LIPMAN
DESIGNED TO PERFORM · BUILT TO LAST
ESTABLISHED 1966

Level 6, 66 Berry Street
North Sydney NSW 2060
Australia

www.lipman.com.au
ABN: 8400 1548 830

29 January 2019

Security of Payment Reforms: Implementation
Regulatory Policy, BRD
Department of Finance, Services and Innovation
Locked Bag 2906
LISAROW NSW 2252

Via email: securityofpayment2018@finance.nsw.gov.au

Dear Sir/ Madam,

RE: SECURITY OF PAYMENT REFORMS – IMPLEMENTATION
Options Paper – December 2018

With reference to the above document we have considered the content around the commencement options and relative impacts of same.

Instead of responding to the proposed timing of each commencement option we have chosen to comment more generally around these. We have, however, made more targeted comments under individual headings for the proposed further reforms to the Regulation. For ease of reference we have responded to these in the format presented in the Options Paper.

We recognize that the Amendment Act was assented to on 28 November 2018 but also wish to raise concerns within our response in relation to the key reform of reducing the maximum time of payments from head contractors to subcontractors from 30 business days to 20 business days. We address this concern later in our response.

General comment around commencement options dates

Although we have no real objection to the staged introduction of the commencement options, we opine that the most effective form of implementing the reforms would be to enact them all under one commencement date. We are cognizant of the fact that the third tranche of the reforms requires subordinate legislation and/ or administrative changes to be enacted before they can commence. We see the satisfaction of these requirements as being the most suitable time to enact all the reforms at once. Due to the large volume of reforms to consider as part of the Amendment Act it will be a far easier task for the Industry to digest, understand, plan for

(through both training and significant administration changes) and implement rather than having to keep track of which reforms apply and which ones don't at any particular point in time.

We agree with the general rule provided by the Amendment Act that the reforms will not apply to a construction contract entered into prior to commencement (with "construction contract" being defined as the contract between the Principal and Contractor).

Proposed reforms to the Regulation

Reducing the threshold for retention money trust requirements

Reducing the threshold for retention money trust requirements from $20 million to $10 million is an adjustment that a number of companies will not be able to deal with. In our case, most of our projects are over $20m so a reduction to $10m is of little significance to our business. We see the administrative impost upon contractors already complying within this space and adhering to the legislation under the Act as being negligible in lowering the threshold.

We do not, however, agree with removing the annual reporting requirements in clause 16 of the Regulation. Lipman see this as being a fundamental requirement for building companies operating with robust financial systems, probity and accountability. The argument could be raised that if companies building projects in excess of $10 million can neither afford nor have the expertise to affect this form of reporting then it's questionable as to whether they should be operating in this space in the first instance. In addition we also see this as being the key to transparency and independent accounting of the trust account records (refer section "Inspection of trust account records").

Furthermore our experience in dealing with a raft of subcontractors across both the Sydney metro and regional country areas has demonstrated no proof to date that annual reporting requirements are encouraging head contractors to take out bank guarantees in place of retention. Quite simply contractors and subcontractor could neither sustain nor support such a limiting activity taking place especially in regional areas where affordability around obtaining bank guarantees is almost non-existent.

In relation to the question around extending the retention trust money obligations to the entire contracting chain we see this as being problematic for the following reasons:

a. Determining appropriate trades (in this case sub-subcontractors) to which this may apply becomes discretionary and subjective;
b. Nominating a minimum threshold amount for sub-subcontracts valued over a certain amount becomes problematic to determine (i.e. a large subcontract sum does not necessarily indicate a large sub-subcontract sum); and
c. The management, checking and ensuring compliance in the sub-subcontract space would invariably fall back upon the contractor as their responsibility.

d. The introduction of this requirement for sub-subcontractors could be utilized by unscrupulous third parties as a means for causing unsubstantiated claims leading to industrial unrest on projects.

Inspection of trust account records

We see this proposal as not offering any value in the areas of providing increased transparency of payments or providing greater protections to subcontractors.

The proposal is of no added value for the following reasons:

a. Accounting practices dictate that monies sitting in a retention fund at any one time do not have specifically "hived-off" amounts pertaining to individual subcontractor retention amounts held in the trust;
b. Intermittent transfers of subcontractor retentions into the individual trusts are grouped and not labelled individually in relation to each subcontractor;
c. Where reconciled amounts in trust funds are provided these will need to have the names of all other subcontractor's redacted from the document making it all but meaningless.

As mentioned above we see the most effective and transparent means of giving subcontractors comfort and certainty that their funds are in fact in trust as being through the independent audit undertaken through the Contractor and the checking of same by the Office of State Revenue. The provision of a certificate to subcontractors on an annual basis from these audits ought to be sufficient to provide subcontractors with certainty in relation to trust monies.

In the event that these inspections become enacted under the Reforms Lipman submits that an appropriate fee be charged for these services. Lipman would envisage such a fee to be in the vicinity of $350-$500 per inspection and that the subcontract be limited to a number of inspections per annum for administrative reasons.

Prescribing penalty notice offences and increased values of penalty units

The vast majority of reputable contractors comply in relation to the nominated offences under the Act and Regulation. We argue that there are already sufficient penalties under the Act including that claims become invalid in the event that Supporting Statements don't accompany head contract claims. We also propose that the cost to the Government of administering a penalty infringement notice system would not only far outweigh revenue recovered through infringements but would not likely change any undesirable behaviours of non-compliant contractors under the Act and Regs.

To that end we neither support offences being subject to penalty infringement notices nor increases in the values of penalty units.

LIPMAN
DESIGNED TO PERFORM · BUILT TO LAST

Other matters

Prohibiting a corporation in liquidation from making payment claims

We note, and welcome, the reform preventing a corporation in liquidation from serving or enforcing a payment claim. We are curious, however, as to how this would apply in the instance where a construction contract were terminated as a result of a liquidation not following an administration or scheme of arrangement (bearing in mind the introduction of 13 (1C) allows a payment claim to be served on and from the date of termination)? Given the overwhelmingly high number of liquidations come from Subcontractors and the liquidators pursuit of 'low hanging fruit', it appears inevitable that there will be confusion in the amendment. Does the condition of the corporation in liquidation override that of the terminated contract?

Reduction in time of head contractor to pay subcontractor from 30 business days to 20 business days

As mentioned above we still see this as being problematic across the Industry in NSW for a number of reasons with the most obvious being that the legal inconsistency across Australia has become undesirable in relation to managing and administering differing payment terms between States and Territories.

Industry practice has been to pay subcontractors on 30 day payment terms meaning that subcontractors are paid at the end of the following month after submitting a payment claim. Typically this meant that subcontractors would submit their payment claims by the 25th of the month allowing the head contractor to accommodate these claims within their own claim to the principal. In adopting the shortened time frame of 20 business days from payment claim some payment claims for subcontractors will fall well inside the end of the following month. This would mean that head contractors would not only need to make wholesale changes to their internal accounting systems to accommodate these changes but contractor's run the risk of being cash negative with some principals not adhering to 15 business day payment terms (which incidentally are typically submitted a number of days into the next month after which the works were undertaken).

In recognizing that there was no logic to the differing approaches and timeframes that currently exist within the various jurisdictions, "Recommendation 19" under the J Murray AM's Review of Security of Payment Laws in 2017 suggested a payment term not exceeding **25 business days** for harmonization purposes.

As Lipman and most reputable contractors already pay on 30 day payment terms a legislative change to 25 business days would require little or no change to their current accounting and

internal payment procedures. As such we fully support J Murray's recommendation of payment 25 business days from payment claim or payment by the end of the following month to avoid the potential wholesale change to accounting procedures and systems along with supporting a timing recommended under the harmonization of the Act.

We hope the above comments on the Options Paper prove useful to NSW Finance Services and we welcome any feedback.

Yours faithfully,
LIPMAN PTY LTD

JEREMY PIDCOCK
Commercial Manager