to make a number of new initiatives mandatory under the legislative regime.

5.1.1 New Provisions

The Committee proposes a number of mandatory provisions be implemented which would require the amendment of current New South Wales legislation, or the creation of new legislation.

These provisions include the introduction of a mandatory Building Code of Conduct (The Code) governing payment and notification behaviour in the building industry.

To strengthen the efficiency of the Code in changing payment behaviour, it is proposed that a Building Registration Authority be established by legislation to monitor behaviour and breaches of the Code (Refer 5.2).

The Code is directed specifically at eliminating slow payment and reducing the magnitude of insolvencies. (Refer 5.3)

To assist the Code and the BRA there would be a legislated requirement for written contracts for all building work (Refer 5.3) and that such contracts contain certain terms (Refer 5.4).

5.1.2 Amendments to Legislation

Contractors Debts Act 1997

The *Contractors Debts Act 1997* includes a number of provisions for a person to recover moneys owed by a defaulting contractor. Included in these provisions is that an attachment order may be made against any person from whom the unpaid person may be able to recover the debt.

Under Section 14 of the Act, power is given to a court to make an attachment order against any person from whom the unpaid person may be able to recover the debt under the Act. An attachment order effectively freezes moneys owed in the hands of the person named in the attachment order pending the result of the litigation.

The Minister noted in his second reading speech to the Bill that Section 14:

> provides for a court in which proceedings are first commenced for the recovery of a debt owed to the unpaid person for work carried out or materials supplied

> by the unpaid person to make an attachment order against any other person from whom the unpaid person may be able to recover the debt under the proposed Act. The effect of such an order will be that money owed by the principal to the defaulting contractor under the contract will be frozen pending judgment being given in the proceedings between the unpaid person and the defaulting contractor. This will protect the fruits of any judgment in the event that the unpaid person should prove successful in these proceedings.

During the course of this inquiry it has been brought to the Committee's attention that, in a case where the principal has already paid the defaulting contractor for moneys owed to the unpaid person for work contracted, an attachment order could not be made against the principal.

The Committee believes that in such cases, it is necessary for an attachment order to be capable of being made against the defaulting contractor and recommends this legislative amendment.

Commercial Tribunal Act 1984

The Committee proposes that all prosecutions for breaches of the Code and all appeals regarding registration by the BRA be heard in the Commercial Tribunal or its successor bodies.

Section 18 of the *Commercial Tribunal Act 1984* states:

> **18 Jurisdiction and functions of Tribunal**
> (1) The Tribunal has such jurisdiction as is, and such functions as are, conferred on it by or under an Act.

A note attached to the Commercial Tribunal Act 1984 states that the following Acts confer jurisdiction on the Tribunal:

Building Services Corporation Act 1989
Consumer Credit Administration Act 1995
Credit Act 1984
Credit (Finance Brokers) Act 1984
Credit (Home Finance Contracts) Act 1984
Fair Trading Act 1987
Motor Dealers Act 1974
Registration of Interests in Goods Act 1986
Retail Leases Act 1994
Trade Measurement Act 1989
Trade Measurement Administration Act 1989
Travel Agents Act 1986

Under Section 18(4) (a) and subject to section 33, a judgment or order of the Commercial

Tribunal has the same effect as, and may be enforced in the same way as, a judgment or order of the District Court.

A similar provision to that being recommended by the Committee is provided in the Retail Leases Act 1984. *Division 3 Determination of retail tenancy claims by Commercial Tribunal* in that Act defines the meaning of a claim, sets out which claims can be lodged in the Tribunal, the jurisdiction and the powers of the Tribunal, including the power to make an order to pay money or to perform any specified work or service.

5.1.3 Jurisdiction of the Small Claims Division, Local Court

It is envisaged that under the proposed adjudicated dispute resolution process, any disputes concerning moneys owed, which fall within the jurisdiction of the Small Claims Division of the Local Court, could be heard in that court.

This does not prevent the parties to a dispute from utilising the adjudicated dispute resolution process, any specified dispute resolution clauses in their contract or pursuing recompense under the Contractors Debts Act 1997 or other legislation.

Currently, the Small Claims Division provides resolution of civil disputes for claims valued up to $3,000 without formal court proceedings or legal representation. Undefended claims result in a judgement within 28 days.

Defended action depends on court lists but averages four to six weeks. The court order is final. With court facilities in 161 locations this avenue provides a cost effective and accessible remedy for small disputes.

The fee for filing a statement of claim in the Small Claims Division is $51 for a claim not exceeding $3,000 and $68 for a claim exceeding $3,000 but not exceeding $10,000.

Under the Local Courts (Civil Claims) Act 1970 *Part 3 - Jurisdiction, Division 1 - Amounts* Section 12 relates to the jurisdiction of the Court:

> **(3)** Subject to this Part, a court sitting in its Small Claims Division has jurisdiction to hear and determine actions for the recovery of any debt, demand or damage (whether liquidated or unliquidated) in which the amount claimed is not more than $3,000 (or such greater amount as the rules may prescribe), whether on a balance of account or after an admitted set-off or otherwise.
>
> **(4)** Subject to this Part, a court sitting in its Small Claims Division has jurisdiction to hear and determine actions commenced after the commencement of this section to recover goods that are detained, or to recover the assessed value of the goods, if the value of the goods

together with the amount of any consequential damages claimed for the detention of the goods does not exceed $3,000.

The Committee recommends that the limit on matters which can be resolved in the Small Claims Division be increased from $3,000 to $ 10,000.

5.1.4 Jurisdiction of the Building Disputes Tribunal

It is also envisaged that under the proposed adjudicated dispute resolution process that any dispute between registered entities could be resolved using a claim lodged with the Building Disputes Tribunal or its successor body. The Tribunal currently has jurisdiction for claims up to a limit of $25,000 on residential work only.

No amendment is recommended to this jurisdiction.

5.1.5 Order of Precedence of Resolution Mechanisms

The legislation should provide for the utilisation of the proposed adjudication process as a matter of precedence if notice to this effect is issued by either party.

In the absence of such a notice or by mutual agreement of the parties the dispute can be resolved by lodgement of a claim with either the Building Dispute Tribunal or the Local Court

5.1.6 Recommendations

- The Committee recommends that legislation be introduced to establish the BRA.
- The Committee recommends that legislation be introduced to establish a mandatory Building Code of Conduct (the Code) governing payment and notification behaviour in the building industry.
- The Committee recommends that the Contractors Debts Act 1997 be amended to include provision for an attachment order to be made against the defaulting contractor.
- The Committee recommends that jurisdiction be conferred on the Commercial Tribunal or its successor bodies to hear prosecutions on breaches of the Code and appeals in relation to registration decisions made by the BRA.
- The Committee recommends that the monetary jurisdictional limit in the Small Claims Division in the Local Court be increased from $3,000 to $10,000.

5.2 Building Registration Authority

5.2.1 Introduction

The Discussion Paper released by the Committee proposed that new legislation would establish a Building Registration Authority (BRA) which would be responsible for:

- registration of entities engaged in commercial, industrial and residential building;
- prosecuting breaches of the Act and Code;
- monitoring compliance; and
- accrediting dispute resolution bodies and adjudicators.

5.2.2 Analysis of Public Submissions

A large majority of public submissions supported the establishment of such an authority.

The submission from the Civil Contractors Federation [sub.25] stated:

> that the establishment of a licensing/registration system is critical to the future of contractors in the building and construction industry.

The Australian Constructors Association [sub.12] also said that it:

> ..supports in principle the proposal to establish a licencing and registration system for contractors operating in the commercial building sector...

while the Australian Industry Group [sub.13] noted that:

> key elements of the Standing Committee's framework including registration and licensing.... were supported.

Representations at discussions with the insurance industry were unequivocal in identifying registration as a prerequisite to any form of mandatory insurance regime.

The only submission which made any adverse reference to the BRA was received from the Housing Industry Association [sub.26] who stated that:

> HIA has...remained consistently opposed in principle to licensing of commercial builders and to third party interference in contractual relationships.

As a consequence the broad thrust of the role of the BRA has been adopted from the Discussion Paper.

In pages 12 to 14 of the Committee's Discussion Paper, the role and powers of the Authority

are expanded under the following headings:

- Registration.
- Compliance with the Act and the Building Code of Conduct.
- Adjudication.
- Owners and Principals.
- Breaches of the Act.
- Powers of Investigation.
- Power to Prosecute.
- Power to Decline an Application or Renewal.

5.2.3 Areas of Adjustment to the Discussion Model

5.2.3.1 Scope of Registration of building entities

Non-Building Construction

The Committee received a number of submissions on the range of building entities who would be required to register under the proposed scheme. Particular attention was given to the intention to exclude contractors solely engaged in civil works (eg. roads, dams, bridges etc).

The submission from the Civil Contractors Federation [sub.25] states:

> The civil contracting industry requires a registration/licensing system far more than any other sector of the industry as there is no licensing system in this industry at all, at the current time... The Civil Contractors Federation has in fact been working on a proposal to introduce licensing in the civil construction industry for some time, and as such the type of BRA proposed in the discussion paper would be welcomed by this industry.

As many of the problems encountered in the civil construction industry are very similar to those encountered in the building industry, it is anticipated that a large proportion of the security of payment reforms recommended within this Report could be adapted for the civil construction industry.

The Committee therefore recommends that participants in that sector adopt the notification and adjudication measures advocated in the Building Code of Conduct.

The Committee recognises that security of payment problems are a much broader issue than simply the building industry. The scope of this inquiry has, however, been focussed on investigation of *security of payments for subcontractors in the building industry*. The contracts in civil construction are generally much larger and, based on recent history in Victoria, so are the disputes.

As such, civil works (ie. roads, dams, bridges) falls outside of the Committee's terms of

reference and its recommendations in this Report focus on activities in the commercial, industrial and residential building sector.

Owners, principals and project managers.
The Discussion Paper made particular mention of the requirement for registration of owners and principals:

> who concurrently enter contracts with more than one contractor for the completion of building work on a site which they own or lease and project managers who contract with owners or principals for the management of building contracts between those parties and other registered building contractors.[4]

The Committee received no specific comments regarding this group of registrants. The Committee believes that full registration requirements are appropriate in specified circumstances whereby owners, principals, and project managers assume the role of the head contractor in a relationship with subcontract trades.

Specialist Supplier Category
A number of submissions advocated the registration of consultants and the provision of access to notification and dispute resolution processes to suppliers, hirers and professional service providers.

Specialist suppliers may provide their services to the principal, head contractor or subcontractor depending on the way the building project has been structured. These suppliers are most likely to be at the end of the contractual chain and less likely to be subject to demands for payments from others.

In these circumstances full registration would not necessarily be appropriate, as this may cause unnecessary administrative and cost burdens on large segments of business, many of whom may be peripherally involved in the building industry.

The Committee recognises that there is potential for businesses in this category to be impacted economically by the insolvency of, or delays of payment by their registered entity clients.

In the submission by the NSW Security of Payment Committee (SPC) [sub. 27] it was submitted:

> those suppliers, hirers and service providers must be entitled, at their cost to utilise notification, adjudication and Designated Trust Account provisions of the proposed legislation.

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[4] Joint Standing Committee on Small Business: **Discussion Paper - Security of Payment in the New South Wales Building Industry**; August 1998, p13.

> It is suggested individuals/entities....could be registered in separate categories eg "registered supplier"....(for a fee) if this is necessary to enable them to be entitled to utilise those provisions...

The Committee believes that the use of the notification and dispute resolution provisions of the Code by suppliers to the industry should be encouraged.

However, the cost of extending these services to such a broad spectrum of businesses would be substantial. Consequently access to these provisions could be achieved only through the registration of hirers and material and service suppliers.

Such registration would be optional for all suppliers but as outlined above would be necessary if the supplier wished to access the standard contractual terms concerning payment, notification and adjudication.

It should be noted, that registered specialist suppliers would be subject to the same requirements imposed in respect of written contracts, instructions or supply arrangements as other registered entities if they wish to utilise the provisions of this legislation.

It is, however, anticipated that specialist suppliers would be excluded from a number of the mandatory requirements under the Code, in particular Mandatory Security of Payment Insurance.

The payment of a nominal registration fee would contribute to the administration costs associated with the expansion of the registration base and the recording of additional dispute data.

The names and details of principals, directors and executive officers and managers of a registered entity would be recorded by the BRA in the Building Registration Information System (BRIS).

5.2.3.2 Public Disclosure of BRA Records

Several submissions canvassed the issue of public disclosure of the records of the BRA. The majority of submissions favoured public disclosure of:

- substantiated breaches; and
- the results of disciplinary action but not of reported disputes.

In their submission to the Committee, FAI Insurance [sub.21] specified a special requirement of insurers, stating:

> The Registration /Licensing Authority must be obliged to inform insurers of all matters referred for dispute resolution, prosecution, warnings, fines and all cancellations suspensions or non renewal of licences.

This process is consistent with the protocol established between the Department of Fair Trading and insurers under the Home Warranty Scheme for residential building.

The Committee recognises that there is a need for insurers to have available the most relevant information relating to the risks they are undertaking. It is, therefore, recommended that a protocol be established for the exchange of information between the Authority and any insurers confirming their intention to provide insurance products to registered contractors.

If insurers are to have access to information relating to the performance of registered entities, the Committee believes that it would be impractical to deny such access to other parties, who are dealing with registered entities. Consequently, information on the number and status of current disputes should be available to all enquirers.

The Committee is of the opinion that records of disputes, which have been resolved, should be withdrawn from publication from the time the resolution is notified unless the Adjudicator's Report identified a breach of the Code.

Breaches of the Code should be separately recorded and this information should also be publicly available.

5.2.4 Outline of the BRA's Role

Registration
The proposed legislation would require that all contractors and subcontractors (and in certain instances owners, principals and project managers) who are engaged in contracts in commercial and industrial building will be required to register with the BRA prior to entering into such contracts.

It is anticipated that building and trade contractors already licensed by the Department of Fair Trading for residential building work will be registered automatically with the BRA. (There may be an additional charge for this registration and the accompanying extension of services).

Owner-builders undertaking residential building work under an owner builder permit issued by the Department of Fair Trading under the Home Building Act will become registered entities automatically by issue of that permit.

The scope of this registration would seek to harmonise with the existing scope of licensing of residential, commercial and industrial building entities performing building work as defined in Section 4 of the Queensland Building Services Authority Act 1991 and its regulations.

The most recent proposal for reform in Queensland seeks to rationalise the number and classifications of licenses but does not propose any reforms in relation to the definition of building work.

The Committee recommends that a separate registration category for specialist suppliers is created. The registration of specialist suppliers would be optional for all material and professional service suppliers who supply materials or services which are utilised in the planning, design or construction of a building.

The BRA would be responsible for processing all applications for registration and registration renewals.

Adjudication
The BRA would be responsible for the development and maintenance of an accredited network of appropriately qualified adjudicators and accredited professional bodies and institutes. These bodies would nominate accredited adjudicators from their membership.

The BRA would not adjudicate disputes but would refer parties in dispute to accredited bodies or institutes who would appoint an adjudicator. (This aspect is covered in greater detail in section 5.5).

Compliance with the Act and the Building Code of Conduct
The Committee anticipates that the BRA would be required to administer the proposed legislation which would underpin the Code for all registered entities. As a consequence, it is expected that the BRA would be responsible for investigating and prosecuting unregistered building entities and registered entities, which operated in breach of the Act or the Code.

Under the proposed legislation, any building entity would be in breach of the Act if they entered into building contracts while unregistered. The legislation would provide for sanctions ranging from formal warnings for a first offence to prosecution in the Local Court with penalties of up to 100 points (currently $11,000) per offence for repeat offenders.

If a building entity was found to have repeatedly entered into contracts while unregistered, the legislation would give the BRA the power to prosecute for the disqualification of principals, directors and operational managers of the unregistered building entity who are also principals, owners, directors and operational managers in a registered entity from holding such office in a registered entity.

The BRA would be responsible for the administration of disciplinary actions which would include formal warnings, imposition of fines, temporary suspension and permanent deregistrations following prosecutions for major or consistent breaches of the Code by registered entities.

Powers of Investigation
The BRA would have the powers to:

- investigate any breach of the Code;
- require copies of all contractual arrangements;

- require certification from the principal or chief financial officer that the registered entity has the financial resources to pay its obligations as they become due and payable; and
- demand the provision of an independent financial assessment by a certified public accountant or external auditor of the registered entity's continuing financial viability.

In order to pursue investigations into breaches of the Code, the BRA would have the power to suspend, for a period of up to 60 days, the registration of any registered entity associated with the principals, directors and operational managers of the entity under investigation.

For the suspension of registration to continue beyond 60 days, the BRA would need to seek an order for disqualification against the registered entity in the Commercial Tribunal or its successor bodies. (Any suspension of registration only restricts the registered entity from entering new contracts, it does not interfere with the completion of existing contracts.)

Power to Prosecute
After investigation, the BRA would be able to prosecute for breach of the Code in the Commercial Tribunal or its successor bodies and seek penalties and disqualifications against individuals and associated registered entities.

Power to Decline an Application or Renewal
The BRA would have the power to decline an application for registration or application for renewal of a registration from any building entity which has an unsatisfactory record or any individual who has been a principal, director or operational manager of a building entity with an unsatisfactory record.

Building entities and individuals would have the right to appeal to the Commercial Tribunal or its successor bodies against any BRA decision regarding their registration but not about any other building entities' registration.

Power to disclose information
The BRA would have the power to establish protocols for sharing all information on its records with any insurer confirming its interest in providing insurance products for this purpose. The Authority would also have the power to disclose information on current disputes, disciplinary actions taken and breaches of the Building Code of Conduct but would remove, after notification of resolution, information on disputes which have been resolved where there was no breach.

5.2.5 Conclusions

The Committee regards the monitoring and compliance responsibility of the BRA as critical to the success of the proposed reforms. For this reason it strongly recommends that the courts and tribunals support the BRA by imposing appropriate penalties.

In particular, it is essential that registration is denied to people and entities who have demonstrated that their behaviour endangers the viability of others in the industry. Regular unreasonable delays in payment, failure to co-operate with proposed dispute resolution processes, failing to comply with adjudicators' orders or lodging and pursuing vexatious claims would warrant the consideration of de-registration.

Further, the Committee believes that the re-entry of such building entities and associated individuals into the industry using new or different business structures or through the nomination of alternative officers should be stringently examined.

5.2.6 Recommendations

- The Committee recommends that the BRA be responsible for:
  - registration of entities engaged in commercial, industrial and residential building work;
  - prosecuting breaches of the legislation and Code;
  - monitoring compliance; and
  - accrediting dispute resolution bodies and adjudicators.

- The Committee recommends that the BRA be responsible for processing all applications for registration and registration renewals.

- The Committee recommends that all contractors and subcontractors (and in certain instances owners, principals and project managers) who are engaged in contracts in commercial and industrial building be required to register with the BRA.

- The Committee recommends that all contractors who currently hold Residential Building Licences would automatically be registered by the BRA.

- The Committee recommends that a separate registration category for specialist suppliers be created.

- The Committee recommends that the registration of specialist suppliers be optional for all suppliers, hirers, and professional service providers who supply materials or services which are utilised in the planning, design or construction of a building.

- The Committee recommends that owners, principals, and project managers who assume the role of the head contractor in a relationship with subcontractor trades be required to register.

- The Committee recommends that information relating to the performance of registered entities be available to the public.

- The Committee recommends that the Department of Fair Trading Residential Building

Licensing Database be utilised as the basis for the Building Registration Information System (BRIS).

5.3 Building Code of Conduct

5.3.1 Introduction

The basic aim of a code of conduct is to encourage transparency in dealings between the contracting parties.

One of the benefits of implementing a code of conduct, is that it allows the Government to introduce obligations that meet the needs of a specific industry while avoiding the complexities and expense of detailed legislation. The Committee believes that the implementation of a code of conduct will act as a catalyst for reform within the building industry.

In addition to the direct benefits of having general principles of industry behaviour, it is considered by Australian Accountant that "much of the benefit of having a code arises from the process of its development."[5]

The Committee agrees with this opinion and believes that industry representatives should be directly involved in the development process of a building industry specific code of conduct. As the article by Australian Accountant notes, "...they will then be more likely to accept it; feel they have some ownership of it; and be more likely to be motivated by it."

5.3.2 General Provisions

In response to the assertion in the Discussion Paper that a Building Code of Conduct (The Code) is a necessary component of the proposed security of payment model, the submission from Specialist Contractors [sub.24] stated:

> We...fully support a Code of Conduct for the industry. A Code of Conduct is long overdue....The introduction of a Code governing payment and notification behaviour in the building industry should be directed specifically at eliminating slow payment and reducing the magnitude of insolvencies.

The Committee agrees with the Specialist Contractors that there is a need to eliminate slow payment and reduce the magnitude of insolvencies from the building industry and believes that the implementation of a mandatory Code will achieve this result.

It is proposed, therefore, that a Building Code of Conduct be introduced for registered entities which would require:

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[5] Australian Accountant: **Codes of Conduct - a framework for ethics**; February 1998; p1.

- all contracts to be written and contain certain terms;
- debtors to notify creditors of intention to revise payment;
- the BRA to be notified in the event of a dispute between the contract parties;
- a prescribed dispute resolution process be adopted;
- a designated trust account (DTA) to be established to keep disputed monies while the dispute is settled; and
- all parties to abide by the adjudicator's decisions.

The Code will also establish standard contract terms covering payment, notification, dispute resolution and suspension of work which would be implied if they were not already expressly contained in a building contract. (These standard conditions are outlined in more detail in section 5.4.)

As already outlined in 5.2, breaches of the Code will be recorded on the registered entities' record maintained by the BRA and will be part of the information available to insurers and the public on enquiry.

5.3.3 Registration

In response to the section on Building Code of Conduct outlined in the Discussion Paper, the Committee has received a number of submissions indicating that the Code of Conduct should apply equally to contractors and subcontractors.

In his submission to the Committee, Mr Geoff Markham - Institute of Arbitrators & Mediators Australia [sub.5] queried whether the Code should only apply to contractors:

> A matter to be considered is whether or not subcontractors ought be registered and also be required to comply with the Building Code of Conduct.

This position was supported by Mr Ken Ware - Austruc Constructions Ltd [sub.18] who stated:

> registration and Code of Conduct should apply equally to subcontractors.

As noted in Mr Markham's submission:

> As the provisions of the Code are presently stated, one could envisage that in certain circumstances, a subcontractor could commit the following breaches:
> - failure to respond to dispute notification;
> - failure to attend dispute resolution;
> - failure to deposit monies in dispute in a trust account;
> - failure to comply with an adjudicators decision; and
> - making claims which an adjudicator has assessed as being vexatious

The Committee agrees that registration and the Code of Conduct is applicable to all entities which contract for building work in the industry and has amended its definitions of registered entity and building entity to ensure there is no future confusion.

It is the Committee's opinion that legislation establishing the BRA should also make reference to a mandatory Code of Conduct for all registered entities. By supporting the provisions of The Code with legislation, all registered entities would be obliged to comply with the Code or face deregistration.

The legislation would therefore stipulate that only registered entities would be able to enter into contracts for the provision of building work.

This proposal was supported in the submission received from Mr Craig Long - Civil Contractors Federation [sub.25] who stated:

> ...the Federation believes that only licensed contractors and subcontractors should be able to be engaged by developers, owners or contractors in a subcontracting arrangement.

The Committee agrees that only registered entities should be used when undertaking building works. If it comes to the attention of the BRA that unregistered building entities are undertaking building works these unregistered building entities will be prosecuted in the Local Court for a breach of the legislation.

It must be emphasised that registered entities, including those entities such as owner-builders and residential trade contractors whose registration is affected automatically as a result of licences or permits issued by the Department of Fair Trading, would all be equally subject to the requirements of the Code and are entitled to the services available.

5.3.4 Breaches of the Code

In the Discussion Paper, the Committee outlined behaviour which would constitute a breach. Such breaches of the Code would include:

- contracting without a written document;
- making contracts that inadequately specify the registered entity and registration number;
- making contracts which include clauses which are prohibited by the Code;
- failure to respond to dispute notification;
- failure to attend dispute resolution;
- failure to comply with an adjudicator's order;
- failure to deposit monies in dispute in a Designated Trust Account; and
- vexatious claims.

And after the relevant legislation is proclaimed:

- failure to effect MSPI.

After the Code has been implemented, an opportunity exists for the collation of dispute data and breaches of the Code by the BRA. This information could then be used to monitor contractor and subcontractor behaviour and as a basis for decisions on disciplinary action and registration.

As outlined in the Committee's Discussion Paper, consistent breaches of the Code may result in the suspension of a registered entities' registration. Suspension of registration would prevent such entities from entering into new contracts but would allow for the completion of existing contracts.

The submission to the Committee from Austruc Constructions Ltd [sub.18] disagreed with suspended entities being prevented from entering into new contracts:

> The proposal that suspension of registration would prevent the contractor from entering new contracts is an unrealistic approach which could incur the industry in huge expense by delay penalties when a contractor is contractually bound, or a Client is experiencing holding or other costs.

The Committee maintains that the option to suspend is a necessary component of these reforms. The threat of suspension of a registered entities' registration for violation of the provisions of the Code is an essential sanction to enable the BRA to seek and enforce compliance with the Code. The Committee's sentiment on deregistration where the viability of other parties in the industry is threatened has already been summarised in 5.2.5.

5.3.5 Recommendations

- The Committee recommends that a mandatory Building Code of Conduct for registered entities be introduced and include the following requirements:
  - that all contracts be written and contain certain terms;
  - that creditors notify debtors of their intention to revise payment within a specified time;
  - that the BRA be notified of disputes involving registered entities;
  - that a prescribed dispute resolution process be adopted;
  - that a designated trust account (DTA) be established to keep disputed monies while the dispute is settled;
  - that all parties abide by the adjudicator's decision; and
  - that all registered entities secure mandatory security of payment insurance when these requirements are proclaimed.

- The committee recommends that the Code specify standard implied terms of payment,

notification, adjudication and suspension of work in the event these are not expressly contained in a written contract.

- The Committee recommends that the minimum standard contract terms outlined in the Code apply equally to the registered entity and the other party to a contract for building if unregistered.

- The Committee recommends that consistent breaches of the Code may result in the suspension of a registered entities' registration.

- The Committee recommends that the BRA have the power to suspend the registration of any registered entity associated with the principals, directors and operational managers of the registered entity under investigation, for a period of up to 60 days.

- The Committee recommends that the BRA collate dispute data and breaches of the Code.

5.4 Standard Contract Requirements

5.4.1 Introduction

One of the main objectives of the Building Code of Conduct is to prescribe certain minimum standard terms to be included in all written contracts for building work entered into by registered entities.

In order to achieve this aim, the industry must firstly adapt to the use of written contracts. If a registered entity does not utilise written contracts, the benefits arising from the legislated Code of Conduct minimum standard terms related to payment, notification and adjudication will not be available to the parties for that contract.

It is the Committee's belief that the introduction of minimum standard contract terms for all written contracts entered into by registered entities will lead to more transparency within the building industry and have a beneficial effect on the industry's payment behaviour.

As such, it is proposed that all written contracts should include the following general terms:

- all parties' Registered Entity Registration numbers;
- detailed statement of scope of works to be performed;
- the work completion date;
- details of payment terms;
- details of notification terms;
- dispute resolution and/or adjudication provisions; and
- right to suspend work without penalty in three specified circumstances.

Further, it is proposed that the following terms be prohibited in building contracts:

- 'pay if paid' and 'pay when paid' clauses; and
- 'contracting out of the provisions of the Code' clauses.

In order for the minimum standard contractual terms to gain prompt industry compliance, the Committee believes that these standard requirements (including the requirement for written contracts) need to be incorporated within the legislative provisions of the Building Code of Conduct.

The proposed legislation will provide that, in the event that a written contract for building work fails to incorporate the minimum standard contractual terms, then the Code's standard terms for payment, notification, adjudication and suspension of work requirements will be incorporated into the contract as implied terms.

It should be noted, however, that there will be no implication of the Code's standard terms in the case of unwritten or verbal contract between registered entities.

5.4.2 Payment Terms

The standard payment term outlined in the Discussion Paper was set at 14 days from the date of receipt of invoice. The Committee received a number of submissions which addressed the likelihood of the proposed payment schedule being adopted by the industry.

In their submission to the Committee, the Australian Constructors Association [sub.11] stated:

> The Association believes that the payment terms...are unrealistic and required further development.

This statement was supported by the Australian Industry Group [sub.12]:

> The Australian Industry Group supports the proposal that contracts be in writing but believes that the proposals related to payment...are commercially unrealistic.

The submission to the Committee from Austruc Constructions Ltd [sub.18], noted that there would be difficulty within the industry adapting from the current payment terms to those proposed in the security of payment model:

> ....this requirement is abnormal to industry practice. The industry usually works on a 30 day system for both subcontractor/creditor and client payment.

The Committee concedes that the 14 day payment term described in the Discussion Paper is a tight time frame. It should be noted, however, that the 14 day payment term is an implied

statutory (Code) term which will only apply in the event that a written contract does not expressly specify alternate payment terms.

The onus is, therefore, placed on all registered entities to ensure that commercially acceptable payment terms are expressly specified in all written contracts.

A number of submissions to the Committee also asserted that any prescribed payment terms should also be extended to include the principal/client. As was noted by the Australian Constructors Association [sub.11]:

> The proposed payment terms must be extended to bind the principal/client if the system is to operate equitably. Alternatively the framework could require terms in the head contract/subcontract to be aligned.

This position was supported by the Australian Property Institute [sub.17]:

> The proposed 14 day payment provision will be unfair unless a similar requirement is mandatory in head contacts.

The Committee recognises that a need exists for any payment terms to be comparable between all levels of the building industry and encourages the use of contracts with reflective payment clauses as recommended by the Government's Code of Tendering.

If a contract between the principal/client and a contractor does not specify payment terms, the Committee can see no reason why statutory (Code) implied payment term (ie. 14 days from receipt of invoice) should not apply.

The Committee also proposes that legislation prohibit 'pay when paid', 'pay if paid' and 'contracting out of the Code' clauses from written contracts. The prohibition of these clauses was supported in the majority of submissions.

As was noted by the Australasian Dispute Centre [sub.11]:

> ...'pay when paid' and 'pay if paid' clauses must not be available to contractors as such approaches...are unfair and draconian.

Note: Any express specification of payment terms in a written contract is valid and binding and supersedes the 14 day implied payment term specified in the Code. The Committee's recommendations do not seek to interfere with normal contractual arrangements.

5.4.3 Notification Terms

As part of the minimum standard contractual terms, the Committee proposes that every written

contract for building work entered into by a registered entity incorporate notification terms. In the Committee's Discussion Paper, it was proposed that notification terms should be 7 days from the receipt of invoice or any subsequent notice.

As part of this process, the Committee believes that the following notices should be included as non -excludable implied terms in the Building Code of Conduct:

- *Notice of Intent to Revise Payment*. A notice sent from the debtor to the creditor after receipt by the debtor of the creditor's invoice prior to the invoice being due and payable and within 7 days of receipt.
- *Notice Requiring Adjudication.* A notice sent by the creditor to the debtor after receipt of a Notice of Intent to Revise Payment in the event that payment is being withheld, delayed and/or is incomplete.
- *Notice to Suspend Work.* A notice sent in any of 3 sets of circumstances
  - (1) from the creditor to the debtor: in the circumstances where the creditor has sent an invoice and no notification to revise payment has been received and there has been incomplete payment of the invoice by the debtor on or by the express or implied payment date.
  - (2) from either the creditor or debtor: in the circumstance where there is a failure to comply with an adjudicator's order;
  - (3) from either the creditor or debtor: if insolvency proceedings commence against the other party.
- *Notice of Intent to Litigate.* A notice sent by either party to the dispute following receipt of an order from an adjudicator.

A number of submissions to the Committee noted that the time frame for response to notices was extremely tight. This position was supported by the Civil Contractors Association [sub.25]:

> ...the 7 day requirement is unrealistic and...in fact 14 days would be a realistic and workable time frame for such notification.

The Committee acknowledges that the 7 day notification term may cause concern within some sectors of the building industry. However, this is the first step in a process which may take up to 21 days to reach resolution. In other parts of the industry, delays extending beyond 21 days also bring considerable hardship.

As a non-excludable implied term provided for in legislation, however, a 7 day time frame is considered appropriate.

The Committee does recognise that on occasions, especially where contracts require certification or inspection of work, the 7 day notification term will be impractical. In these circumstances, the initial notice of *Intent to Revise Payment* will be extended by the time stipulated for such certification and inspection. It should be noted, however, that in any

instance such an extension cannot exceed the date when payment is due or 21 days - whichever period is less.

Note: The express terms in a written contract will not be able to override the non-excludable implied terms specified in the Code for notifications.

5.4.4 Adjudication Terms

As part of the minimum standard contractual terms, the Committee proposes that the Code require every written contract for building work incorporate a number of standard adjudication provisions. These provisions would include:

- a requirement that disputes be subject to prompt impartial adjudication, including details of how disputes are to be resolved;
- a requirement that all parties comply with the adjudicators' decisions (an adjudicator's decision may be subsequently tested in an appropriate court or Tribunal);
- a requirement that monies identified by an adjudicator as being in dispute be held in a DTA from the time they are due and so ordered by the adjudicator until the time the dispute is ultimately resolved between the parties; and
- a requirement that monies specified in the adjudicator's order are placed into a DTA at the time either party issues a *Notice of Intent to Litigate*.

The minimum standard contractual adjudication terms specified in the Code would require:

- the nomination of an impartial accredited adjudicator; and
- the adjudicator to provide a decision within 7 days of notification of the dispute.

The time frame proposed in the Discussion Paper was commented upon by a number of submissions. The Institute of Arbitrators & Mediators Australia [sub.2] stated:

> The time frame being contemplated...is extremely tight and it is essential that the relevant documents, from both parties, are provided to the adjudicator as early as possible and prior to the adjudicator visiting the site and/or hearing the dispute.

This position was supported by FAI Insurance [sub.21]:

> It is essential that reasonable time is allowed for both parties to prepare submissions for the adjudication...a period of 10 working days would be more reasonable.

After much discussion with professional bodies who presently provide arbitration and mediation services, the Committee has concluded that the 7 day adjudication period is

achievable.

In the event that the adjudicator cannot provide a final decision within the 7 day time frame, there is an option to obtain an extension of time with the knowledge and agreement of the parties in dispute.

Note: The express terms in a written contract will not be able to override the non-excludable implied terms specified in the Code for adjudication. It will be possible to specify other and subsequent alternative dispute resolution processes.

5.4.5 Variations

Variations within contracts are major cause of disputes within the building industry. In order to assist an adjudicator in reaching a decision, the Committee believes that variations must be seen as an extension of the written contract.

In this sense, any variations to a written contract involving a registered entity will be required to:

- be in writing; and
- possess or refer to the basic terms and conditions of the main contract, unless these terms and conditions are expressly varied in the variation documentation.

The resolution of any dispute concerning variations will, therefore, be governed by the express terms in the variation or the express and implied terms specified in the original written contract.

If any variations have not been documented in writing, a dispute relating to a variation will not be able to be resolved by the notification/adjudication Code provisions

Note: The express terms in the written contract or a term expressly varied in the variation documentation will override the 14 day implied payment terms specified in the Code.

5.4.6 Suspension of Work Provisions

As part of the minimum standard contractual terms, the Committee proposes that the Code require every written contract incorporate suspension of work terms.

The minimum standard terms of contract will recognise the right of either party to issue a notice of *Intent to Suspend Work* without penalty in the following 3 specified circumstances:

- in the event that payment to a creditor has been withheld, delayed and/or is incomplete beyond the express or implied due date without prior *Notice of Intent to Revise*

Payment being given. (7 days notice of *Intent to Suspend Work* must be given);

- if either party fails to comply with an order issued by the adjudicator (7 days notice of *Intent to Suspend Work* must be given); and
- if insolvency proceedings commence in relation to either party (*Notice of Intent to Suspend Work* effective immediately).

A number of submissions to the Committee expressed concerns that the minimum standard terms incorporated the right to suspend work, with Mr Tony Glambedakis [sub.10] stating:

> Suspension of works should be the very last option (other than on safety grounds) because of the cumulative effects to all other trades, which will make a trade sectional problem a general problem to everyone on a construction site.

This opinion was shared by Mr Geoff Markham - Institute of Arbitrators & Mediators Australia [sub.5] who noted:

> The rights...to suspend work requires very careful consideration as the financial consequences of suspension may, in many cases, be completely out of proportion to the sum actually in dispute.

The Committee recognises that the right to suspend work is not without risk of being used vexatiously by either party. It should be noted, however, that suspension of work can only occur at the expiration of the notice of *Intent to Suspend Work* and only if the circumstances giving rise to the notice remain unchanged. This provision states that there must be 7 days notice provided prior to stopping work.

The Committee remains convinced that this period of time is enough for payment to be completed to the creditor or be placed in the DTA. The onus is clearly placed on the defaulting party to rectify the payment situation or to negotiate for extended terms directly with the other party.

Any extension in payment terms should be in writing. If the payment terms extend the period of time available to deposit monies into the DTA, the adjudicator and BRA should be notified.

It should be noted that a party is not entitled to suspend work if they have received a notice of *Intent to Litigate* or a notice to pursue alternative dispute resolution options outlined in the contract, or if there is evidence that an adjudicators payment order has been deposited into a DTA.

Note: The express terms in a written contract can document additional circumstances for the issue of a *Notice of intent to suspend work*. However, express terms cannot exclude the 3 circumstances specified in the Code nor increase the length of notice required.

5.4.7 Recommendations

- The Committee recommends that all written contracts include the following general terms:
  - all parties Registered Entity registration number;
  - detailed statement of scope of works to be performed;
  - the work completion date;
  - details of payment terms;
  - details of notification terms;
  - dispute resolution and/or adjudication terms; and
  - right to suspend work without penalty in three specified circumstances.

- The Committee recommends that legislation prohibit:
  - 'pay if paid' and 'pay when paid' contract clauses; and
  - "contracting out of the Code" contract clauses.

- The Committee recommends that in the event that a written contract for building work does not include minimum standard contractual terms, then the Code's terms for payment, notification, adjudication and suspension of work will be incorporated into the contract as implied terms.

- The Committee recommends that a 14 day payment term, (from receipt of invoice), be required by the Code to operate as an implied term in the event that a written contract does not expressly stipulate payment terms.

- The Committee recommends that a 7 day statutory notification term, from the receipt of invoice or any subsequent notice, be required by the Code to be a non-excludable implied term in all written contracts for building work.

- The Committee recommends that a 7 day adjudication term, from the date of notice. be required by the Code to be a non-excludable implied term in all written contracts for building work.

- The Committee recommends that any variations:
  - be in writing; and
  - possess or refer to the basic terms and conditions of the main contract, unless these terms and conditions are specifically altered in the variation documentation.

- The Committee recommends that if a registered entity enters into an unwritten contract for building work there should be no be no minimum standard implied terms applicable to such contract and hence no protection from the proposed reforms.

- The Committee recommends that the Code require every written contract for building

work incorporate the Code's suspension of work terms as a non-excludable implied term.

- The Committee recommends that the right to issue a notice of *Intent to Suspend Work* **without penalty** be required by the Code to be a non excludable implied terms prescribed in every written contract for building work in three circumstances:

    1. In the event that payment to a creditor has been withheld, delayed and/or is incomplete beyond the due date without prior notice of Intent to Revise Payment.
    2. If either party fails to comply with an order issued by an adjudicator.
    3. If insolvency proceedings commence in relation to either party.

5.5 Adjudication Process

5.5.1 Standard Requirements

Adjudication is an integral component of the reforms proposed in this Report. The adjudication process will provide a fast, cost effective resolution of disputes between contractual parties at all levels of the construction chain.

Under the requirements of the Building Code of Conduct all contracts will require the inclusion of a non-excludable implied term specifying that any party to a contract may refer a dispute to an adjudicator after exchange of notifications.

After the BRA has been notified of a dispute, it would co-ordinate the process of nomination of an accredited adjudicator.

The arrangements for the appointment of an adjudicator would be subject to the following statutory requirements:

- that the adjudicator be independent, accredited by the BRA and be appointed by a body which is accredited by the BRA for nominating adjudicators;
- that the BRA be advised within seven days of the receipt of a notice of intent to revise payment; and
- that the adjudicator provide an adjudication order within seven days of being appointed.

5.5.2 Powers and Responsibilities of the Adjudicator

The adjudicator would have the power to request all relevant contract documents from both parties and may take the initiative in ascertaining the facts and the law in order to resolve the dispute.

The adjudicator would act impartially and avoid incurring unnecessary expense. Expenses incurred and charges for the adjudicator's services would be met jointly by the parties to the dispute. To compensate innocent parties for exaggerated or vexatious claims or unnecessary delays to the adjudication process, the adjudicator would be empowered to vary the allocation of charges and award costs of the adjudication only against the party at fault.

Under the terms of the Code, the adjudicator would be responsible for arranging an adjudication and providing a decision from the initial session within seven days of being appointed. This decision could be final by ordering the debtor to pay the creditor any monies which are found to be due and payable.

The decision may, however, be interim or provisional by ordering an amount of disputed monies to be placed into a DTA and providing the parties with a written summary of the dispute. Any written summary could then be used by the parties in pursuing litigation or other dispute resolution options in their contract.

If, at the end of the initial adjudication session there is no conclusive decision the parties to the dispute may opt to:

- continue with the adjudication process into a further session;
- utilise other dispute resolution processes in their contract (eg arbitration, expert determination or mediation);
- litigate in court or a Tribunal; or
- agree on a mutually acceptable settlement.

The decision of the adjudicator will be provided to both parties in writing and a copy will be provided to the BRA. The decision will specify the amount and date of any payment ordered. It will also record any breaches of the Code discovered in the process of the adjudication and any variation to the allocation of charges for the adjudicator's services.

In addition the adjudicator's orders can also specify if any of the building work is defective, if there is a requirement to undertake any rectification and if so by what date and the net result of any claims for set-off.

5.5.3 Enforcement of Adjudicators Decision

It is essential for the decision of the adjudicator to be enforceable.

The Committee, therefore, proposes that an adjudicators order, if not appealed within 7 days, be enforceable in a court of law.

This view was supported by the Institute of Arbitrators and Mediators [sub.5]:

> If the adjudication decision is not appealed, then it is essential that the

legislation contain enforcement provisions in similar terms to s33.(1) of the Commercial Arbitration Act 1984.

Section 33(1)(a) of Commercial Arbitration Act 1984 states:

> *"An adjudicator's decision made under the provisions of this Act may, by leave of the Court, be enforced in the same manner as a judgement or order of the Court to the same effect, and where leave is so given, judgement may be entered in terms of the adjudicator's decision."*

Either or both parties are able to use the adjudicator's Report in any subsequent dispute resolution or litigation.

5.5.4 Appointment of Adjudicators

As part of the inquiry, the Committee has held a number of briefings with professional bodies and organisations who currently offer arbitration or mediation services and whose members will, in all probability, comprise the majority of adjudicators. It is the Committee's impression, supported by participants at these meetings and a number of submissions, that there are sufficient experienced adjudicators currently working throughout New South Wales who would provide services to satisfy the demand.

The minimum standard contractual adjudication terms set out in the Code would outline:

- that the nomination of an impartial accredited adjudicator will be coordinated by the BRA; and
- that the adjudicator is to provide an adjudication order within 7 days of notification of the dispute.

The adjudicator's order is to be based on:

- information provided about the dispute,
- terms set out in the contract between the disputing parties, and
- any further material considered relevant to the resolution of the dispute.

If the adjudicator is unable to resolve the dispute within the seven days, an order is to be issued specifying the amount of money which must be placed into a DTA pending the resolution of the dispute. The options of concluding the adjudication or proceeding to a further stage are discussed in the next section.

The proposed time frame for the adjudication process is outlined in section 5.4.4 of this Report titled Adjudication Terms.

5.5.5 Sessional Structure

The Committee proposed the adoption of a sessional structure of fees according to the complexity of the dispute.

The sessional structure would classify disputes into three categories: standard, intermediate, and complex. Fee levels would be commensurate with the time required to complete the adjudication. The following indicative description and fee guidelines emerged from discussions with professional bodies.

Standard
A standard adjudication requiring preparation, arrangement, a site meeting or hearing of one to two hours duration and confirmation of decision would incur a standard fee in the vicinity of $500. It is envisaged most single trade disputes (eg. quality of works dispute) would be settled at the standard level.

Intermediate
An intermediate adjudication requiring preparation, arrangement, site meeting or hearing taking up to six hours duration and confirmation of decision would incur an intermediate fee in the vicinity of $1000. It is envisaged most multiple trade and contractual disputes would be settled at this intermediate level. It is proposed that the adjudicator would not go beyond this category of resolution without the approval of the parties to proceed.

Complex
Adjudication requiring more than six hours of site visit(s) and hearing time would be classified as a complex adjudication. An adjudication at this level may have unusual quality or contractual issues, which are not capable of resolution by direct inspection of the work or examination of the contract documentation.

In such instances, it would be necessary for the adjudicator to provide both parties with an estimate of the time anticipated and rate on which their fee would be based. It is envisaged that no monetary limit is placed on this category. It would be within the control of either party to the dispute to limit their expenditure when giving approval to proceed.

In complex adjudications, if either party does not agree to proceed the adjudicator will conclude the adjudication at the intermediate limit. The adjudication order will include instructions on what monies are to be deposited in a DTA, what alternative options the parties have for the subsequent resolution of their dispute and a summary of the position at which the adjudication was concluded.

Mr Arthur Krust, AMK Constructions Pty Limited [sub.2] in a submission to the Committee commented on the sessional structure proposal:

> The sessional structure is a good proposal to provide additional time and scope for the resolution of more complex disputes through the intermediate and

complex staged adjudications.

The Committee believes that the sessional structure will provide a framework within which adjudicators can provide the parties to a dispute with a timely determination and would quickly identify vexatious claims thereby minimising unnecessary delays to the adjudication process.

5.5.6 Limits on Adjudication

A number of submissions received by the Committee expressed concern that adjudicators could not adequately consider disputes concerning particularly complex issues or large amounts of money.

The Institute of Arbitrators and Mediators [sub.5] proposed that the adjudication process be capped at $75,000. This submission suggested that disputes concerning monies in excess of this amount are likely to be complex:

> ...involving substantive contractual issues and would require a special class of adjudicator...

The Australian Property Institute [sub.17] also hold the view that adjudication is not appropriate for more complex claims or disputes relating to large amounts. In particular the submission states that:

> the notification process outlined in Figure 3 of the Discussion Paper and the time period for provision of documentation is likely to be unworkable in complex matters.

Submissions were similarly concerned with the Committee's proposal that claims concerning disputed monies of less than $10,000 be heard in the Small Claims Division of the Local Court.

It is envisaged that, following an amendment to the Local Courts (Civic Claims) Act 1970 which would increase the Small Claims Division jurisdiction to $10,000, disputes within that jurisdiction could be heard in the Small Claims Division of the Local Court.

The Institute of Arbitrators and Mediators also called for the proposed provision of claims to be heard in the Small Claims Division be deleted as it was concerned that claims of up to $10,000 would be heard without any expert advice.

The Committee believes that adjudication must be an option for all parties in the contractual chain.

The Committee also believes that the Sessional Structure will provide an effective mechanism by which an adjudicator can readily determine their ability to resolve the dispute.

Under the process recommended by the Committee, an adjudicator hearing a complex claim which they believe is beyond the scope of adjudication, can order monies in to trust and prepare a report summarising the situation. This report can be used subsequently by either party in litigation or alternative dispute resolution processes provided in the contract.

As circumstances may arise where payment for a quantum of building work is the subject of a dispute at more than one interface in the contract chain, adjudicators may take into consideration the existence of other disputes and more particularly the existence of monies already in DTA's at other points in that contract chain.

5.5.7 Liability and Indemnity

The Committee believes that adjudicators should not be held liable for any part of the adjudication proceedings apart from liability for fraud.

This point of view was supported in the submission from A.M.K. Constructions Pty Ltd [sub.2] which stated:

> Legislation must indemnify adjudicators and their nominating bodies from subsequent Court proceedings, except in the case of fraud.

In a letter to the Committee dated 4 August, 1998, Mr G Markham, Chairman NSW Chapter of the Institute of Arbitrators and Mediators was also concerned about adjudicator liability.

> It is recommended that a clause similar to s.51 of the Commercial Arbitration Act be included in legislation. Such a clause would read:
>
> "An adjudicator is not liable for negligence in respect of anything done or omitted to be done by the Adjudicator in the capacity of Adjudicator but is liable for fraud in respect of anything done or omitted to be done in that capacity."

In addition the Committee believes that it is necessary to include provisions which ensure the adjudicator cannot be compelled to give evidence in any subsequent litigation or alternative dispute resolution process

5.5.8 Conclusions

Adjudication is an integral component of the reforms proposed in this Report.

The Committee envisages that the adjudication process will provide a fast, cost effective resolution of disputes. The Committee firmly believes that it is essential that all contractual parties at all levels of the construction chain have access to the adjudication process.

The Committee further believes that the adjudication and nomination procedures proposed will ensure independent and impartial adjudication by experienced adjudicators. Strict guidelines will provide for complex situations in which an adjudicator is unably to make a decision within the prescribed time. In addition, the Committee understands from professional bodies currently providing adjudicators that there are sufficient adjudicators working throughout New South Wales to satisfy the demand.

5.5.9 Recommendations

- The Committee recommends that the BRA be responsible for the development and maintenance of an accredited network of appropriately qualified adjudicators and accredited professional bodies and institutes.

- The Committee recommends that the appointment of an adjudicator be subject to the following statutory requirements (which would operate as non-excludable implied terms in every written contract for building works covered by the Code) :
  - that the adjudicator be independent, accredited by the BRA and be appointed by a body which is accredited by the BRA for the nomination of adjudicators.
  - that the BRA be advised within 7 days of the notice of *Intent to Revise Payment*.
  - that the adjudicator provide an adjudication order within 7 days of being appointed.

- The Committee recommends that an adjudicators order, if not appealed within 7 days be enforceable in a court of law.

- The Committee recommends that the Code adopt of a sessional structure of fees according to the complexity of the dispute. The sessional structure would be classified into 3 categories: standard, intermediate and complex.

- The Committee recommends that adjudicators not be held liable in respect of anything done or omitted to be done during any part of the adjudication proceedings apart from liability for fraud.

- The Committee recommends that legislative provisions be implemented which ensure that the adjudicator cannot be subpoenaed to provide evidence in any subsequent litigation or alternative dispute resolution process.

5.6 Designated Trust Account

5.6.1 Introduction

One of the key thrusts of the security of payment reforms proposed by the Committee is the requirement for all registered entities to establish a designated trust account (DTA).

As outlined in the Discussion Paper, the Committee has proposed that a DTA be used for the lodgement of monies following an adjudication or the receipt of an attachment order. Subsequent certification of the deposit would provide the creditor and the BRA with evidence that the debtor is not withholding monies.

It should be noted that monies can only be lodged into a DTA by a debtor subject to:

- monies in dispute being due and payable under the conditions of the contract; and
- the adjudicator specifying the amount to be paid or placed into trust.

5.6.2 Operation of the Trust

On receipt of a notice of *Intent to Revise Payment* from the debtor, the creditor has the option to issue a *Notice Requiring Adjudication*.

Under the provisions of the Code, the adjudicator must determine if there are any monies which are due and when they are payable by the end of the initial consultation. If the adjudicator is unable to issue a final decision, he/she must determine the extent of monies to be lodged in the DTA. These monies will remain in the DTA until the matter is resolved by the adjudicator's final order, or by subsequent dispute resolution or litigation.

This reform proposal allows for either party to issue a notice of *Intent to Litigate* within 7 days of the adjudicator's decision. As a prerequisite to proceeding with litigation or any other dispute resolution process, monies ordered to be paid by the adjudicator must be placed into the DTA.

If, after 7 days, the adjudicator's decision has not been appealed, there is provision for the adjudicator's order to be enforced by leave of the Court, in the same manner as a judgement or order of the Court. (Refer section 5.5)

This issue received some attention due to the time frame within which the debtor must respond. As was noted by Mr Geoff Markham - Institute of Arbitrators and Mediators Australia [sub.5]:

> When an adjudicator orders that monies be placed into a DTA, it is really not possible for this to be done immediately. Many projects are funded by a lending authority on a 'cost to completion basis' and a contractor may have to borrow funds. A fourteen day period would be more reasonable.

The Committee acknowledges that in certain circumstances immediate payment into the trust will be impractical. In such instances, the adjudicator can provide a discretionary judgement as to the time frame either for payment to the creditor or lodgement of monies into the DTA.

In the event of a vexatious claim or an unreasonable basis for declining to either pay monies owed or to lodge such monies into the DTA, the adjudicator is empowered to find that either

party has acted in bad faith and record such a finding in his/her decision. Such a finding would be regarded as a breach of the Code and recorded by the BRA.

5.6.3 Use of Bank Guarantees/Insurance Bonds

In the Discussion Paper, the Committee queried whether bank guarantees should be considered as a substitute for monies in trust. This issue was addressed in the majority of submissions with those opposed and in favour of using bank guarantees equally distributed.

The main argument of those opposed to the use of bank guarantees focussed on the 'trust' element of having monies in a DTA. This aspect was broached by Mr Frank Featherstone - Citycover (Aust) Pty Ltd [sub.3] who noted:

> We do not consider that Bank Guarantees should be considered as substitutes for monies in trust...monies in trust denotes a professional approach, makes it clear that there is a 'trust' element involved and also makes it clear that amounts concerned are someone else's money.

The use of bank guarantees was also opposed by Mr Ken Hinds - Australasian Dispute Centre [sub.11]:

> As to bank guarantees being considered for monies in trust - we cannot see this working as our experience with bank guarantees are that they are subject to manipulation and injunctions if a bank guarantee is called upon...certainty is needed and therefore cash security is really the best option.

Those in favour of the use of banking guarantees argued that the provision of security of any sort should be sufficient. This point was supported by Mr Michael Collins - Australian Property Institute [sub.17] who noted:

> Provision of adequate security of any sort (whether by way of an unconditional undertaking from a financial institution or a parent guarantee or charge) should be sufficient.

Support for both bank guarantees and insurance bonds was received from Mr Craig Long - Civil Contractors Federation [sub.25] who stated:

> The Civil Contractors Federation believes that unconditional bank guarantees and insurance bonds should be considered as substitutes for monies in trust.

The Committee is of the opinion that a flexible approach must be taken with regard to obtaining security for monies in dispute. It is therefore proposed that the use of unconditional undertakings such as bank guarantees and insurance bonds be allowed for the purpose of securing any monies in dispute.

5.6.4 Trustee Requirements

It was proposed in the Discussion Paper that any registered entity required to deposit monies into a DTA would also act as the trustee. As such, the registered entity would be responsible for disbursements from the DTA in accordance with the payment orders issued by the adjudicator or by subsequent dispute resolution or litigation.

A number of submissions to the Committee detailed concerns over a registered entity acting as trustee. The majority of these submissions suggested that it would be preferable to have a third party administering the DTA. This concept was expanded on by the Specialist Contractor's submission [sub.22] which stated:

> Monies ordered into trust should be held by the BRA. This would ensure that the authority is aware of progress in the dispute and the money is secure.

The Committee, while recognising the potential benefits of an independent trustee, was not convinced that a separate entity should be considered as it has not been established that there is a need to transfer control from the registered entity. It is anticipated that the trustee will be required to provide the other party and the BRA with evidence that any monies in dispute have been segregated by a deposit into a special purpose trust account or by the provision of unconditional security.

In addition, the trustee will also be held accountable for any delay in depositing monies due and payable into the DTA without a proper basis for such a delay. Such an act will be considered to be an act of bad faith and as such, a breach of the Code.

The Committee believes that a failure by a registered entity to deposit monies into a DTA as ordered is a serious breach of the Code. As a first offence, such a serious breach warrants the issuing of a demand by the BRA for a certification of solvency to be signed by the entities Principals and Chief Financial Officer.

Any subsequent breaches of this type could result in the BRA demanding an independent certification of solvency if there is no satisfactory explanation of the entities actions.

5.6.5 Recommendations

- The Committee recommends that a designated trust account be used for the lodgement of monies following an adjudication or the receipt of an attachment order.

- The Committee recommends that in the event that either party notifies their intent to litigate or to use other dispute resolution clauses specified as stated in the contract, all monies ordered for payment by the adjudicator are to be placed into a designated trust account as a prerequisite to proceeding.

- The Committee recommends that the use of unconditional undertakings, such as bank guarantees and insurance bonds, be allowed for the purpose of securing monies in dispute.

- The Committee recommends that any registered entity required to deposit monies into a designated trust account also act as the trustee.

- The Committee recommends that failure by a registered entity to deposit monies into a designated trust account as ordered, warrants the issuing of a demand by the BRA for a certification of solvency to be signed by the entities' Principals and Chief Financial Officer on the first offence. Any subsequent breaches of this type could result in the BRA demanding an independent certification of solvency.

5.7 Mandatory Security of Payment Insurance

5.7.1 Introduction

The segment of the Discussion Paper which attracted the most divergent responses was the proposal regarding the introduction of mandatory insurance.

This initiative aims to provide a safety net for all parties who have a contract for work on a building site including subcontractors, material suppliers and services providers such as architects, engineers, and quantity surveyors.

The Discussion Paper proposed that all registered entities be required to take out Mandatory Security of Payment Insurance (MSPI) to guarantee the payment of subcontractors and suppliers in the event of the registered entities' insolvency. This would be a precondition to signing any building contract.

It has been proposed that the requirement to hold mandatory insurance would initially be delayed during the implementation of other measures proposed by the Committee and then phased in over a period of a further two years. The MSPI would initially be introduced for registered entities entering contracts exceeding $5 million. The threshold would then be lowered to include contracts exceeding $1 million before being extended to include all contracts.

The phased introduction of the MSPI would give the insurance industry time to develop appropriate products and premiums, and to give registered entities time to determine the insurers requirements and, where necessary, restructure their capital to meet projected requirements.

While Government work is subject to all the provisions of the proposed reform, it is proposed that the Government, as the principal on a building project, would not be required to register

or hold security of payment insurance. However, MSPI would be required for all other registered entities in that contractual chain on a Government building project.

5.7.2 Cost to the Industry

A number of submissions expressed concern regarding the cost of mandatory insurance to the industry. In particular, submissions including that of the Australian Industry Group [sub.12] and the Australian Constructors Association [sub.13] called for the scheme to be properly analysed and costed prior to further development.

While the Committee acknowledges the difficulty of assessing the potential costs to the industry in the absence of data, it remains in favour of mandatory insurance.

In discussion with insurance industry representatives the absence of data for the assessment of risk was reaffirmed and the Committee's enquiries have yielded only anecdotal information since it was first highlighted as an industry problem during the Royal Commission into Productivity in the Building Industry in New South Wales in 1991/2.

Despite these concerns, the Committee proposes that legislation for the introduction of mandatory security of payment insurance be pursued.

A number of submissions were supportive of the concept of mandatory insurance as a means for ensuring security of payment in the industry and the success of the reforms overall.

In order to adequately assess the impact of mandatory insurance to the industry, the Committee recommends that legislation for the introduction of mandatory insurance be delayed until the relevant Minister is satisfied that the scheme is feasible and that the costs to the industry are not prohibitive.

The Committee proposes that a working party be established for this purpose and that its report be referred back to this Committee or another relevant Committee of the Parliament.

5.7.3 Current Measures

During the course of the inquiry the HIA Insurance Services representatives advised the Committee that the Security of Payment Bond currently available through HIA, had a potential to attract reduced quotations for building work from subcontractors who would recognise the increased security from dealing with contractors having such a bond. The Security of Payment Bond is currently the only product available.

This bond has published a premium range from .185 per cent to .305 per cent of the contract value. In the event of insolvency it provides reimbursement of 80% of any debt less an excess of $1000. The Committee considers that this Bond represents a minimum level of benefits, which should be available from the mandatory insurance scheme.

The Committee has been satisfied that in the event of the introduction of mandatory insurance there will be sufficient interest from insurers to establish a competitive market. Submissions to the Committee have outlined the position these insurers would adopt to the establishment of solvency criteria and acknowledge that premiums will be a critical factor in the financial feasibility of the scheme.

The payment behaviour of the registered entities in the industry which will now be under continuous scrutiny will provide the other information required for this assessment.

5.7.4 Phasing of MSPI

The submissions received also varied significantly in their responses to the phasing of the introduction. There was certainly no consensus position and there is no compelling reason why the phasing should not be varied from the sequence suggested in the Discussion Paper if there is a sound basis.

The suggestion put by FAI Insurance and the Specialist Contractors that after the initial delay of one year that all contracts become subject to mandatory insurance has some attraction. The capacity of the industry to cope with a surge such as this would be more evident to the working party reporting on the feasibility of the scheme and they should be free to recommend an alternative.

In the absence of a clear consensus the Committee's recommendation on phasing the introduction of mandatory insurance will remain unchanged.

5.7.5 Conclusions

The Committee proposes that all registered entities be required to take out Mandatory Security of Payment Insurance (MSPI) to guarantee the payment of all parties who have a contract for building work on a site including subcontractors, material suppliers and other service providers in the event of contractor insolvency.

The Committee is acutely conscious of the importance of a competitive and cost effective mandatory insurance scheme to the long term effectiveness of this package of reforms. It has registered the concerns of industry about the absence of costings and actuarial assessments of such a proposal. It is appreciated that Insurers will be able to determine appropriate premium levels only after an assessment of the changed behaviour resulting from these reforms.

With this concern uppermost the Committee has recommended a delay to the introduction of MSPI and a requirement for the Minister to receive a satisfactory assessment by an industry party of the financial feasibility. It is also recommended that the assessment of the working party be referred to this Committee or a relevant Committee of the Parliament for its review and advice to the Minister.

The Committee believes that if implemented, the MSPI will provide added assurance for the continuity of payments to employees of all organisations.

5.7.6 Recommendations

- The Committee recommends that all registered entities who contract be required to take out mandatory security of payment insurance to ensure the payment of all parties who have a contract for building work on a site.

- The Committee recommends that legislation for the introduction of mandatory security of payment insurance only be implemented after receipt by the Minister of a satisfactory assessment from an industry working party advising on the feasibility of the scheme.

  It is further recommended that the assessment of the working party be referred to this Committee or another relevant Committee of the Parliament for its review and advice to the Minister.

- The Committee recommends that, if introduced, mandatory security of payment insurance be deferred for a period of 12 months.

- The Committee recommends that the implementation of mandatory security of payment insurance then be phased in over a further period of 2 years commencing with contracts exceeding $5 million. This contract limit would be reduced after 12 months to $1 million and then eliminated so that mandatory security of payment insurance would apply to all contracts.

6 Implementation of Reforms

The Department of Public Works and Services has been responsible for the policy formation on Security of Payment for a number of years.

The Committee envisages that the Minister for Public Works and Services would be responsible for the introduction of new or amended legislation. Further, the Department would be tasked with implementing, administering and auspicing the legislation and overseeing any new agency such as the BRA.

The Committee envisages that the BRA would operate as a co-ordinating body for the reforms outlined in this Report. The BRA would be responsible for registration of building entities; collation of dispute data; administration of the Code and administration of the adjudication network.

Department of Fair Trading's Residential Building Licencing database is to be utilised as the basis of the Building Registration Information System (BRIS). The Department of Fair Trading and the BRA would establish mutually accessible information systems and may even consider providing seamless information services to the building industry on behalf of both agencies.

The Discussion Paper proposed that all contractors, who currently hold Residential Building Licences and owner-builders issued with a permit would automatically be registered by the BRA. The need for a separate registration and license would be removed. The Committee endorses this principle but recognises there may need to be some increase in the combined fee to assist with funding of services.

The Committee anticipates that once established the BRA would function in a cost neutral capacity with registration fees covering operational costs.

6.1 Recommendations

- The Committee recommends that the Minister for Public Works and Services be responsible for the introduction of new or amended legislation providing for security of payment reforms proposed in this document.

- The Committee recommends that the Department of Public Works and Services be responsible for the implementation, administration and auspicing the legislation and overseeing any new agencies such as the Building Registration Authority (BRA).

- The Committee recommends that a BRA be established to operate as the coordinating body for the security of payment reforms outlined in this

Report.

- The Committee recommends that the BRA monitor industry behaviour and breaches of the Building Code of Conduct.

- The Committee recommends that the Building Code of Conduct incorporate minimum standard contract terms covering payment, notification, dispute resolution and suspension of work which would operate as implied terms if they were not expressly contained in the contract for building work.

List of Participants

The following participants provided the Committee with expert comments and advice on the detail of the security of payment reforms.

- AON Corporate Risk Services
- Association of Consulting Engineers Australia
- Attorney General's Department
- Australian Bankers Association
- Australian Constructors Association
- Australian Institute of Banking
- Australian Institute of Quantity Surveyors
- Australian Finance Conference
- Australian Pre-mixed Concrete Association
- Australian Property Institute
- Australian Securities Commission
- Brookvale Insurance Brokers Pty Ltd
- Building Industry Specialist Contractors Organisation
- Chubb Insurance Company of Australia Ltd
- Construction Forestry Mining Energy Union (Construction Division)
- Construction Payments Group;
- Construction Policy Steering Committee
- Department of Fair Trading
- Department of Public Works and Services
- FAI Insurance
- GIO Insurance
- HIH Winterthur Insurance
- Housing Industry Association
- Jardine Australian Insurance Brokers Pty Ltd
- Insurance Council of Australia
- Institute of Arbitrators and Mediators Australia
- Master Builders Association
- MMI Insurance Group
- Multiplex Constructions
- Master Plumbers Association
- National Electrical Contractors Association
- NSW Security of Payments Committee
- Property Council of Australia
- QBF Trade Indemnity Ltd
- Royal Australian Institute of Architects
- Sedgwick Ltd
- Zurich Australia Insurance Ltd

List of Submissions

1. Mr Mark Olifinsky (Brookvale Insurance Brokers Pty Ltd).
2. Mr Arthur Krust (AMK Constructions Pty Ltd).
3. Mr Frank Featherstone (Citycover 'Aust' Pty Ltd).
4. Mr Peter Foster (Jardine Australia Insurance Brokers Pty Ltd).
5. Mr Geoff Markham (The Institute of Arbitrators & Mediators Australia)
6. Mr Martyn Chapman (The Royal Australian Institute of Architects)
7. Mr Roy Amos (Chubb Insurance Company of Australia Limited)
8. Mr Bob Moroney (Sedgwick Limited)
9. Brett Jenik (Roswell Constructions)
10. Tony Glambedakis (Subcontractor)
11. Mr Ken Hinds (Australasian Dispute Centre)
12. Jim Barrett (Australian Constructors Association)
13. David Whiting (Australian Industry Group)
14. Mr Peter Merity (Building and Construction Lawyer).
15. Mr Robert Jochelson (Australian Corporate Reporting).
16. Mr Sandro Spinetti (Australian Institute of Quantity Surveyors).
17. Mr Michael Collins (Australian Property Institute).
18. Mr Ken Ware (GM, Austruc Constructions Pty Ltd).
19. Mr Ian Gilbert(Director, Australian Bankers Association).
20. Ms N A Sherman (Director S Monkel Pty Ltd).
21. Mr Trevor Stinton (FAI General Insurance Co Ltd).

22. Mr Greg Brown (Group DMD, HIH Insurance).

23. Mr Sam Wilson (Principal Construction and Contract Services Pty Ltd).

24. Mr I Warren et al (Specialist Contractors including CPG and BISCOA).

25. Mr Craig Loug (Executive Director, Civil Contractors Association).

26. Ms E Crouch (Regional Director Housing Industry Association).

27. Mr Ivan Haege and Mr D Armstrong on behalf of (NSW Security of Payment Committee SPC)

28. Mr Paul Crittenden MP

29. Mr S Edwards (Australian Finance conference)

30. Mr I Widdup (Multiplex Constructions (NSW) Pty Ltd)

31. Construction Policy Steering Committee

Proceedings of the Committee

The Proceedings of the Committee for the Report on Security of Payment for the New South Wales Building Industry include minutes of all meetings.

The minutes of the Committee meetings 10-11 follow.

Minutes of Meeting No. 10 - Wednesday, 24 June 1998 At 4.30pm

1. Members Present:
Hon E Obeid MLC (Chairman), Hon J Schipp MP, Mr J Hunter MP, Mr J Tripodi MP, Mr J Watkins MP, Mr T Windsor MP

2. Apologies:
Hon R Jones MLC, Hon M Kersten MLC, Ms R Meagher MP

3. Confirmation of Minutes
Resolved on the motion of Mr Schipp and seconded by Mr Windsor that the minutes of the meeting held on 7 May 1998 be adopted by the Committee.

4. Overseas Study Tour
The Director noted that correspondence was received from the Speaker informing the Chairman that the Committee's proposed study tour has not been approved.

Discussion ensued in relation to a possible study tour to New Zealand to look at small business innovations.

Resolved, on the motion of Mr Hunter and seconded by Mr Schipp, that the Director research small business initiatives in New Zealand and other jurisdictions relevant to the operations of the Committee.

5. *Retail Tenancy Inquiry*
Discussion ensued regarding the Committee's advertisement calling for submissions for the Inquiry into Retail Tenancy.

Mr Hunter noted the National Retail Tenancy Code Inquiry by the Senate Economics References Committee and asked whether the Committee had contacted other states as to any developments.

Mr Schipp requested that the Secretariat find out if and when the Senate Committee would be holding hearings in Sydney and possible attendance by the Small Business Committee at these hearings.

Resolution to Call for Submissions
Resolved, on the motion of Mr Windsor and seconded Mr Tripodi, that the Committee agree to place advertisements in the Sydney Morning Herald and a selection of regional newspapers announcing its inquiry into retail tenancy and calling for public submission and comment.

Resolved, on the motion of Mr Hunter and seconded Mr Tripodi, that the Director distribute to Members a summary of all submissions received and a decision then be made on whether further consultation by way of public or in-camera hearing is required.

Distribution of Submission List
Discussion ensued as to whether Members would be sent a complete or abbreviated copy of all submissions.

It was decided that the Secretariat summarise all submissions and the summation be sent to Members.

Acceptance of late Submissions
Resolved, on the motion of Mr Hunter and seconded Mr Tripodi, that the Committee accept late submissions to the Retail Tenancy Inquiry.

6. Security of Payments for Subcontractors Inquiry
The Chairman asked the director to provide Members with a background to the inquiry and to the sub-committee developments to date.

Discussion ensued.

Proposed Model
The Director outlined the workings of the security of payment model developed by the sub-committee for Members.

Members questioned how the model would work in a number of scenarios in the construction industry.

Discussion ensued as to whether the model should be tabled by the Committee or should be released as a Discussion paper for industry comment.

Resolved, on the motion of Mr Hunter and seconded Mr Schipp, that the Security of Payments Proposed Model as revised be included in a Discussion Paper to be tabled in the Parliament and circulated to relevant industry bodies and their representatives for their comment and submission to the Committee and that a preamble be included in the discussion paper outlining the Committee's activities resulting in the production of a Discussion paper.

That in the Discussion paper there is a reference to a Background paper summarising the sub-committees inquiries into the deemed trust proposal which would be tabled and issued for information.

Resolved, on the motion of Mr Hunter and seconded Mr Schipp that any editorial changes to the Discussion paper be made by the Secretariat prior to tabling.

Mr Schipp raised the possibility of the Committee inquiring into the security of small business premises. Discussion ensued.

7. Amendment to the Committee's Terms of Reference

Mr Gonye (Clerk Assistant) advised the Chairman that the Committee's Terms of Reference were to be amended as requested to enable reports to be tabled in the Legislative Council out of session.

8. General Business

There was no other business.

9. Next Meeting

To be advised.

The meeting closed at 6.55pm

Minutes of Meeting No. 11 - Tuesday, 22 September 1998 At 4pm

1. Members Present:

Hon E Obeid MLC (Chairman), Hon J Schipp MP, Hon M Kersten MLC, Hon R Jones MLC, Mr J Tripodi MP, Mr J Watkins MP, Mr T Windsor MP

2. Apologies:

Mr J Hunter MP, Mr R Meagher MP

3. Confirmation of Minutes

Resolved on the motion of Mr Watkins and seconded by Mr Schipp that the minutes of 24 June 1998 be adopted by the Committee.

4. Matters Arising

New Zealand Small Business

The Director provided an overview of small business programs which are currently operating in New Zealand. Programs of interest include: Mentoring Program, Be Your Own Boss, Business Grow Program.

It was raised by Mr Schipp that a visit to New Zealand to view these programs in operation may be worthwhile for the Committee. Any study tor could focus on the effects of the GST and the cost of operating small businesses and take in national, regional and local initiatives.

Discussion ensued.

Resolved on the motion of Mr Schipp and seconded Mr Jones that, the Director will canvass dates for a study tour to New Zealand with members and will gain approval from the Speaker after such dates have been finalised.

5. Retail Tenancy

Director provided an overview of the submissions received by the Committee and outlined that due to the contentious nature of some information, a number of submissions had asked for confidentiality.

Mr Schipp stated that security for retailers was a major problem. Apologised that Mr Graham Parnell had not been in touch with the Director on this issue. Director stated that he would continue to try and contact Mr Parnell.

Mr Kersten mentioned that over shopping was a concern. The continued expansion of shopping centres and major retailers has made it economically impossible for small businesses to survive.

It was noted that US legislation does exist to prevent the continued development of shopping centres to ensure that over shopping does not occur.

Debate ensued.

6. Security of Payment

Discussion Paper

Chairman stated that the Discussion Paper was tabled out of session.

Background Paper

Chairman stated that the Background Paper was tabled out of session.

Advertising

Resolved on the motion of Mr Kersten and seconded Mr Schipp, that the Committee agree to placed advertisements in the Sydney Morning Herald and a selection of local and ethnic papers calling for submissions and comments on the Discussion Paper.

Consideration of Draft Report

Chairman provided an overview of the Report.

Debate ensued over the merits of the Report.

Mr Tripodi stated that the relationship between the client/principal and the contractor needed to have a dispute mechanism similar to the adjudication system.

It was agreed that there should be no legislation for mandatory security of payment insurance until the Minister and Working Party were convinced of the merits of the scheme.

The Committee discussed the cost implications of the proposal including the cost of registration. The Chairman advised that the cost of registration was likely to be similar to that currently charged by the Department of Fair Trading for licensing of residential building and that those builders already licences would only pay a nominal surcharge.

A number of members questioned the decision to exclude civil contractors with specific reference to the submission from Mr Paul Crittenden MP.

Director outlined that the civil side of the industry was comprised of approximately 85% of government contact work. If civil contractors were included the size of contracts in this part of the industry would mean large premiums because of the possible consequences of a major contractor becoming insolvent. This cost would eventually be passed back to the principal/client - the government.

The Chairman noted that it may be possible for private civil contractors to be registered at a later date.

Mr Tripodi stated that he believed that for the reforms to be effective, the industry must be on a level playing field ie reforms must include government. Mr Obeid agreed that an open ended section could be included within the Report stating that extending the reforms to civil contractors is something worth considering.

Resolved on the motion of Mr Tripodi and seconded Mr Kersten, that the Draft Report as amended be accepted by the Committee and tabled in both Houses of Parliament.

Resolved on the motion of Mr Schipp and seconded Mr Tripodi, that the specialist advisor assist the Committee and recommend changes to the text of the Report as amended to clarify legislative recommendations and legal and technical terminology which is used.

Resolved on the motion of Mr Kersten and seconded Mr Schipp, that the secretariat make any editorial and typographical changes to the Report as amended prior to tabling.

7. *Other Business*
There was no other business.

8. Next Meeting
To be advised.
Meeting closed 5.37pm.