

Improved Security of Payment Legislation and Project Bank Accounts: A Joint Solution to Payment and Insolvency Issues in the Construction Industry?

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Abstract

The Australian construction industry accounts for approximately 10 per cent of the nation's gross domestic product, but is responsible for nearly a quarter of all insolvencies. News of major builders becoming insolvent and leaving many subcontractors unpaid for work completed is all too commonplace, and lengthy payment delays often result in the insolvency of smaller subcontractors. A key measure available to reduce payment issues is security of payment ('SOP') legislation which deals with payment times and processes, payment disputes, and mechanisms for resolving such disputes on an arguably level playing field. However, whilst current SOP measures assist in mitigating problems encountered by parties in payment disputes, they are perhaps too disparate and under-utilised by industry participants. The foregoing has not gone unnoticed; in 2015, the Senate Economics References Committee reported on insolvency in the construction industry, calling for nationalisation and reform to existing SOP regimes. It also recommended the use of project bank accounts ('PBAs') to facilitate more secure and transparent payments to contractors and subcontractors. This paper considers the payment issues prevalent in the construction industry before commenting on current SOP legislative regimes: why they are perhaps less effective than intended and recommendations for improvement. The focus then turns to explaining and analysing PBAs, and their potential benefits, reception and inclusion in Queensland's recently enacted *Building Industry Fairness (Security of Payment) Act 2017* (Qld).

Keywords

Construction Industry; Insolvency; Project Bank Accounts; Security of Payment; Subcontracting

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I INTRODUCTION

The Senate Economics References Committee produced a report in December 2015 entitled *'I Just Want to be Paid': Insolvency in the Australian Construction Industry* ('the Senate Report'),¹ which found that:

Businesses operating in the Australian building and construction industry face an unacceptably higher risk than any other stand-alone industry of either entering into insolvency themselves, or becoming the victim of insolvency further up the contracting chain.²

The Senate Report was considerable in scope and detail which in itself is arguably testament to the extent and nature of the problems faced by participants in Australia's construction industry. Furthermore, the Senate Report lamented the culture of non-payment of subcontractors that is pervasive in the construction industry,³ despite the legislative security of payment ('SOP') measures currently enacted in various Australian jurisdictions. The Senate Report made 44 recommendations, although this paper predominantly focuses on two major proposals, namely a uniform, national SOP legislative regime with a rapid adjudication process and a two-year trial of project bank accounts ('PBAs') on certain Commonwealth projects from July 2016.⁴

In addition to the Senate Report, the Australian Government's Department of Jobs and Small Business conducted a *Review of Security of Payment Laws* ('DJSB Review') in December 2017 which made 86 recommendations on this topic.⁵ The DJSB Review also called for improved, uniform SOP legislation and the use of PBAs throughout the contracting chain for projects over \$1 million.⁶

This paper provides an overview of the payment problems apparent in the construction industry, before exploring both the shortcomings and effectiveness of current SOP legislative regimes and examining recommendations for improvement. The paper then outlines the origin and characteristics of PBAs and assesses their use as a means of making security of payment more certain and transparent. Advantages and disadvantages of PBAs will be canvassed and criticisms will be raised and

¹ Senate Economics References Committee, Parliament of Australia, *'I Just Want to be Paid': Insolvency in the Australian Construction Industry* (2015).

² *Ibid* 13.

³ *Ibid*.

⁴ *Ibid* 13.

⁵ J Murray, 'Review of Security of Payment Laws' (Final Report, Department of Jobs and Small Business, December 2017).

⁶ *Ibid* 382.

addressed. Finally, the paper will examine the use of PBAs in Queensland's recently enacted *Building Industry Fairness (Security of Payment) Act*.⁷

II CONSTRUCTION INDUSTRY PAYMENTS AND INSOLVENCY: THE PROBLEM

Insolvency rates in the Australian construction industry are extremely high when compared to other industries, and the impact of a head contractor being unable to pay subcontractors for works completed (sometimes including a failure to return retention money held at project completion) and subsequently entering into external administration is tremendous.⁸ News reports of the collapse of tier one and tier two builders (large, often national or international builders) are far too common.⁹

A significant factor contributing to the incidence of small-scale subcontractor insolvency is payment delays. In 2017, the Australian Small Business and Family Enterprise Ombudsman ('ASBFEO') conducted a survey which indicated that one in five construction businesses had over \$100 000 in late payments owing to them.¹⁰

As briefly mentioned above, the Senate Report highlighted the payment issues experienced by participants in the Australian construction industry and made 44 recommendations surrounding possible manners of overcoming these high payment delay and insolvency rates.¹¹ Importantly, the Senate Report emphasised that:

...there is one principle and one principle only that should be observed in relation to security of payment in the construction industry. It is a fundamental right of anyone who performs work in accordance with a contract to be paid without delay for the work they have done.¹²

Accordingly, the Senate Report made two major recommendations: firstly, that there be uniform, national legislation dealing with SOP and rapid dispute adjudication; and secondly, that PBAs be used in a two-year trial on projects where Commonwealth funding exceeded \$10 million.

⁷ *Building Industry Fairness (Security of Payment) Act 2017* (Qld).

⁸ See generally Australian Securities and Investment Commission ('ASIC'), *Insolvency Statistics - Series 3: External Administrator Reports* (2018) <<https://asic.gov.au/regulatory-resources/find-a-document/statistics/insolvency-statistics/insolvency-statistics-series-3-external-administrator-reports>>.

⁹ Emily Piesse, *Cooper & Oxley Placed in Administration as Subcontractors Assess Debts up to \$1 Million* (8 February 2018) ABC News <<http://www.abc.net.au/news/2018-02-08/wa-builder-cooper-and-oxley-placed-in-administration/9410034>>.

¹⁰ Australian Small Business and Family Enterprise Ombudsman ('ASBFEO'), 'Payment Times and Practices Inquiry - Working Paper 3' (Working Paper No 3, 2017).

¹¹ Senate Economics References Committee, above n 1.

¹² *Ibid* 169.

Furthermore, if successful in trials, it was posited that PBAs should be legislatively described as best practice in the private sector.¹³

The extent of the insolvency problem evident within Australia's construction industry is emphasised by the fact that over the last decade, whilst the construction industry has accounted for approximately 10 percent of the nation's gross domestic product, it has simultaneously been responsible for approximately 25 per cent of all corporate insolvencies.¹⁴ A considerable proportion of these insolvencies resulted from inadequate cash flows.¹⁵ On this point, it is important to note that inadequate cash flows ranked as the highest cause of insolvency in the construction industry over the five-year period being 2009-2014.¹⁶ The Australian Securities and Investments Commission ('ASIC') reported that in this same period, 2009-2014, the construction industry had the third highest number of external administrator appointments of all industry sectors.¹⁷

The problem of construction insolvency is exacerbated by the structure of the industry wherein major projects are assigned to head contractors, who are not employees of owners or clients and who subsequently subcontract most, if not all, of the project work to specialist subcontractors. The ultimate effect of this is that the industry's market power becomes concentrated towards the top of the construction chain, which often results in the unfair treatment (particularly with regard to payment) of subcontractors, who are often terminated or bankrupted, or who withdraw and are easily replaced in the industry's extremely competitive market.¹⁸ In many cases, the market is competitive to the extent that subcontractors tender with little to no margin in expectation that variations in the work will arise to produce profits. In these cases, even the slightest payment delays cause major issues.¹⁹

Further, the pyramid-like structure of a construction contract chain usually means that terms between a client and head contractor will be passed down, 'back-to-back', to all subcontractors in the contract chain. Generally, any

¹³ Ibid xvii.

¹⁴ Ibid 16.

¹⁵ ASIC, 'ASIC Reports on Corporate Insolvencies 2015-16' (Media Release, 16-436MR, 14 December 2016) <<https://asic.gov.au/about-asic/media-centre/find-a-media-release/2016-releases/16-436mr-asic-reports-on-corporate-insolvencies-2015-16/>>; ASIC, 'Insolvency Statistics - Series 3 External Administrator Reports: July 2015 to June 2016' (2018) 6 <<https://download.asic.gov.au/media/4110162/2015-2016-asic-insolvency-statistics-series3-1.pdf>>.

¹⁶ Senate Economics References Committee, above n 1, 17.

¹⁷ Ibid; ASIC, Submission No 11 to Senate Economics References Committee, *Insolvency in the Australian Construction Industry*, April 2015, 3.

¹⁸ Senate Economics References Committee, above n 1, xx. See also Filipe Barbosa et al, *Reinventing Construction Through a Productivity Revolution* (February 2017) McKinsey & Company <<https://www.mckinsey.com/industries/capital-projects-and-infrastructure/our-insights/reinventing-construction-through-a-productivity-revolution>>.

¹⁹ Senate Economics References committee, above n 1, 21.

onerous provisions between a client and head contractor are similarly passed down, often to subcontractors which, because of their size and simplicity, cannot cope with the associated risks or mitigate against them.²⁰ As a result of complex payment processes and protracted payment times being passed down through the contracting chain, subcontractors near the bottom of the pecking order face tremendous cash flow pressure.

This lopsided concentration of power is widely lamented. In its preparation of the Senate Report, the Economics References Committee received numerous submissions from subcontractors, legal professionals, industry experts, unions, regulators, government departments and academics who were frequently critical of major construction head contractors (known as ‘tier one’ or ‘tier two’ constructors). However, the Australian Construction Association, which solely represents the largest tier one constructors in Australia, declined to make any submissions and the largest constructors themselves also did not contribute.²¹

The Senate Report further commented on the impact the biased nature of the construction industry and resultant insolvencies has on the business, finances, health and personal lives of subcontractors.²² Suicides are not uncommon in the industry – in 2015, a Western Australian businessman took his life after his business faced insolvency due to non-payment by a head contractor on a major Perth public works project.²³

The impact on the economy is also significant. The Senate Report relayed that ASIC figures for the construction industry in 2013-2014 documented a shortfall of liabilities over assets available to creditors in the range of \$1.6-2.7 billion.²⁴ Furthermore, in a risky environment where there is no certainty as to cash flow or even payment for work completed, it is unsurprising that investment and innovation are extremely low and that the construction industry is amongst the least innovative industries nationally.²⁵

The 2017 ASBFEO survey indicated that a high number of construction businesses had difficulties paying their wages and bills: 50 per cent reported that they were at risk of insolvency, 68 per cent indicated a heavy reliance on debt to continue operating, 74 per cent stated that payment issues were affecting their physical wellbeing and 88 per cent

²⁰ Murray, above n 5, 12.

²¹ Senate Economics References Committee, above n 1, 3.

²² *Ibid* xx.

²³ Jonathan Barrett, ‘Suicide Focuses Attention on John Holland and WA Subcontracting Laws’, *Financial Review* (online), 9 August 2015 <<http://www.afr.com/business/construction/suicide-focuses-attention-on-john-holland-and-wa-subcontracting-laws-20150806-gitc0i>>.

²⁴ Senate Economics References Committee, above n 1, xx.

²⁵ *Ibid* xxi.

acknowledged they had experienced adverse impacts on their mental wellbeing.²⁶

Unfortunately, whilst the current SOP legislative regimes existing in different Australian jurisdictions are well intentioned, they do not work effectively as they differ too widely and are often inaccessible to those most likely to benefit from them. Payment times in the Australian construction industry are, at the time of writing, the worst in the world with an average overdue time of 26.4 days. This is far longer than the second worst nation, Mexico, which experiences average payment delays of up to 18.6 days. Major world economies have late payment times of seven days or less, with many experiencing average *early* payments.²⁷

Payment problems in Australia are exacerbated by the fact that the construction industry remains a national industry that is regulated by piecemeal and differing methods across state borders with minimal uniformity.²⁸ It is therefore strongly suggested in the Senate Report that harmonised, national SOP legislation and the use of PBAs may significantly address many of the current issues faced.²⁹

Finally, apart from poor payment practices, factors such as inability to access sophisticated legal advice, lack of resources and expertise in contract negotiations, intense competition amongst subcontractors and fear of being excluded from future work add to the plight of lower-order subcontractors.³⁰

III SECURITY OF PAYMENTS LEGISLATION

Payment delays and disputes in the construction industry arise in relation to claims for payment for works completed, sometimes called ‘progress claims’, and the return of retention money at the end of a project or at the end of a defects liability period.

SOP legislation which is intended, amongst other things, to address or prevent payment issues in the construction industry currently exists in every Australian state and territory.³¹ Retention trust fund legislation is not

²⁶ ASBFEO, above n 10.

²⁷ Murray, above n 5, 14.

²⁸ See Matthew Bell, ‘Security of Payment: Can Victoria Offer Insights into the Re-shucked Oyster of Judicial Review?’ (2011) 27 *Building and Construction Law Journal* 36; Philip Marquet, ‘Judicial Review of Security of Payment Adjudications: Key Doctrinal Uncertainties and Proposals for Reform’ (2015) 31 *Building and Construction Law Journal* 4.

²⁹ Senate Economics References Committee, above n 1, xxiv.

³⁰ *Ibid* 19.

³¹ *Ibid* 121. In the Australian Capital Territory, see the *Building and Construction Industry (Security of Payment) Act 2009* (ACT). In New South Wales, see the *Building and Construction Industry Security of Payments Act 1999* (NSW). In the Northern Territory, see the *Construction Contracts (Security of Payments) Act 2004* (NT). In Queensland, see the

as pervasive, but has recently been enacted in New South Wales and partly in Western Australia and the Northern Territory. ‘Retention’ refers to money withheld, for example, from each payment by a contractor to a subcontractor as a guarantee of the subcontractor’s performance, or to be used if necessary to rectify any defective work of the subcontractor. Retention money withheld may be deposited into a trust account, particularly if required by legislation; however, it is often simply retained by the contractor, who benefits not only from the security derived from this arrangement but also in respect of their own cash flow. Typically, half of the retention money is returned to the subcontractor on the completion of a project and the other half at the end of a defects period which is generally twelve months in duration. Therefore, whilst payment disputes usually arise in relation to progress claims, they may also include claims involving retention money.

One of the main aims of SOP legislation is to provide for the relatively quick adjudication of payment disputes, especially in comparison to litigation, with the additional benefit of identifying companies in financial distress *before* they collapse and leave subcontractors unpaid for the work they have performed.³² Mr Robert Gaussen, Senior Adjudicator, Senior Mediator and previous Produce and Grocery Industry Ombudsman for the Australian Government, stated that:

The best early warning system you can have is speedy applications made under the security of payment legislation. If people are not being paid and they are making their applications quickly, you identify the signs. They are out there on the public record.³³

There are, however, differences between the various state regimes, resulting in the emergence of what might be called an ‘East Coast’ and a ‘West Coast’ model.³⁴ In relation to the ‘East Coast’ model, New South Wales, Victoria, Queensland, Tasmania, South Australia and the Australian Capital Territory use a replicated version of the *Building and Construction Industry (Security of Payment) Act 1999* (NSW).³⁵ The East Coast model features Acts that can override inconsistent contractual

Building Industry Fairness (Security of Payment) Act 2017 (Qld). In South Australia, see the *Building and Construction Industry Security of Payment Act 2009* (SA). In Victoria, see the *Building and Construction Industry Security of Payment Act 2002* (Vic). In Western Australia, see the *Construction Contracts Act 2004* (WA).

³² *Ibid.*

³³ Evidence to Senate Economics and References Committee, Parliament of Australia, Adelaide, 21 September 2015, 62.

³⁴ Senate Economics References Committee, above n 1, 122.

³⁵ See, eg, *Building and Construction Industry (Security of Payment) Act 1999* (NSW); *Building and Construction Industry (Security of Payment) Act 2002* (Vic); *Building and Construction Industry (Security of Payment) Act 2004* (Qld); *Building and Construction Industry (Security of Payment) Act 2009* (Tas); *Building and Construction Industry (Security of Payment) Act 2009* (SA); *Building and Construction Industry (Security of Payment) Act 2009* (ACT).

provisions and establish rapid adjudication systems where qualified adjudicators make prompt decisions on payment disputes that are enforceable through the courts as judgment debts. Some detractors have claimed that this creates a default entitlement to payment for the benefit of subcontractors; on balance, however this does not appear to be the case.³⁶ Key features of the East Coast model include interim payment regimes, a restriction of claims to claims for payment for work carried out pursuant to a construction contract, the use of a payment schedule by the recipient of a claim for setting out proposed payments, the requirement to submit reasons for non-payment of a claim and the referral of any dispute to fast track adjudication.³⁷

Both Western Australia and the Northern Territory adopt the West Coast model. Originally based on the United Kingdom model, its aims are similar to all state SOP legislation appearing in this field, particularly in relation to providing rapid adjudication processes. However, the Western Australian and Northern Territory legislative regimes operate quite differently in that they employ ‘a more simplistic approach that attempts not to interfere with the contractual rights and obligations of the parties to a construction contract’.³⁸ Effectively, this means that the West Coast models attempt to operate with reference to the actual contract between the parties rather than overriding contractual rights with statutory rights, as is arguably the case with respect to the East Coast models.³⁹ Other features of the West Coast models are their provision for interim payment regimes and for the ability of either party to make a claim for the performance or non-performance of obligations under a construction contract; a distinct mode of interaction with contracts between parties, which means that their provisions generally do not override those contained in contracts; and less restrictive dispute resolution procedures.⁴⁰

Further, to assist in the practice of resolving disputes with reference to the actual contract existing between the parties, the Western Australian and Northern Territory *Acts* prohibit certain provisions in construction contracts and imply provisions into contracts where they are otherwise silent.⁴¹ The West Coast models are also less restrictive on adjudicator appointments, submissions to adjudicators and the process by which an adjudicator reaches decision.⁴² The timeframes within which the aggrieved party can make claims and within which a liable party must pay

³⁶ Senate Economics References Committee, above n 1, 123.

³⁷ Murray, above n 5, 27.

³⁸ Senate Economics References Committee, above n 1, 125.

³⁹ Society of Construction Law Australia, *Report on Security of Payment and Adjudication in the Australian Construction Industry* (Report, February 2014) 15.

⁴⁰ Murray, above n 5, 27.

⁴¹ Senate Economics References Committee, above n 1, 125.

⁴² *Ibid* 126.

determined amounts range from as little as 10 business days to 90 business days.⁴³

SOP legislation is the subject of constant debate between industry participants, and regular review and amendment by the various state governments,⁴⁴ some of which is briefly discussed below. Whilst reviews and amendments across jurisdictions have improved payment practices, some problems still remain, including insolvencies at the top of the contractual chain, complex and confusing legislation, differing approaches and processes to adjudication, the imposition of unfair contract terms by parties with stronger bargaining power, intimidation and fear of retribution, and late payments.⁴⁵

In New South Wales the 2012 Collins Review into insolvency in the New South Wales construction industry called for shorter payment times,⁴⁶ the requirement that adjudicated payment amounts be paid into a trust,⁴⁷ increases to the powers and jurisdiction of adjudicators,⁴⁸ and more rigorous training for adjudicators.⁴⁹ In response, the New South Wales Government passed the *Building and Construction Security of Payment Amendment Act 2013* (NSW) which included prompt payment provisions,⁵⁰ a requirement that the head contractor give a statutory declaration to the principal that the head contractor has paid all of their subcontractors before the head contractor receives payment from the principal,⁵¹ and penalties for falsifying such declarations.⁵² However, the requirement to give a statutory declaration in this situation has been criticised as ‘putting the cart before the horse’ due to the fact that most of the time, the head contractor relies on payment from the principal *before* they are able to pay their own subcontractors.⁵³ Arguably, this is likely to increase, rather than decrease, insolvency rates as noted in the Supreme Courts of Victoria and Queensland.⁵⁴

⁴³ Ibid 127.

⁴⁴ See, eg, Rex Deighton-Smith, *Review of the Building and Construction Industry (Improving Productivity) Act 2016* (Report, Department of Jobs and Small Business, Australian Government, 4 April 2018).

⁴⁵ Murray, above n 5, xviii, xiv.

⁴⁶ Bruce Collins, ‘Independent Inquiry into Construction Industry Insolvency in NSW’ (Final Report, New South Wales Government, November 2012) recommendations 24, 29.

⁴⁷ Ibid recommendation 33.

⁴⁸ Ibid recommendation 39.

⁴⁹ Ibid recommendation 40.

⁵⁰ *Building and Construction Industry Security of Payment Amendment Act 2013* (NSW) [3].

⁵¹ Ibid [7].

⁵² Ibid [9].

⁵³ Evidence to Senate Economics References Committee, Parliament of Australia, Perth, 26 October 2015, 40.

⁵⁴ *BRB Modular Pty Ltd v AWX Constructions Pty Ltd* [2015] QSC 218, 16-34. See also *Westbourne Grammar School v Gemcan Constructions Pty Ltd* [2017] VSC 645.

In 2015, the New South Wales Government announced a review of its *Building and Construction Industry Security of Payments Act 1999* and sought discussion paper feedback on existing timeframes, processes, the use of PBAs and statutory trust accounts to cure problems within the construction industry. At the time of writing, this feedback is still under consideration.⁵⁵

In 2014, the Western Australian Government commissioned a review ('Evans Review') of its *Construction Contracts Act 2004* ('CCA').⁵⁶ In the final report, produced in 2015, reviewer Professor Philip Evans indicated that the CCA had been well received since its inception and was generally effective as a scheme for evaluating payment claims and resolving disputes.⁵⁷ Professor Evans noted that the CCA had likely resulted in improvements in contract administration and business practices, although not necessarily in the case of small contracting businesses.⁵⁸

Professor Evans opined that the main issue inherent within the SOP process was its under-utilisation by lower order subcontractors.⁵⁹ Indeed, it remains true that many subcontractors are simply unaware that such legislation and alternatives exist,⁶⁰ believing that their only options are often protracted contractual dispute resolution processes or litigation.⁶¹ Further, the majority of SOP legislation has only been in force for a relatively short period of time.

The Evans Review did not suggest significant structural amendments to the CCA and instead recommended that existing legislation – including provisions dealing with time limits for making claims,⁶² responding to claims,⁶³ making adjudications,⁶⁴ regulating adjudicators⁶⁵ and the prohibition of contracting out of the CCA – *not* be changed.⁶⁶

⁵⁵ Murray, above n 5, 30.

⁵⁶ Philip Evans, 'Statutory Review of the Construction Contracts Act 2004 (WA)' (Discussion Paper, Western Australian Building Commission, October 2014).

⁵⁷ Philip Evans, *Report on the Operation and Effectiveness of the Construction Contracts Act 2004 (WA)* (August 2015) 1 <https://www.commerce.wa.gov.au/sites/default/files/atoms/files/cca_review_report.pdf>.

⁵⁸ *Ibid.*

⁵⁹ Evidence to Senate Economics References Committee, Parliament of Australia, Perth, 26 October 2015 2.

⁶⁰ Andrew Wallace, *Payment Dispute Resolution in the Queensland Building and Construction Industry* (Final Report, Queensland Building and Construction Commission, May 2013).

⁶¹ Evans, above n 57, 91-93.

⁶² *Ibid.* 23.

⁶³ Evans, above n 57, 25.

⁶⁴ *Ibid.* 27.

⁶⁵ *Ibid.* 42, 45, 46, 63.

⁶⁶ *Ibid.* 97.

Following the Evans Review, the CCA was amended to include an increase of the time limit for making an application from 28 calendar days to 90 business days,⁶⁷ the ability to recycle rejected payment claims⁶⁸ and the ability for adjudicators to make decisions on disputes even where an applicant had failed to comply with all of the formal requirements.⁶⁹

The state of Queensland has been particularly active with its SOP legislation. In 2014, following a 2013 review on payment dispute resolution known as the Wallace Review, the Queensland Government made amendments to its *Building and Construction Industry (Security of Payment) Act 2014*. These amendments included a new process for appointing adjudicators and a dual model of adjudication for ‘simple’ and ‘complex’ payments, with a different timeframe for ‘complex’ applications.⁷⁰ Again, and importantly, in 2017, following further reviews in 2015 and 2016,⁷¹ the Queensland Government enacted the *Building Industry Fairness (Security of Payment) Act*,⁷² replacing its prior SOP legislation and calling for the use of PBAs, as discussed in further detail below.

Some jurisdictions such as New South Wales provide an additional avenue for seeking payment by permitting a process whereby subcontractors can ‘skip up the contractual chain’ and make claims for payment to the principal in cases where the contractor has failed to pay on time.⁷³ In Queensland, claims made under the *Subcontractor’s Charges Act 1974* resulted in the money claimed by subcontractors being taken out of circulation and charged for the benefit of the subcontractor.⁷⁴ However, these alternative avenues may often be more technical and featuring longer timeframes, and are sometimes an ‘either/or’ alternative to the SOP process, as is the case in Queensland.⁷⁵

In early 2017, the Australian Government’s Department of Jobs and Small Business commissioned a national review of SOP Laws (‘DJSB Review’) in the building and construction industry.⁷⁶ The issues paper in relation to the DJSB Review (‘Issues Paper’) acknowledged the shortcomings of the existing SOP regimes in Australia identified in the Senate Report, and stated that the aims of the DJSB Review included consolidating prior reviews and reports, consulting with various participants in the

⁶⁷ *Construction Contracts Act 2004* (WA) s 26(1).

⁶⁸ *Ibid* ss 3, 26(1).

⁶⁹ *Ibid* s 31(2)(ia).

⁷⁰ See *Building and Construction Industry Payment Amendment Act 2014* (Qld).

⁷¹ Murray, above n 5, 33.

⁷² See generally *Building Industry Fairness (Security of Payment) Act 2017* (Qld).

⁷³ *Contractors Debts Act 1997* (NSW) s 9.

⁷⁴ *Subcontractor’s Charges Act 1974* (Qld) s 5.

⁷⁵ Senate Economics References Committee, above n 1, 126.

⁷⁶ Murray, above n 5.

construction industry and making recommendations on overcoming these shortfalls.⁷⁷

The issues paper foreshadowed an examination by the DJSB Review of the SOP model adopted by Queensland prior to 2014.⁷⁸ However, Queensland's recently enacted *Building Industry Fairness (Security of Payment) Act 2017* (Qld) (discussed in further detail below) – which repealed and replaced both the *Building and Construction Industry Payments Act 2004* (Qld) and *Subcontractors' Charges Act 1974* (Qld) – leapfrogged the DJSB Review. Accordingly, the DJSB Review only considers Queensland's original Bill,⁷⁹ although such consideration would likely be the same in relation to the new Act.

The issues paper also indicated that the DJSB Review would consider statutory construction trusts and PBAs, and noted that the Queensland Government was about to introduce legislation requiring the use of PBAs for certain construction projects.⁸⁰ This is discussed further below.

The DJSB Review made numerous recommendations with respect to revising SOP legislation as a means of achieving legislative best practice and improving fairness amongst industry stakeholders. Chief amongst these recommendations is the uniform use of SOP legislation based on the East Coast model (notably New South Wales') and the use of statutory trusts and PBAs throughout the payment chain.⁸¹ The DJSB Review considered that any improvements to SOP legislation must firstly improve the cash flow of parties through prompt payment mechanisms. Secondly, adjudication processes needed to be more efficient, and finally, payments for progress claims should be held in trust for the benefit of the parties to whom they are due.⁸²

The DJSB Review undertook a comprehensive analysis of SOP legislation in the various jurisdictions as well as the many prior reviews into this legislation's effectiveness. Following a detailed examination of submissions by stakeholders and a discussion of the advantages and disadvantages of the East and West Coast models, the DJSB Review made some important recommendations, including that the most effective model in relation to prompt payment would be a modified East Coast model,⁸³ and that legislation should be drafted as simply as possible and not use a

⁷⁷ Murray, 'Review of Security of Payment Laws' (Issues Paper, Department of Employment, February 2017) 4.

⁷⁸ *Ibid* 3.

⁷⁹ Murray, above n 5, xiii.

⁸⁰ Murray, above n 77, 18.

⁸¹ Murray, above n 5.

⁸² *Ibid* xiv.

⁸³ *Ibid* recommendation 1.

two-tier system for simple and complex payments (although extensions of time could be granted for complex adjudications).⁸⁴

The DJSB Review also recommended a broader definition of 'construction work',⁸⁵ 'related goods and services',⁸⁶ and 'construction contract'.⁸⁷ In terms of adjudicating disputes the DJSB Review recommended generally, amongst other things, a period of 20 business days from the due date for payment to lodge an adjudication application,⁸⁸ a period of five business days within which to respond to an adjudication application⁸⁹ and a period of 10 business days, extendable to 30 business days, within which the adjudicator must make a decision.⁹⁰ Lastly, the DJSB Review recommended that there be a uniform approach to SOP legislation amongst the various Australian jurisdictions, or at least a greater consistency between them.⁹¹ The DJSB Review considered that this could be achieved by, for example, federal legislation via the constitutionally granted corporations power,⁹² although this power may arguably be limited, as it might not extend to the many unincorporated businesses in the construction industry.⁹³ A more feasible approach would be the use of mirror or 'harmonised' legislation which already occurs to some extent in the East and West Coast's respective models.

In comparison to the relatively generous time frames provided in the amended Western Australian Act, the model recommended by the DJSB Review appears to provide significantly shorter time periods within which a party may make an adjudication application, namely 20 business days compared to 90 business days. Arguably, one of the main factors contributing towards the reduced effectiveness of SOP adjudications is the minimal awareness small subcontractors have of their existence and the short time frames within which applications must be made.

This may especially be so where smaller contractors abide by protracted contractual dispute resolution processes in good faith before availing themselves of other dispute resolution avenues, often when they are well out of time to make an adjudication application. It could even be argued that more sophisticated parties may intentionally delay payments to small subcontractors by creating frivolous disputes, handled through lengthy contractual dispute resolution processes, to avoid potential adjudication

⁸⁴ Ibid recommendation 2.

⁸⁵ Ibid recommendation 4.

⁸⁶ Ibid recommendation 5.

⁸⁷ Ibid recommendation 6.

⁸⁸ Ibid recommendation 35.

⁸⁹ Ibid recommendation 39.

⁹⁰ Ibid recommendation 42.

⁹¹ Ibid 316.

⁹² *Commonwealth of Australia Constitution Act* s 51(xx).

⁹³ Murray, above n 5, 316.

applications and limit subcontractors to time-consuming and expensive litigation to recover payments instead.

Of course, the most important question is whether or not SOP regimes actually work. Evidence suggests that SOP regimes are effective due to their ‘quick, efficient, cheap, effective and fair’ handling of payment disputes.⁹⁴ However, it should also be noted that one of the most significant problems with the SOP regimes is that they do not really provide security of payment at all due to the fact that obtaining a judgment does not guarantee payment, especially when there are numerous instances of the contractor themselves being or becoming insolvent.⁹⁵ Arguably, even if national harmonisation of SOP legislation was achieved, it would remain unlikely to adequately address issues of non-payment when the principal or head contractor is, or becomes, insolvent.

In addition to the problem of insolvency, other problems that the Senate Report identified as being significant in relation to the current (and varied) SOP regime were that subcontractors could potentially face intimidation and retribution if they availed themselves of SOP assistance; that the cost of enforcement may still be prohibitive for small subcontractors; that there is a tremendous lack of awareness, education and support for subcontractors utilising SOP; that the appointment of adjudicators is often influenced by head contractors; and that the speed of adjudication remains slow.⁹⁶ These problems are exacerbated by the current, fragmented approach to SOP.

To be effective, any proposed SOP model must be consistent across various jurisdictions and have realistic timeframes that recognise the realities of the industry and the nature of participants therein. However, whilst appropriate, timely and efficient adjudication processes will undoubtedly assist in reducing the incidence of payment delays and insolvencies, consideration must also be given to measures that ensure the funds required to make payments are preserved for that purpose, and not freely disposed of by parties higher up the contracting chain prior to payment of contractors at the bottom end. One such measure that may assist in this regard is the use of statutory trusts or PBAs, which this paper will now proceed to discuss.

III PROJECT BANK ACCOUNTS

The overview of Australia’s various SOP regimes provided above highlights that the problem of non-payment to subcontractors remains

⁹⁴ Evidence to Senate Economics References Committee, Parliament of Australia, Adelaide, 21 September 2015, 58.

⁹⁵ Evidence to Senate Economics References Committee, Parliament of Australia, Canberra, 4 November 2015, 35.

⁹⁶ Senate Economics References Committee, above n 1, 135.

significant. Whilst methods for rapid adjudication and simple, effective and cheap processes are important, what is also required is a means to give more certainty and transparency to actual payments (and retentions).

SOP legislation has mainly focused on the right to progress payments and resolution of payment disputes; however, it does little to ensure that payments made higher up the contractual chain flow down to smaller subcontractors.⁹⁷ A statutory trust or PBA, in conjunction with SOP legislation, would be an effective solution to this problem. Since the vast majority of construction work is performed by subcontractors, many of whom are small businesses, arguably the best way to protect payments to these subcontractors is via cascading statutory trusts in the form of PBAs which secure payments to all subcontractors in the contractual chain for projects over \$1 million.⁹⁸

A PBA is a payment mechanism whereby contracting parties use a dedicated trust account to facilitate payments from the principal to the head contractor and any participating subcontractors.⁹⁹ PBAs can be utilised by agreement between the parties, a mandate provided by policy as is commonly observed with government contracts, or for statutory trusts prescribed by legislation.¹⁰⁰ The advantages of this payment arrangement are that subcontractors may be better protected against head contractors who often experience cash flow issues; that payments are more efficient and streamlined; and that there is greater transparency and accountability.¹⁰¹ Despite this, it should be noted that PBAs do not eliminate payment disputes or problems altogether *per se*; head contractors may still experience financial difficulties, contract disputes may still prolong payments and parties may still seek to resolve disputes or make claims through SOP processes or litigation.¹⁰² However, when using PBAs, progress payments and retention monies are held in trust, independent of the head contractor and principal. This provides greater security for

⁹⁷ Murray, above n 5, 291.

⁹⁸ Murray, above n 5, xxx.

⁹⁹ *Grocon Constructors (Victoria) Pty Ltd v APN DF2 Project 2 Pty Ltd* [2015] VSCA 190, 63. See also Department of Housing and Public Works, Government of Queensland, *Building Industry Fairness Reforms – Project Bank Accounts* (4 June 2018) <<http://www.hpw.qld.gov.au/construction/BuildingPlumbing/Building/SecurityOfPayment/Pages/ProjectBankAccounts.aspx>>.

¹⁰⁰ Department of Finance, Government of Western Australia, *Project Bank Accounts* (2018) <http://www.finance.wa.gov.au/cms/Building_Management_and_Works/New_Buildings/Project_bank_accounts.aspx>. Consider also Collins, above n 46, in his Final Report of the Independent Inquiry into Construction Industry Insolvency in NSW, which was adopted by the state of Queensland in the *Building Industry Fairness (Security of Payment) Act 2017* (Qld).

¹⁰¹ Department of Finance, Government of Western Australia, *AS 2124 Project Bank Account Pack* (1 May 2018) <https://www.finance.wa.gov.au/cms/uploadedFiles/Building_Management_and_Works/New_Buildings/pba_information_pack.pdf>.

¹⁰² *Ibid.*

subcontractors, who are beneficiaries of the trust, as the money is effectively quarantined for them.¹⁰³

PBAs do not fundamentally change the way conventional projects work; monthly claims are still submitted and assessed by the client or superintendent. What changes, however, is that payments are deposited by the principal or client into the PBA trust account created by the head contractor, and from there they are simultaneously disbursed by the bank directly to subcontractors.¹⁰⁴ Retention monies are retained in the PBA and disbursed as appropriate.¹⁰⁵ Therefore, PBAs give greater confidence to subcontractors that they will get paid by providing a fairer and more transparent payment regime.

PBA documentation consists of a Trust Deed Poll and a PBA Agreement. The former is established by the head contractor and is an agreement between it and the principal or client outlining how the PBA will work. The latter is an agreement between the aforementioned parties and the participating bank setting out how the bank account will operate. The head contractor and subcontractors are beneficiaries of the trust.¹⁰⁶

In terms of operation, progress payment claims are submitted as they would usually be. Once they have been certified or approved by the principal, the head contractor issues progress payment instructions to the bank outlining amounts to be paid to the head contractor, subcontractors and any retentions.¹⁰⁷ The progress payment instruction is important as it creates the obligation on the principal to pay into the PBA, it identifies recipients, amounts and retentions, and it acts as an irrevocable direction to the bank to make the required payments.¹⁰⁸

Whilst the use of PBAs has been encouraged for quite some time, the actual adoption of PBAs has been slow until recently. Despite this, momentum appears to be growing and other states may, in time, follow the lead of Queensland in legislatively requiring the use of PBAs more widely, as discussed further below.

A History of PBAs

Statutory trusts were first considered in New South Wales as early as 1991 when the New South Wales Government commissioned a report considering that statutory trusts would have legal shortcomings, would

¹⁰³ Explanatory Notes, *Building Industry Fairness (Security of Payment) Bill 2017*, 3.

¹⁰⁴ Department of Finance, above n 101, 3.

¹⁰⁵ *Ibid.*

¹⁰⁶ *Ibid.* 4.

¹⁰⁷ *Ibid.*

¹⁰⁸ *Ibid.* 5.

increase costs for all parties and were not needed as the problems they addressed were not significant.¹⁰⁹

In 1995, the Western Australian Government also commissioned a report to investigate what, if any, changes to the law should be made to protect payment of subcontractors and workers in the construction industry ('WALRC Report').¹¹⁰ The subsequent Law Reform Commission report considered that statutory trusts had the advantages of ensuring payment, imposing ethical standards, reinforcing good practice, protecting funds from misappropriation, providing a wider range of remedies for breach, and resulting in speedier dispute resolution and speedier payments to subcontractors.¹¹¹

The 1996 Queensland Scurr Report proposed that five per cent of the total contract price of a project be placed into a trust to secure payment of parties further down the line. This proposal was not adopted.¹¹²

The Cole Royal Commission in 2003 noted that Australian jurisdictions had not implemented trust models and that such models were opposed by many key construction organisations. Accordingly, the adoption of a trust model was not recommended.¹¹³

In 2012 the *Inquiry into Construction Industry Insolvency in NSW* ('Collins Inquiry') acknowledged that the WALRC Report, briefly mentioned above, provided the most 'scholarly and convincing analysis of the statutory construction trust'.¹¹⁴ Mr Collins addressed prior criticisms of or reservations concerning statutory trusts, in particular those observed in New South Wales, and recommended that statutory trusts be used in all projects over \$1 million.¹¹⁵

The Evans Review acknowledged prior recommendations by the Law Reform Commission of Western Australia to implement a trust scheme,¹¹⁶ and suggested that, whilst the issue of PBAs was perhaps outside the purview of the review, they had been successfully used in other jurisdictions.¹¹⁷ Furthermore, trust accounts would greatly assist those

¹⁰⁹ Andersen Consulting, 'Feasibility Study into the Proposal Prepared by the NSW Security of Payment Committee' (Final Report, 28 May 1993).

¹¹⁰ Law Reform Commission of Western Australia, *Financial Protection in the Building and Construction Industry*, Project Report No 82 (1998) 1, Terms of Reference.

¹¹¹ *Ibid* 52-53.

¹¹² A Scurr, 'Report of Commission of Inquiry into Security of Payment in the Building and Construction Industry and Dissenting Report' (Report, 1996).

¹¹³ Commonwealth, Royal Commission into the Building and Construction Industry, *Final Report* (2003) 295.

¹¹⁴ Collins, above n 46, 214.

¹¹⁵ Murray, above n 5, 298.

¹¹⁶ Evans, above n 57, 80.

¹¹⁷ *Ibid* 83.

subcontractors at the lower end of the chain,¹¹⁸ and the use of trust accounts would cut down on illegal phoenix activity and the use of false statutory declarations.¹¹⁹ The 2015 Senate Report recommended the use of PBAs.¹²⁰ Finally, the 2017 DJSB Review recommended a cascading statutory trust should apply to all parts of the contractual payment chain,¹²¹ and that the Australian Government should take the lead in establishing a nationally consistent statutory trust model.¹²² Despite these many recommendations, however, there have also been considerable criticisms of PBAs particularly, and unsurprisingly, from major head contractors.

B Criticisms of PBAs

One major criticism of PBAs is that they are complicated and costly. (although PBAs are in fact no more complicated or costly to establish and administer than normal bank accounts).¹²³ It has also been commented that the use of PBAs creates additional administrative costs and uncertainty, that they are an ‘unreasonable legislative interference’, that they do not adequately solve insolvency problems but rather exacerbate them by not allowing builders to divert money from one project to another.¹²⁴

Master Builders of Australia (NSW Chapter) has opposed the use of any trust arrangement, suggesting that participants in the construction industry lack the management and financial skills necessary to adequately administer and use PBAs.¹²⁵ This is contrary to Professor Philip Evans’ view, that such suggestions of a lack of skills amongst industry professionals are ‘offensive and demeaning’.¹²⁶

Master Builders Queensland, in its recent response to the Queensland Building Plan Discussion Paper stated that it does not support PBAs and does not believe that the Queensland Government’s PBA model will be able to effectively facilitate payment to all levels of subcontractors. Further, PBAs, it is suggested, will add cost and complexity to the industry

¹¹⁸ Evidence to Senate Economics References Committee, Parliament of Australia, Perth, 26 October 2015, 3-4.

¹¹⁹ *Ibid* 17, 42.

¹²⁰ Senate Economics References Committee, above n 1, 13.

¹²¹ Murray, above n 5, recommendation 85.

¹²² *Ibid* recommendation 86.

¹²³ Cabinet Office, United Kingdom, *A Guide to the Implementation of Project Bank Accounts (PBAs) in Construction for Government Clients* (3 July 2012) 5.

¹²⁴ Senate Economics References Committee, above n 1, 164; Housing Industry Association Limited (‘HIA’), Submission to Queensland Government, *Queensland Building Plan*, 20 February 2017, 11.

¹²⁵ Master Builders of Australia New South Wales Chapter, Submission to New South Wales Government, *Independent Inquiry into Construction Industry Insolvency*, 16 July 2014, 4.

¹²⁶ Evidence to Senate Economics References Committee, Parliament of Australia, Perth, 26 October 2015, 4.

and will not improve payments within the industry.¹²⁷ Master Builders recommends instead that improved financial reporting requirements, improved dispute resolution mechanisms, enforced contracts and payments, and better education would be far more effective.¹²⁸

The Housing Industry Association's ('HIA') response to the Queensland Building Plan Discussion Paper makes similar criticisms, in that, since PBAs only address one tier of the contractual chain, they do not guarantee payment further down the chain. Further, when the builder and the developer are the same entity, the PBA is ineffective and default by a building owner will eliminate security from the PBA.¹²⁹ The HIA response further outlines that trust arrangements will deprive the industry of cash flow and working capital by preventing the movement of funds to other projects.¹³⁰

In response to such criticisms, evidence suggests that the administrative burden and cost of using PBAs is not high and, in fact, the use of PBAs may reduce costs if subcontractors no longer need to consider or provide contingencies in their quotes to protect against payment delays.¹³¹ In fact, evidence in the United Kingdom has indicated that procurement costs have fallen slightly due to subcontractors not being required to inflate fees in order to cover the risk of non-payment.¹³² Further, it has been suggested that properly implemented PBAs can reduce construction costs by one per cent,¹³³ although others believe such reduction is as high as 2.5 per cent.¹³⁴ In response to cash flow criticisms, it has been submitted that the practice of using funds from one project to subsidise another is perhaps unconscionable,¹³⁵ or, at worst, illegal.¹³⁶

The WALRC Report provides succinct discussion on criticisms levelled against PBAs, arguing that the costs of administering such schemes are likely to be low and no more than required generally for the proper running

¹²⁷ Master Builders Queensland, Submission to Queensland Government, *Queensland Building Plan Discussion Paper*, February 2017, 2.

¹²⁸ Grant Galvin, *Queensland Builders Reject Project Bank Accounts* (7 June 2017) Master Builders Australia <<https://www.masterbuilders.com.au/Blog/Project-Bank-Accounts>>.

¹²⁹ HIA, above n 124, 3.

¹³⁰ *Ibid* 4.

¹³¹ Law Reform Commission of Western Australia, above n 110, 53.

¹³² Corrs Chambers Westgarth, *Project Bank Accounts: Building Industry Fairness* (2 November 2017) <<https://www.corrs.com.au/assets/publications/QBIF-project-bank-accounts2.pdf>>.

¹³³ Cabinet Office, United Kingdom, *Project Bank Accounts – Briefing Document* (10 February 2012).

¹³⁴ United Kingdom Office of Government Commerce, *Guide to Best 'Fair Payment' Practices* (2007) 3 <<https://www.bipsolutions.com/docstore/pdf/18463.pdf>>.

¹³⁵ Evidence to Senate Economics References Committee, Parliament of Australia, Perth, 26 October 2015, 4.

¹³⁶ Evidence to Senate Economics References Committee, Parliament of Australia, Adelaide, 21 September 2015, 59.

of a business.¹³⁷ Additionally, trust schemes may deter underbidding if parties are unable to divert funds to other projects, and may encourage better project funding management practices.¹³⁸

Despite the criticisms above, the use of a statutory trust model has generally had support throughout Australia. The 1995 WALRC Report explicitly recommended it,¹³⁹ and the 2012 Collins Inquiry noted that:

There is no question that the statutory construction trust is fully effective in protecting subcontractors against the loss of progress claims paid by the owner to the head contractor and lost in the event of the head contractor's insolvency.¹⁴⁰

The 2015 Senate Report also indicated that union and contractor association support for trust schemes for entire projects, rather than just retention funds, has been strong.¹⁴¹

IV USE AND RECEPTION

Where PBAs have actually been used in projects, the benefits have been appreciated. Western Australia has seen strong support for PBAs and was one of the first Australian jurisdictions to trial and subsequently use PBAs in major projects.¹⁴² In November 2013, the Western Australian Department of Finance ('the Department') began trialling PBAs,¹⁴³ following similar trials that had previously occurred in New South Wales, Victoria and the Northern Territory. The Western Australian trial involved seven selected projects in the Department's Building Management and Works ('BMW') construction portfolio. Once completed, the trial demonstrated that PBAs could indeed improve the certainty and timing of payments for subcontractors, but that the model needed refining as it could be more efficient.¹⁴⁴

The Western Australian Government was sufficiently satisfied with the trial that in August 2016 it announced that PBAs would be used for

¹³⁷ Law Reform Commission of Western Australia, above n 110, 53 [3.16].

¹³⁸ *Ibid* 55 [3.18].

¹³⁹ *Ibid* 105.

¹⁴⁰ Collins, above n 46, 133.

¹⁴¹ Senate Economics References Committee, above n 1. See, eg, Construction, Forestry, Mining and Energy Union, Submission No 15 to Senate Economics References Committee, *Insolvency in the Australian Construction Industry*, 1 May 2015, 4; Evidence to Senate Economics References Committee, Parliament of Australia, Adelaide, 21 September 2015, 15.

¹⁴² Department of Premier and Cabinet, Government of Western Australia, 'WA Leads the Way with Project Bank Accounts' (Media Statement, 30 September 2016) <<https://www.mediastatements.wa.gov.au/Pages/Barnett/2016/09/WA-leads-the-way-with-project-bank-accounts.aspx>>.

¹⁴³ Department of Finance, above n 101.

¹⁴⁴ *Ibid*.

government BMW projects worth over \$1.5 million, using the generic Australian Standard AS2124 contract.¹⁴⁵ The government subsequently announced up to 30 projects that would commence by 30 June 2017 and that would be using PBAs.¹⁴⁶ The total value of these projects was estimated at \$220 million, with the first project, the Margaret River Rapids Landing Primary School, worth \$12.5 million.¹⁴⁷

This was welcome news for Western Australian subcontractors plagued by payment scandals in the past few years, including the embattled Perth Children's Hospital project and the Elizabeth Quay project.¹⁴⁸

When their use for BMW projects was announced by the Western Australian Liberal Government in 2016, the opposition at that time criticised the proposed PBAs as not going far enough,¹⁴⁹ and promised to strengthen proposed Liberal reforms, ultimately resulting in a Western Australian Labor policy on protections for subcontractors which called for the establishment of PBAs for government projects and a better 'security of payments' mechanism for government and non-government contracts.¹⁵⁰

In a December 2016 report, the Western Australian Auditor General, Colin Murphy, acknowledged significant improvement in processes that help ensure security of payments particularly within BMW projects,¹⁵¹ which were the focus of PBA trials. The report expressed the view that PBAs, improved SOP legislation and the introduction of a code of conduct for state-procured construction projects would improve the construction industry in Western Australia.¹⁵²

¹⁴⁵ Office of the Auditor General, Western Australia, 'Western Australian Auditor General's Report: Assessment of Progress to Improve Payment Security for Government Construction Subcontractors' (Report, 31 December 2016) 7 <[http://www.parliament.wa.gov.au/publications/tailedpapers.nsf/displaypaper/3914924ae5344d2e750de62c48258091001330da/\\$file/4924.pdf](http://www.parliament.wa.gov.au/publications/tailedpapers.nsf/displaypaper/3914924ae5344d2e750de62c48258091001330da/$file/4924.pdf)>

¹⁴⁶ Department of Premier and Cabinet, above n 142.

¹⁴⁷ *Ibid.*

¹⁴⁸ *WA Rolls out New Laws to Help Subbies Not Being Paid for Work* (20 September 2016) news.com.au <<https://www.news.com.au/national/western-australia/wa-rolls-out-new-laws-to-help-subbies-not-being-paid-for-work/news-story/630240ca474e7bf34ce353475b953127>>.

¹⁴⁹ Charlotte Hamlyn, *Construction Reforms Criticised by WA Opposition* (12 August 2016) ABC News <<http://www.abc.net.au/news/2016-08-12/construction-reforms-criticised-by-wa-opposition/7728856>>.

¹⁵⁰ Western Australian Labor Party, 'Protections for Subcontractors' (Policy, August 2016) 3 <https://www.subcontractorswa.com.au/resources/docs/Protections_for_Subcontractors.pdf>.

¹⁵¹ Office of the Auditor General Western Australia, above n 145.

¹⁵² *Ibid.* 10.

However, the Auditor General noted that BMW trials indicated that whilst PBAs can be used successfully to improve the transparency of the payment process and speed of payment for subcontractors, they cost approximately \$80 000 per project (on projects exceeding \$1.5 million), and were challenging to create and demanding to administer.¹⁵³ Arguably, further work and education is required in this area.

PBAs and trust schemes have had success in other jurisdictions outside of Australia. Mandatory trust arrangements exist in the United States of America, Canada and the United Kingdom ('UK')¹⁵⁴ although there may be some differences in how they are used. For example, Maryland's lien arrangement also applies to payments from owners to builders and therefore applies to work performed by subcontractors up and down the construction chain. Further, it does not require that funds be placed in a separate trust account.¹⁵⁵

In September 2009, the UK Government Construction Board mandated that PBAs be used for government funded construction work unless there was a compelling reason to avoid their use.¹⁵⁶ In October 2009, the UK's Joint Contracts Tribunal published PBA documentation to be used with its main standard forms of contract.¹⁵⁷

Three years after the implementation of PBAs, the UK Cabinet Office reported that PBAs had been a success and were instrumental in paying government suppliers on time. Although the government had committed to deliver £4 billion worth of construction projects in the first three years using PBAs, their success had actually resulted in £5.2 billion worth of projects being delivered using PBAs in that time.¹⁵⁸ However, the uptake of PBAs in the private sector in the United Kingdom has been slow.¹⁵⁹

In 2014 the Construction Leadership Council proposed a Construction Supply Chain Payment Charter by which signatories would agree that from 2018 they will adhere to 30-day payment terms and by 2025 they will no longer withhold retentions.¹⁶⁰ Such charters have been proposed as

¹⁵³ Ibid 15-16.

¹⁵⁴ Senate Economics References Committee, above n 1, 159.

¹⁵⁵ HIA, above n 124, 6.

¹⁵⁶ Cabinet Office, above n 123.

¹⁵⁷ Evans, above n 57, 85.

¹⁵⁸ United Kingdom Cabinet Office and The Right Honourable Lord Maude of Horsham, *Project Bank Accounts Are Helping to Pay Government Suppliers on Time* (2 July 2014) <<https://www.gov.uk/government/news/project-bank-accounts-are-helping-to-pay-government-suppliers-on-time>>; Cabinet Office, above n 133.

¹⁵⁹ HIA, above n 124, 6.

¹⁶⁰ United Kingdom Department for Business, Energy and Industrial Strategy, 'Construction Supply Chain Payment Charter' (10 August 2016) <https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/541454/construction-supply-chain-payment-charter.pdf>.

alternatives to PBAs, with some suggesting that they are a sign that PBAs are having some success in changing payment cultures.¹⁶¹

V PROJECT BANK ACCOUNTS: QUEENSLAND'S NEW APPROACH

Statutory construction trusts for retention monies, but not other project monies, are used in Western Australia,¹⁶² the Northern Territory¹⁶³ and New South Wales.¹⁶⁴ However, they have not been legislatively mandated until recently in Queensland. The use of a statutory construction trust for an entire project via PBAs is prescribed by Queensland's new *Building Industry Fairness (Security of Payment) Act 2017* (see below).

In August 2017, Queensland's Australian Labor Party ('ALP') introduced the *Building Industry Fairness (Security of Payment) Bill 2017* ('BIF Bill') into its parliament.¹⁶⁵ The BIF Bill called for radical amendments to existing SOP legislation and stricter penalties including prison for head contractors who offend. The BIF Bill also recommended the amendment and consolidation of the *Building and Construction Industry Payments Act 2004* and the *Subcontractors' Charges Act 1974* into one Act and for the introduction of PBAs and a variety of key changes intended to improve security of payment for subcontractors.¹⁶⁶ The ALP, who also launched an intensive advertising campaign,¹⁶⁷ introduced the BIF Bill in order to be 'putting the construction industry on the level'.¹⁶⁸

In October 2017, the BIF Bill was passed, resulting in the replacement of the *Building and Construction Industry Payments Act 2004* (Qld) and the *Subcontractors' Charges Act 1974* (Qld) by the *Building Industry Fairness (Security of Payment) Act 2017* (Qld) ('Queensland Act'). The Act contains

¹⁶¹ United Kingdom Department for Business, Innovation and Skills, 'Government and Industry Agree New Construction Payment Charter' (Press Release, 22 April 2014) <<https://www.gov.uk/government/news/government-and-industry-agree-new-construction-payment-charter>>.

¹⁶² *Construction Contracts Act 2004* (WA) sch 1, div 9, s 11.

¹⁶³ *Construction Contracts (Security of Payments) Act* (NT) sch 1, div 9, s 10.

¹⁶⁴ *Building and Construction Industry Security of Payment Amendment (Retention of Money Trust Account) Regulation 2015* (NSW).

¹⁶⁵ *Building Industry Fairness (Security of Payment) Bill 2017* (Qld).

¹⁶⁶ Thomson Geer Lawyers, *CONSTRUCTION ALERT: Building Industry Fairness (Security of Payment) Bill 2017: Securing a Fairer Payment Regime for Subcontractors in Queensland - but at what Cost?* (24 August 2017) <<http://www.tglaw.com.au/corporate/publications/urgent-construction-alert-building-industry-fairness-security-payment-bill-2017-securing-fairer-payment-regime-subcontractors-queensland-cost/>>.

¹⁶⁷ See, eg, Queensland Department of Housing and Public Works, *Queensland Building Plan - Project Bank Accounts TV Commercial* (1 February 2017) YouTube <<https://www.youtube.com/watch?v=gcSQPsZ769A>>.

¹⁶⁸ Department of Premier and Cabinet, Queensland Government, 'Palaszczuk Government to Introduce Landmark Building Industry Fairness Legislation' (Media Statement, 22 August 2017) <<http://statements.qld.gov.au/Statement/2017/8/22/palaszczuk-government-to-introduce-landmark-building-industry-fairness-legislation>>.

some improvements to payment claims, payment schedules and adjudication and, importantly, provides for the utilisation of PBAs for particular construction projects.¹⁶⁹

Of particular importance are the provisions relating to PBAs, modelled somewhat on Western Australian trials and experiences with PBAs.¹⁷⁰ Pursuant to the Queensland Act, the mandatory use of PBAs by head contractors and first tier subcontractors¹⁷¹ will be phased in over two years commencing in early 2018. State construction projects over \$1 million (with some exceptions) will be required to use PBAs¹⁷² and any state project may be declared a PBA project by regulation.¹⁷³ Importantly, it is anticipated that from 1 January 2019, the legislation will be expanded to require the use of PBAs for projects over \$1 million where the principal is a private party.¹⁷⁴

Further, whilst the Queensland Act only provides for payments from head contractors to their subcontractors (first tier subcontractors) and not from first tier to second tier subcontractors and so on, it does include a mechanism whereby PBAs could be required for payments to lower tier subcontractors.¹⁷⁵

PBAs will be used to hold trust payments by the principal to the head contractor, payments to a subcontractor from a head contractor under a first-tier subcontract, retention monies withheld under a first-tier subcontract, and monies the subject of a payment dispute.

Division 2 of the Queensland Act deals with requirements for establishing PBAs, including a stipulation that each relevant project will require one PBA made up of three separate trust accounts (a general account, a retention account and a disputed funds account) to be established by the head contractor, with the head contractor being the trustee and beneficiary of accounts, and first-tier subcontractors (subcontractors who have contracted directly with the head contractor) also being beneficiaries.¹⁷⁶ The PBA must be operated by a financial institution in Queensland and there are strict requirements as to its operation, including withdrawals, transfers and payment instructions.

¹⁶⁹ *Building Industry Fairness (Security of Payment) Act 2017* (Qld) s 3.

¹⁷⁰ Public Works and Utilities Committee, 'Public Briefing - Inquiry into the *Building Industry Fairness (Security of Payment) Bill 2017*' (6 September 2017) 7.

¹⁷¹ See *Building Industry Fairness (Security of Payment) Act 2017* (Qld) s 6 which provides definitions of the various tiers.

¹⁷² *Ibid* s 14(1).

¹⁷³ *Ibid* s 14(2).

¹⁷⁴ Public Works and Utilities Committee, above n 170, 8.

¹⁷⁵ Corrs Chambers Westgarth, above n 132.

¹⁷⁶ *Building Industry Fairness (Security of Payment) Act 2017* (Qld) s 23.

Progress payments should become more efficient as they are made from the PBA to the head contractor and subcontractors at the same time rather than by a trickle-down effect. Further, they will prevent builders using funds from one project on another.¹⁷⁷

Claims from other creditors (other than the beneficiaries) are excluded from the legislation, as is the investment of the trust funds. The head contractor is to cover the costs of administration and bank fees and cannot recover these from subcontractors.¹⁷⁸ However, the administration and costs are not onerous. Costs of establishing trust accounts can be as little as \$15, with transaction costs as low as \$0.15 per transaction and additional administration time of around five hours per month.¹⁷⁹

Penalties for breaching PBA requirements, and breaches of the Queensland Act generally, are significant and can include imprisonment for up to two years in some cases.

In relation to the general account, there are limits on withdrawals and rules on priority of payment.¹⁸⁰ Payments to subcontractors can only be made from the PBA.¹⁸¹ Of particular significance is that the head contractor will not be entitled to any payment to itself unless sufficient funds are in the PBA to cover payments due to subcontractors,¹⁸² and the head contractor must cover any shortfall thereof or pay out pro-rata to subcontractors.¹⁸³

If there is a difference between the payment schedule issued by the head contractor and the progress payment instruction provided to the principal, a payment dispute arises and the difference is to be placed into the disputed funds trust account.¹⁸⁴ If a head contractor has failed to give a payment schedule to the subcontractor, in response to the subcontractor's claim, a payment dispute also arises and head contractor will be liable to pay the amount claimed by the subcontractor.

A payment schedule is a document provided by a head contractor in response to a subcontractor's payment (or progress) claim. It must identify the payment claim, state the amount that will be paid by the head contractor and if this amount is different to the amount claimed, must state the reasons for the difference.¹⁸⁵

¹⁷⁷ Department of Premier and Cabinet, above n 168.

¹⁷⁸ *Building Industry Fairness (Security of Payment) Act 2017* (Qld) s 43.

¹⁷⁹ Public Works and Utilities Committee, above n 170, 6.

¹⁸⁰ *Building Industry Fairness (Security of Payment) Act 2017* (Qld) ch 2 pt 3 div 4.

¹⁸¹ *Ibid* s 29.

¹⁸² *Ibid* s 32.

¹⁸³ *Ibid* s 30.

¹⁸⁴ *Ibid* ss 35, 36.

¹⁸⁵ *Ibid* s 69.

Given that the Queensland Act only covers projects over \$1 million and prescribes PBAs for use between head contractors and first-tier subcontractors, one might question how this assists subcontractors on smaller projects and smaller than tier-one subcontractors on any project. It is important to note that firstly, the PBAs form an important step in giving certainty to cash flow between principals, head contractors and first-tier subcontractors that has traditionally been problematic and the cause of many insolvencies lower down the chain.

Secondly, the pre-existing *Subcontractors' Charges Act 1974* (Qld) and the adjudication processes under the previous SOP suite are now revised and included in the *Building Industry Fairness (Security of Payment) Act 2017* (Qld).¹⁸⁶ Therefore, subcontractors not included in the PBAs are still arguably better off than before.¹⁸⁷

Other criticisms of the Queensland Act are that engineering and residential projects are excluded, that it initially requires the use of PBAs only for projects between \$1 million and \$10 million, and that it does not currently apply to non-government contracts.¹⁸⁸

Despite these criticisms or shortfalls, arguably PBAs are the way forward. Hopefully, if successful, the mandated use of PBAs will become more commonplace and pervasive and cover a broader range of construction projects.

VI CONCLUSIONS AND RECOMMENDATIONS

The construction industry is responsible for a disproportionate number of insolvencies. Lower order contractors and subcontractors face huge cash flow risks due to mismanagement of projects or the collapse of head contractors, a trend that still happens all too frequently.

The impact of payment delays, defaults and insolvencies upon the industry is tremendous and has resulted in cost increases due to the pricing in of payment default contingencies by those who can afford to make allowance for such considerations. However, lower order subcontractors with extremely thin profit margins and stiff competition simply cannot mitigate against payment or cash flow risks and are unfortunately the ones who suffer most when a head contractor fails to pay or becomes insolvent. The impact of such uncertainty around payment upon the financial, physical

¹⁸⁶ *Ibid* ch 3.

¹⁸⁷ Public Works and Utilities Committee, above n 170, 10.

¹⁸⁸ Ted Williams, *Project Bank Accounts – Do They Cheque Out?* (26 April 2017) PiperAlderman <<https://www.piperalderman.com.au/publications/construction-infrastructure/article/28403>>.

and mental wellbeing of smaller subcontractors is significant and highly damaging.

Current SOP legislative regimes that have been enacted in various Australian jurisdictions have been somewhat effective in addressing many of the issues faced within the industry, especially in relation to payment and payment disputes. This is largely achieved by the provision of swift payment adjudication procedures, measures to deal with disputes generally and some prescriptions in relation to contracting. However, there is a lack of both uniformity and consistency between the various jurisdictions. The differing timelines, processes and formalities make this a complex and confusing area for many smaller construction industry participants. There is also the problem of a lack of awareness amongst smaller businesses of the availability of SOP legislation, and even where this awareness does exist, there is a reticence to use such initiatives for fear of intimidation or retribution in a very competitive market.

Unfortunately, then, a conclusion can be drawn that, despite good intentions, Australian SOP legislation has not effectively provided the payment protection often desperately required by small subcontractors, and has not prevented Australia from being amongst the world's worst performers when it comes to payment delays in the construction industry.

Furthermore, despite frequent reviews in some jurisdictions, SOP legislation does not extend to ensure secure and transparent payment from head contractors down the contractual chain (except as of very recently in Queensland).

Whilst acknowledging that no system will guarantee payment in all circumstances, a statutory trust mechanism such as a PBA creates a more secure and transparent payment system that can alleviate many payment problems. Since payment procedures are controlled and head contractors cannot simply pay themselves first or divert funds to other projects, payment is arguably more secure and decisions by lower order subcontractors about whether or not to make a claim and face retribution are largely eliminated.

Although there have been criticisms of the effectiveness, administrative costs and complexity of PBAs, their use and reception in trials across various Australian states, especially Western Australia, has been largely positive. The United Kingdom has seen a slight reduction in costs of government construction due to the use of PBAs, but it is too early to tell whether this will occur in Australia.

The Queensland Government has fully supported the use of PBAs by mandating their use in certain government construction projects from 2018

and in certain private construction projects from 2019. The *Building Industry Fairness (Security of Payment) Act 2017* (Qld) provides detailed guidance on the use of PBAs and may provide a useful model for other jurisdictions.

However, in order for the implementation of PBAs to be successful, effort needs to be applied to increase education about and awareness of their existence and operation, especially amongst lower order subcontractors. The costs and complexity of PBAs need to be low and participants at all levels of the industry need to experience their operation as being an effective part of the range of security of payment measures.

In conclusion, implementation of uniform SOP legislation that provides for fair payment mechanisms and practices, whilst facilitating simple, cheap, effective and fair payment dispute mechanisms with realistic timeframes and mandating the use of PBAs throughout the contract chain in all significant construction contracts, at the very least, will go a long way towards alleviating the payment and insolvency issues faced by the Australian construction industry.