Explanatory Statement

Building and Construction Industry Security of Payment Amendment Bill 2018

August 2018

Contents

Introduction

This Explanatory Statement relates to the *Building and Construction Industry Security of Payment Amendment Bill 2018* (the Bill) as publicly released on 22 August 2018.

It has been prepared to assist the reader of the Bill understand the proposed amendments to the *Building and Construction Industry Security of Payment Act 1999* (the Act) and to help inform submissions on it. This Statement also provides an overview of the potential regulatory impacts created by the proposed amendments.

This Statement is intended to be read in conjunction with the Bill and is not a comprehensive description of all provisions.

Overview

Background to Act

The Act is designed to ensure that any person who undertakes to carry out construction work, or who undertakes to supply related goods and services, under a construction contract is entitled to receive, and is able to recover, progress payments for that work or supply of goods and services.

The Act aims to ensure that contractors and subcontractors are paid promptly, that money is moved down the contracting chain faster, and that disputes over payments can be resolved quickly and fairly.

The Act commenced on 26 March 2000 following the NSW Parliament Joint Standing Committee on Small Business Report: Security of Payment for the NSW Building Industry (the Report).

When the Report was tabled on 13 October 1998, the Chairman of the Committee stated:

> Subcontractors bear a disproportionate share of the security of payment burden. They suffer from slow and delayed payment during the building work; they encounter difficulty in getting retention monies when work is completed; and they are usually the largest group of unsecured creditors if a head contractor goes into liquidation.[1]

To implement the Report's recommendations, the Building and Construction Industry Security of Payment Bill was introduced into Parliament on 8 September 1999. In the second reading speech it was noted:

> It is all too frequently the case that small subcontractors, such as bricklayers, carpenters, electricians and plumbers, do not get paid for their work. Many of them cannot survive financially when that occurs, with severe consequences to themselves and their families. The Government is determined to rid the construction industry of such totally unacceptable practices.[2]

NSW review

In response to a spate of insolvencies in the NSW building and construction industry in 2012, the Government initiated the Independent Inquiry into Construction Industry Insolvency (the Collins Inquiry) in August 2012.

The Collins Inquiry looked into the nature and extent of construction industry insolvencies and payment practices. It also examined protections for subcontractors, the impacts of insolvency on subcontractors and possible means to address insolvencies.

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[1] New South Wales, Legislative Council 1998, *Debates*, 13 October, p. 8075.
[2] New South Wales, Legislative Assembly 1999, *Debates*, 8 September, p. 103.

In January 2013, the Report of the Collins Inquiry was released and proposed 44 recommendations.

In response to the Collins Inquiry, the Government introduced reforms to help ensure prompt payments for subcontractors. The three major changes to the Act were:

- establishing prompt payment provisions
- requiring a head contractor to give a principal a written statement that all subcontractors have been paid when making a claim for payment
- new provisions to allow contractors to be fined and/or imprisoned for providing a false or misleading statement in order to get paid.

These reforms were consistent with the recommendations of the Collins Inquiry and the original intention of the Act.

During Parliamentary debate on the reforms, the Government recognised that stakeholders had expressed other concerns about the operation of the Act and it was stated that a formal review would commence in 2015.

A series of roundtables were held in 2015 to discuss the review of the Act, and in late 2015 the Government released a Discussion Paper for industry and public consultation. The paper was designed to guide discussion about whether the current laws are working as they should and outlined potential options for improving them.

The paper addressed the following topics:

- progress payments
- how payment claims are made
- payment due dates and schedules
- suspension of work when claims are not paid
- retention monies
- adjudication of disputes
- other issues concerning security of payment laws.

A total of 69 submissions were received, including responses from key industry stakeholders. These submissions confirmed strong support for the continued operation of the security of payment legislation. However, consensus amongst stakeholders indicated an opportunity to effect improvements.

The reforms contained in the Bill and discussed in this paper are the result of extensive consultation led by Fair Trading with industry stakeholders in 2017 and 2018 during the review of the Act.

This Explanatory Statement is being released for public consultation simultaneously with a Consultation Paper on a proposal for a statutory trust for the Government's consideration as part of the NSW review.

Commonwealth Murray Review

On 21 May 2018, the Commonwealth Government released the final report of the Review of Security of Payment Laws (the Murray Review), undertaken by Mr John Murray AM. Mr Murray was tasked with examining ways to improve consistency in security of payment legislation and enhance the level of protection afforded to subcontractors to ensure they obtain payment for work completed or supplied goods or services. Mr Murray was also tasked with identifying areas of best practice for security of payment legislation after examining the operation of legislation in all Australian jurisdictions.

The final report of the Murray Review contains 86 recommendations. One of the key findings from the review was the need for consistency in security of payment laws across Australia. This would provide for the equality of rights and protections across jurisdictions, as well as reducing complexity and administrative burden.

The NSW Government is currently working with Commonwealth, State and Territory jurisdictions as part of the Building Ministers Forum (BMF). The BMF are considering and responding to the findings and recommendations of the Murray Review.

The Bill has not been prepared to give effect to the Murray recommendations, however, it is worth noting that the proposed reforms are consistent with the findings of the Murray Review.

Rationale for reform

The building and construction industry is a significant contributor to the NSW economy, representing around 8 per cent of NSW's total industry output and more than 8 per cent of the workforce. Unfortunately, the industry is also known as having a high incidence of insolvency and relatively poor payment practices. In the last two years there have been a series of construction industry insolvencies in NSW across a range of projects where parties have been owed amounts ranging from $1 million to $20 million. In some cases, the party who has become insolvent was themselves owed money by debtors.

However, NSW's experience with insolvency in this sector is not unique and aligns with the experiences in other jurisdictions. In the last decade, the building and construction industry contributed to around 20 per cent of insolvencies occurring nationally.[3]

Given the hierarchical nature of contracting in the industry, insolvency by a single entity often impacts a range of other parties in the contractual chain. Subcontractors at the base of the contractual chain are particularly vulnerable to harm as they are likely to be small businesses with a reduced ability to withstand unplanned financial losses.

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[3] Ibid, p. 16.

Government intervention through the Act is necessary to facilitate prompt payment and preserve cashflow, and to resolve disputes quickly and efficiently. The NSW Government's statutory review determined that there is strong support for the continued operation of the Act. A key finding of the Review was that an opportunity exists to make enhancements to the Act to ensure that it more effectively deliver its objectives.

The proposed reforms in the Bill are designed to provide greater protection for subcontractors and promote cash flow and transparency in the contracting chain. It is considered that the reforms will provide significant benefits within the industry to prevent the high incidence of non-payment to contractors and subcontractors. In developing the reforms, a measured and balanced approach has been taken to ensure that any additional regulatory burden to businesses in the sector are minimal.

Further information on the regulatory impact of specific reforms is explained in the next chapter of this paper.

Outline of reforms to the Act

Rights to progress payments

Establishing a minimum monthly entitlement to a progress payment

References in Bill: [3] Section 8 Rights to progress payments; [1] Section 4 Definitions; [2] Section 4, definition of "progress payment"

This reform seeks to overhaul the definition of 'reference date' to provide a statutory minimum entitlement to a progress payment at least once per month, for work done within that month. Although any contractual term that attempts to avoid the monthly entitlement would be void, parties will have the freedom to agree that progress payment claims be made more frequently (for example, every 7 to 14 days).

Construction contracts may also incorporate provisions requiring payment to be made in a single or one-off instance, or according to milestones. Single or one-off payments are common in contracts that provide for a small quantity of construction work to be completed in a very short timeframe. Payment would then be provided on completion of work or a single supply of goods and payment on delivery, or both.

On the other hand, milestone payments are found in contracts where payment is to be made on the achievement of certain events, and require payment to be made where specific stages of work and/or services are delivered.

This reform is aimed at removing industry confusion about the definition and preventing the potential for a party to undermine the primary objective of prompt payment under the Act.

Stakeholder feedback received as part of the NSW review indicated that permitting a reference date to be determined under the construction contract may result in a party 'delaying' the occurrence of a reference date to the detriment of subcontractors who have no other option than to 'take it or leave it'.

The reform will simplify the operation of the Act in relation to entitlements for progress payments and ensures that the Act more effectively meets its primary objective of promoting cash flow.

This reform is consistent with recommendation 14 of the Murray Review which proposes that a person who has undertaken to carry out construction work (or who has undertaken to supply related goods and services) under a construction contract is able to make a payment claim for every named month, or more frequently is so provided under the contract.

Establishing an entitlement to a final progress payment after termination

Reference in Bill: [3] Section 8 Rights to progress payments

This reform will establish a statutory entitlement, where a contract has been terminated, to make a final progress payment for work carried out (or related goods and services supplied), up to the date of termination.

An entitlement to make a payment claim arises on the occurrence of a reference date, which may be determined by the contract, or if the contract is silent, is statutorily determined to be the last day of the month.

The High Court, in *Southern Han,*[4] recently determined that where a contract expressly provides for reference dates, these reference dates do not survive the termination of the contract. For example, a reference date of 3 July would be extinguished if the contract was validly terminated on 29 June.

Following this decision, it is alleged that a practice emerged whereby head contractors strategically wait until the work is completed, or close to completion, and then terminate the contract prior to a reference date, to prevent a claimant from making a final claim. This practice unfairly leaves a claimant 'out of pocket' for any work performed since their last progress payment. It also undermines a key objective of the Act, which is to ensure that subcontractors get paid for work they have done.

This reform is consistent with recommendation 17 of the Murray Review.

Shortening payment due dates

Reference: [4] Section 11 (1A) (a) Due date for payment and [5] Section 11 (1B) (a)

This reform shortens when progress payments become due and payable to head contractors and subcontractors.

The reform provides that:

- the timeframe for a progress payment to be made by a principal to a head contractor should be a maximum period of 10 business days (currently 15 business days), or earlier if provided in the contract
- the timeframe for a progress payment to be made by a head contractor to a subcontractor should be a maximum period of 20 business days (currently 30 days), or earlier if provided in the contract.

This reform has been developed in response to stakeholder feedback received as part of the NSW review. The feedback suggested that an unintended consequence of the 'maximum payment period' amendments made to the Act in 2014 had significantly extended the payment due date for payments to subcontractors in certain circumstances.

Prior to the 2014 amendments, a progress payment was due and payable on the date set out in accordance with the terms of the contract. The Act provided a 'default' payment due date of 10

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[4] *Southern Han Breakfast Point Pty Ltd (in liq) v Lewence Construction Pty Ltd* [2016] HCA 52.

business days after a payment claim was made if the contract was silent. The 10-business day default provision became redundant on introduction of the 'maximum payment periods' in the Act as these periods became the new defaults, unless contracts provided for a lesser period.

The maximum payment periods were designed to encourage the faster flow of money from the top of the contracting chain. These amendments followed recommendations of the Collins Inquiry to create a 'buffer' in the payment cycle. Collins QC said that such a buffer would:

> …give additional time to the head contractor who, by reason of its position standing in the middle of the contractual relationship, will then be able to benefit from additional time to pay its subcontractors thus improving its own 'cash flow' position…
>
> The buffer proposal is designed to deal with what the Inquiry has concluded is a wide spread practice of "robbing Peter to pay Paul". This juggling act commences when a head contractor finds that it does not have sufficient money from within the particular project pyramid in order to pay the subcontractors who have already done the work and submitted their progress payment claim to it. In that event what is commonplace in the industry is for the head contractor to look to other jobs by way of going to what some contractors call their "treasury" for the purposes of writing a cheque. This could have the effect of disadvantaging any of the subcontractors in other project pyramids.[5]

While these reforms successfully reduced the unacceptably long payment cycles that were found to be plaguing the industry (averaging 45 to 60 days), they inadvertently lengthened payment due dates for smaller operators. Stakeholders advised that these smaller operators who had 'informal contracts' relied on the benefit of the previous 10 business day default. For these stakeholders, the amendments lengthened payment due dates by 20 business days.

In determining what should be the appropriate due date for payment, a delicate balancing act is required between respecting the parties' freedom of contract and recognising the unequal bargaining powers of the parties. It is considered that the proposed shortening of maximum payment due dates (that is, 10 business days and 20 business days respectively) is appropriate to facilitate prompt payment.

It should be noted that reducing the timeframe when progress payments become due and payable will impact the administrative burden for businesses when assessing and responding to payment claims. However, following consultation with industry stakeholders, it is considered that such timeframes are achievable in practice with appropriate business management. The intention of this amendment is to facilitate prompt payment within the industry and any additional regulatory burden introduced is therefore considered necessary to achieve this.

The reforms do not currently reinstate the previous 10 business day default, however, stakeholders are welcome to provide feedback on whether this would be appropriate. Consideration would need to be given to the practical implications of this considering the reduced timeframes. The default would only be relevant for payments from a head contractor to

[5] Collins, B. QC (2012), *Final Report: Independent Inquiry into Construction Industry Insolvency in NSW*, November 2012, p. 365-366.

a subcontractor as the maximum payment period for payments from the principal to head contractors would already be mandated at 10 business days. Applying a default of 10 business days for payments from a head contractor to a subcontractor would remove the ‘buffer’ in the payment cycle.

In providing feedback on the Bill, stakeholders are also welcome to comment on the recent final report of the Murray Review. Recommendation 19 of the Review provides for a ‘maximum payment period’ of 25 business days, unless contracts provide for a lesser period. Where a contract is silent, the Review recommended a 10 business day default period.

Allowing inspection of trust account records

Reference: [6] Section 12A Trust account requirements for retention money

This reform relates to the existing obligation of a head contractor to hold retention money in trust for the subcontractor from whom the money has been retained. The head contractor must ensure that the money is paid into and retained in a trust account established with an approved ADI (see clause 6 of the *Building and Construction Industry Security of Payment Regulation 2008*).

This reform proposes the regulations make provision for the keeping of records by the head contractor in connection with the operation of the trust account and the inspection of those records by the subcontractor entitled to the retention money.

It is proposed that the regulations will provide that inspection of the records will be subject to the following conditions:

- the subcontractor is only entitled to inspect those records that relate to retention money specifically held in trust for them
- the subcontractor is only entitled to those parts of the records that relate to their retention money (that is, to preserve privacy, confidential information about retention money held for other subcontractors would need to be redacted)
- inspection is to be subject to a fee commensurate with the costs involved in providing access to records.

This reform is designed to increase transparency in the management practices of head contractors for retention money trust accounts. The ability to access information about the records will provide subcontractors with greater confidence that retention money is being appropriately held on trust and that such moneys will be available to them when rightfully due.

The reform will also serve as an additional safeguard in ensuring that head contractors are appropriately managing trust money outside of the existing notification requirements under the regulation. If, after inspecting the records, subcontractors have concerns about the management of the trust funds they can raise this with Fair Trading for investigation.

It is considered that this reform will not impose any additional administrative burden on head contractors as they are already obliged to maintain trust account records under clause 14 of the

Regulation. These records detail the amounts deposited into or withdrawn from the account. It is proposed that a head contractor will be able to charge an administrative fee to the subcontractor for the inspection of records.

There is already precedence in the common law for allowing inspections of trust records by beneficiaries. Under the common law, trustees are obliged to keep records of the dealings of the trust which must be produced to the beneficiaries when requested.[6] There is also precedence in other jurisdictions where similar measures have been adopted to facilitate greater transparency within the industry. For example, New Zealand has imposed a statutory obligation on trustees to ensure that the accounting records of all retention money held on trust for the benefit of a party are available for inspection by the party at all reasonable times.[7]

This reform is also consistent with recommendations in the Murray Review and the Collins Inquiry.

The proposed reform to the regulations for the inspection of records of the head contractor by the subcontractor will be drafted and released for public consultation at a later date.

[6] *Spellson v George* (1987) 11 NSWLR 300 at 315-6.
[7] Section 18FC, *Construction Contracts Act 2002.*

Recovering progress payments

Endorsement of payment claim

Reference: [8] Section 13(2)(c)

This reform re-inserts the requirement that a payment claim must include an endorsement that it is a claim being made under the Act.

This requirement was originally included in the principal Act but was removed in 2014 in response to the findings of the Collins Inquiry. The Collins Inquiry determined that this requirement was one of the factors that had led to an under-utilisation of the Act by subcontractors and, as such, should be removed. It was suggested that many subcontractors were hesitant to include such a statement in their payment claims to head contractors as this may be suggestive of potential dispute.

The decision to re-insert this requirement follows overwhelming stakeholder feedback received in support as part of the NSW review. Stakeholder feedback indicated that removing the requirement created significant problems and uncertainty for both respondents and claimants. Stakeholders agreed that a payment claim endorsed with a statement that it is made under the Act evidences a clear intention to engage the formal process under the Act. Stakeholders agreed that an endorsed payment claim alerts the recipient of the severe consequences if it fails to respond within the statutory timeframes by way of a payment schedule.

The reform is also consistent with recommendation 23 of the Murray Review. In the report, it was alleged that removal of the requirement:

> …has also exposed claimants to the potential risk of inadvertently having been taken to have made a claim under the Act when in fact they only intended the claim to have been made under the contract and so potentially having served more than one payment claim for each reference date contrary to section 13(5) of the NSW Act.[8]

This reform will add clarity to the practice of making progress payments under the Act. It may reduce disputes and the need for adjudication through removing any ambiguity about the status of a claim, and generally enhances transparency of existing processes and procedures.

Expressly provide for the withdrawal of adjudication applications

Reference: [14] Section 17A

The reform allows a claimant to withdraw an adjudication application at any time before the application is determined, provided they serve notice of the withdrawal on the respondent and the authorised nominating authority or the adjudicator.

[8] Murray, J. (2017), *Review of Security of Payment Laws: Building Trust and Harmony*, Department of Jobs and Small Business, Canberra, Australia, December 2017, p. 144.

While not expressly provided, this reform will allow a claimant to withdraw an adjudication application if the respondent has paid the amount which is the subject of the application, and the adjudicator is notified accordingly.

The Act currently implies that an adjudication application may be withdrawn or settled (s 29 (4)), but there is no express provision for withdrawal. A claimant is only able to withdraw an application to make a new application where an adjudicator has failed to comply with specified timeframes (s 26).

Section 29 of the Act already makes it clear that an adjudicator is entitled to be paid for the work done and expenses incurred. Under the reform, this provision will ensure that the adjudicator will be paid for their services up until the point of withdrawal.

The proposal seeks to promote the facilitation of timely payments and the rapid resolution of disputes by removing the need for adjudication to continue in circumstances where the issue in dispute has been resolved.

This reform is intended to have the same effect as recommendations 54 and 56 of the Murray Review. The Murray review indicated that clear withdrawal provisions would ensure that the Act would promote greater practicality. For example, where contracting parties had already resolved a disputed payment claim by other means, their resources and those of the adjudicator would no longer need to be spent unnecessarily.

Adjudicator to determine an application within 10 business days

References: [16] Section 21 Adjudication procedures; [17] Section 21(2); [18] Section 21(3)(a)

This reform will make the date of receipt of the adjudication response the trigger for commencing the 10-day deadline for an adjudication determination under the Act.

Currently, an adjudicator's timeframe for determining an adjudication application commences on the date that the adjudicator notified the parties that they accepted the application. In some cases, this means that an adjudicator does not have the adjudication response for consideration for the entire 10-day timeframe.

The reform will mean that adjudicators will have more time to consider an application and, more importantly, will have all relevant material before them when making the decision.

While this is only a marginal increase in the timeframes for adjudicators, the proposal ensures that the overall intention of providing a prompt and cost-effective mechanism for resolving building and construction payment disputes is not unreasonably compromised.

This reform will ensure that the timeframes are consistent with other Australian jurisdictions and with recommendation 42 of the Murray Review.

Regulating Authorised Nominating Authorities

Code of practice for authorised nominating authorities (ANAs)

Reference: [24] Section 28A

This reform provides the Minister with the ability to make a Code of Practice (Code) to be observed by an ANA in relation to its activities under the Act.

ANAs are responsible for receiving adjudication applications and appointing adjudicators for payment claim disputes. In discharging these functions ANAs provide an important support and advisory service to parties in relation to the adjudication procedure under the Act.

It is proposed that the Code will outline and clarify expectations, responsibilities and obligations when undertaking their functions under the Act. Specifically, it is proposed that the Code will address matters in relation to conduct, assessment and selection, training and monitoring of adjudicators, as well as complaint handling procedures.

The Code will replace the existing arrangement whereby an ANA provides the Minister with an undertaking to abide by a Code when applying for an authority under the Act. Replacing this arrangement with a Code that is established under the Act will remove any ambiguity as to whether the existing Code is enforceable. It also provides an opportunity to make best practice improvements to the existing Code, which has remained largely unchanged over the last 10 years.

Failure to comply with the Code will attract a maximum penalty of 50 penalty units. The Minister may also exercise their power to withdraw the authority of the ANA to nominate adjudicators.

An enforceable Code addresses concerns raised by stakeholders as part of the NSW review about the function and effectiveness of ANAs. Feedback received from stakeholders highlighted concerns about the independence of the adjudicator selection process. Stakeholders also emphasised the potential for perceptions of bias and/or conflicts of interest in the current system of adjudication, which operate to erode confidence in the adjudication process.

Formal implementation of the Code will prescribe an accessible, adaptable and enforceable mechanism within the industry, which outlines expected standards of conduct and practices for ANAs and adjudicators in the discharge of their functions. Specifically, the Code will draw upon principles of honesty and fairness, accountability and transparency, and impartiality in processes and procedures.

Implementation of the Code is consistent with the policy intent of recommendation 60 of the Murray Review, which provides for the regulatory oversight of ANAs.

The Code will be drafted and released for public consultation at a later date.

Miscellaneous matters

Supreme Court power to sever and remit adjudication determinations

Reference: [30] Section 32A

This reform expressly enables the Court, where appropriate, to sever part of an adjudicator's determination that is affected by jurisdictional error and, in the process, confirm that the balance of the adjudication decision remains enforceable.

This reform will help dissuade parties from challenging unfavourable decisions. It will also remove the incentive for a party to challenge a decision with only minor mistakes in an attempt to have the entire decision set aside.

In NSW, jurisdictional error currently invalidates the whole of an adjudicator's determination even where the error is confined to one part of the determination.[9]

This amendment is likely to decrease the amount of time taken to finalise an adjudication in relation to the Act. It is unlikely to have a regulatory impact on either party.

Introduction of this amendment is consistent with recommendation 57 of the Murray Review.

Prohibiting a corporation in liquidation from making payment claims

Reference: [30] Section 32B

This reform expressly provides that the Act does not apply to a claimant corporation that is in liquidation.

Specifically, the reform provides that a corporation in liquidation cannot serve a payment claim on a person or take any action to enforce a payment claim (including by making an application for adjudication of the claim) or an adjudication determination.

Further, the reform provides that if a corporation in liquidation has made an adjudication application that is not finally determined immediately before the day on which it commenced to be in liquidation, the application is taken to have been withdrawn on that day.

The purpose of the Act is to assist claimants to maintain cash flow throughout the duration of a construction project, and to enable claimants to obtain payment on an interim basis but preserving the parties' final rights — 'pay-now-argue-later'.

If the corporation claimant is liquidated:

- the claimant no longer needs the cash flow to run its business

[9] See, for example: *Multiplex Constructions Pty Ltd v Luikens & Anor* [2003] NSWSC 1140 at [91] - [92]; See also: *Watpac Constructions (NSW) Pty Ltd v Austin Corp Pty Ltd* [2010] NSWSC 347 at [15] – [33].

- any payments by a respondent under compulsion of the Act to that claimant would, in effect, convert an interim payment into a final payment.

The policy proposition is that, for insolvent claimants, payment would not assist the company's cashflow and would therefore not go toward completing the construction project. Prohibiting claimants in liquidation therefore provides clarity as to the purpose of the Act, which has recently been subject to significant judicial attention in Victoria and NSW.

This reform is consistent with recommendation 10 of the Murray Review.

Investigation and enforcement powers

The following reforms implement standard compliance and enforcement powers that are common in other acts administered by Fair Trading. These reforms are all located in the new Part 3A of the Act for ease of reference by investigators and parties affected by the legislation.

Appointment of authorised officers

Reference: [31] Part 3A, Sections 32C, 32D

The reforms will enable an authorised officer appointed under the Act to investigate and enforce compliance with the Act more broadly than present. Currently, an authorised officer can only be appointed for the specific purpose of investigating compliance with payment claims, as in sections 13 (7) and 13 (8).

Specifically, the reforms provide that an authorised officer's powers may be exercised for the purposes of:

- investigating, monitoring and enforcing compliance with the requirements of the Act
- obtaining information or records connected with the administration of the Act
- enforcing, administering or executing the Act.

Under the reform an authorised officer will include an investigator appointed under section 18 of the *Fair Trading Act* to streamline the appointment process of authorised officers.

Standard information sharing provisions

Reference: [33] Section 36 Disclosure of information

This reform adopts and is consistent with standard information sharing provisions contained in other legislation administered by Fair Trading.

The sharing of information will only be permissible in accordance with s 23 of the *Privacy and Personal Information Protection Act 1998* (NSW). Accordingly, information must not be disclosed unless that disclosure is made:

- with consent obtained from the affected person
- in connection with the administration or execution of the Act
- for the purposes of any legal proceedings under the Act
- in accordance with the requirements of the *Ombudsman Act 1974*
- with other lawful excuse.

To ensure consistency with other legislation administered by Fair Trading, the maximum penalty for disclosing information outside permissible instances will be reduced from 200 to 100 penalty units.

Where information sharing occurs between law enforcement agencies the use and disclosure of information will be supported by existing formal procedures, and incorporated into interagency memoranda of understandings between parties to clarify the obligations of parties. This will facilitate greater transparency in law enforcement procedures and in turn enhance public confidence in law enforcement. Accordingly, it is understood that this amendment is consistent with existing compliance and enforcement powers and, as such, will not adversely impose any additional regulatory impact on contracting parties.

Compliance and enforcement powers and associated offences

Reference: [31] Sections 32F – 32J

The reforms confer additional compliance and enforcement powers under the Act, in line with other legislation administered by Fair Trading. Specifically, the reforms introduce powers to:

- request, inspect and take possession of documents (s 32F)
- ask and require answers to questions (s 32G)
- enter premises (ss 32H, 32I)
- obtain a search warrant. (s 32J)

These powers are to be exercised only where necessary and when investigating complaints of non-compliance with the Act, as well as when obtaining information in relation to a contravention under the Act.

Reforming compliance and enforcement powers is necessary to ensure compliance with the Act and to guarantee the ability of the Act to provide for the prompt payment of contractors down the contracting chain.

The powers are supported by 'standard' offences necessary to provide a robust enforcement mechanism and ensure compliance with these powers.

The offences include, providing false or misleading information and intentionally delaying or obstructing an authorised officer in the exercise of their functions. Further, breach of these standard provisions attracts a maximum penalty of 1,000 penalty units for a corporation and 200 penalty units for an individual.

Introduction of these new offences will require increased enforcement to facilitate greater compliance with the Act within the building and construction industry. Although implementation of these provisions may present some administrative and regulatory burden, the intended outcomes are proportionate to achieving the objects of the Act and ensuring its efficacy.

Updating penalty units

References: [9] Sections 13(7); [10] 13(8); [21] 26A (5); [22] 26B (5); [23] 26D (3); 26E (2) and (3); [31] 32O

Reforms have updated penalty units for offences under the Act. The reforms ensure that the penalties provide an effective deterrent to the commission of an offence. The updated penalties reflect the severity of the offence within the operation of the security of payment framework.

The proposed penalties are aligned with existing offences of a similar nature — or of a similar degree of seriousness — as in other regulatory legislative schemes administered by Fair Trading. **Appendix A** provides a table of the updated penalties with further detail.

The severity of the penalties in the Regulation is designed to ensure that retention money is appropriately accounted for, and attracts a penalty commensurate with the objective seriousness of the offences. Where incidents of non-compliance occur, such as where retention money is misappropriated and not available for payment to subcontractors, the amendment will introduce penalties that are appropriate and proportionate to such conduct.

These offences are pre-existing in the legislation and therefore the proposed amendment will not carry an additional regulatory impact.

Prescribing penalty infringement notice offences

Reference: [32] Section 34B

This reform provides an authorised officer with the ability to issue a penalty infringement notice to a person or corporation where it has contravened the Act. The offences subject to penalty infringement notices will be set in the regulations. **Appendix B** outlines the proposed penalty note offences.

Penalty notices are an effective mechanism of compliance that sends a direct and immediate signal about the importance of ensuring security of payment for subcontractors in the building and construction industry.

The ability of authorised officers to issue and enforce penalty notices provides an efficient and cost-effective means of regulating the security of payment framework. In the alternative, where penalty notices are contested, a recipient may elect to pursue the matter through court, which may be disproportionately costly and time consuming.

The *Fines Act 1996* (NSW) will extend its application to penalty infringement notices issued to offending recipients within the building and construction industry. Accordingly, the infringement notice may then be pursued for internal review, as per Division 2A of the *Fines Act 1996*. Further, where a party remains aggrieved by the decision of the internal review, the matter may then be pursued further through court election.

The proposed amendment will facilitate the quick resolution of more minor offences committed under the Act and serves as an important enforcement mechanism to bring about behavioural change within the building and construction industry. It provides an alternative method of enforcement, thereby promoting timely action and reduced legal costs, while achieving the purposes of the Act. This amendment is unlikely to increase the regulatory impact on contracting parties.

The proposed reform to the regulations to prescribe penalty notice offences will be drafted and released for public consultation at a later date.

Introducing accessorial and executive liability

Reference: [32] Sections 34C and 34D

This reform will ensure that directors and other individuals involved in the management of a corporation are held liable for their involvement in contraventions of the Act.

The reforms will apply accessorial liability to all offences under the Act which are capable of being committed by a corporation. Specifically, liability will extend to a person who is involved in contravention where the person:

- aids, abets, counsels or procures the commission of the corporate offence
- induces, whether by threats or promises or otherwise, the commission of the corporate offence
- conspires with others to effect the commission of the corporate offence
- is in any other way, whether by act or omission, knowingly concerned in, or party to, the commission of the corporate offence.

The reforms will also apply executive liability only to the most objectively serious offences under the Act (see **Appendix C**). Extending these principles of liability for contravention of the Act is crucial to enhance compliance with the Act and to ensure that workers are paid for work performed.

There are compelling public policy reasons for imposing personal criminal liability on a director for the misconduct of a corporation. Corporate misconduct has the potential to cause significant public harm and undermine confidence in financial markets. Moreover, introduction of these principles prevents the ability of directors to be shielded by the corporate veil. Corporate misconduct has wider ramifications not only on individuals but also in relation to employment, growth and business reputation. The liability of a corporation on its own is unlikely to promote compliance with the Act. Extending liability to pierce the corporate veil ensures that directors actively take appropriate steps to ensure compliance with the Act.

In 2015 the report of the Senate Economics References Committee highlighted a culture among some company directors in the construction industry to disregard corporations law. The Report found that some company directors consider compliance with the Corporations Act optional because the consequences of non-compliance are mild and the likelihood that unlawful conduct will be detected and addressed is low.

Incorporation of these provisions and offences acknowledges the role of directors in their capacity to influence the conduct of the corporation. Extending liability to directors promotes compliance with the Act. Further, these provisions will serve to encourage directors to take reasonable steps to ensure their compliance with legislative obligations and to mitigate any potential risk of non-compliance due to the penalties that may be attracted. Section 34D (7) of the Bill outlines reasonable steps, in relation to the commission of an executive liability offence.

Accordingly, the prosecution will bear the legal burden of establishing the elements of the accessory and executive liability offences.

Corporations will likely need to implement additional practices in relation to financial and business management to ensure compliance with these provisions. The amendment, however, is still considered balanced and appropriate, given the public policy considerations discussed above.

Commencement of proceedings

Reference: [32] Section 34A

This reform will increase the statutory limitation period for the commencement of proceedings to two years for offences under the Act.

Extension of the statutory period to commence proceedings will enable Fair Trading to respond to and prosecute contraventions of the Act. Specifically, a two-year extension will also provide the opportunity to resolve complaints where informal attempts have been unsuccessful.

Currently, proceedings for an offence under the Act may be dealt with summarily by the Local Court and, as such, must be commenced within six months from when the offence was allegedly committed (s 179 *Criminal Procedure Act 1986*).

The six-month limitation period has restrained Fair Trading from prosecuting offences. Since the transfer in administration of the Act in 2015, Fair Trading has been unable to pursue 18 instances of non-compliance due to a statute bar that hinders potential prosecution.

Changing the statutory period for the commencement of proceedings will not increase the regulatory burden on contracting parties.

Minor drafting revisions

The Bill also includes minor revisions which have been made to update and improve the drafting of the Act and clarify its intended operation.

These reforms include:

[7] Section 13 Payment claims – revises language in section 13.

The following reforms clarify language for service of notices:

[12] Section 17 Adjudication applications

[13] Section 17(3)(b)

[15] Section 20 Adjudication responses

[19] Section 22 Adjudicator's determination

[20] Section 23 Respondent required to pay adjudicated amount

[25] Section 31 Service of documents

[26] Section 31(1)(d) and (d1)

[27] Section 31(1)(e)

[28] Section 31(3)

[29] Section 31(4).

Proposed reforms to the Regulation

The proposed reforms to the Regulation will be drafted and available for consultation at a later date. Discussion of the proposed reforms is included here for completeness. Stakeholders are welcome to comment on these proposed reforms in their submissions.

Reducing the threshold for retention money trust requirements

Proposed amendment to clause 5

It is proposed that the amended clause will extend trust obligations for retention moneys in order to protect more construction projects.

The Regulation currently requires head contractors to pay retention moneys into a trust account for construction projects valued over $20 million. This provision will reduce the threshold from projects with a value of at least $20 million to projects with a value of at least $10 million.

During the NSW review, stakeholders expressed divergent views on this reform proposal. Those stakeholders in support favour extending the retention money trust requirement to the entire contracting chain and proposed to remove the threshold requirement altogether. On the other hand, some stakeholders opposed this provision as unnecessarily burdensome.

Streamlining the annual reporting requirements (discussed below) will moderate any increased regulatory burden and addresses divergent stakeholder views.

The Murray Review and Collins Inquiry supported expanding retention money trust requirements to all contracting parties under security of payment legislation. Both argued that the administrative burden of a trust was necessary to counter head contractors misusing and withholding retention moneys due to subcontractors.

The proposed reforms moderate the impact of imposing trustee obligations on small businesses by retaining a threshold for trustee obligations for contracts over $10 million. The reform, however, is consistent with the policy intent of recommendation 81 of the Murray Review insofar as it seeks to expand the use of trusts for retention money.

Inspection of trust account records

Proposed amendment to clause 14

As noted above, it is proposed that the Regulation will be amended to allow the subcontractor to inspect the retention money trust account records held by the head contractor.

This proposed reform will be drafted and released for public consultation at a later date.

Streamlining retention money trust reporting requirements

Proposed repeal of clause 16

It is proposed that the Regulation will be amended to remove the annual reporting requirements in clause 16.

Currently, head contractors are subject to several reporting requirements. The most significant reporting requirement is the obligation to submit an annual report on the operation of the trust account to Fair Trading. It has been estimated that the cost of conducting the account review report ranges between $3,000 and $10,000 depending on the complexity of the accounts.

Some stakeholders expressed concerns that the annual reporting requirements are onerous and encourage head contractors to take out bank guarantees in place of retention. It is considered that this practice could have a detrimental impact on some subcontractors, who cannot afford to obtain a bank guarantee, or do not have sufficient security to satisfy one. This may lead to lost work and contribute to financial stress.

This reform will seek to moderate the increased regulatory burden that will result from reducing the threshold from $20 million to $10 million. The strengthened compliance and enforcement framework will allow Fair Trading to adopt a risk-based compliance program, and conduct investigations where necessary. The proposed reform should alleviate concerns about non-compliance. In further support of adopting this approach, it is noted that the reform to provide subcontractors with a right to inspect retention money trust records is also likely to incentivise greater levels of self-regulation.

This proposed reform will be drafted and released for public consultation at a later date.

Prescribing penalty notice offences

As noted above, it is proposed that the Regulation will be amended to prescribe penalty notice offences as set out in **Appendix B**.

These proposed reforms will be drafted and released for public consultation at a later date.

Appendix A

Changes to penalty units

Offence	Description	Maximum penalty in penalty units (pu)
S 13(7)	Supporting statement not attached to payment claim	1,000 pu for corporation 200 pu for individuals
S 13(8)	Supporting statement is false or misleading	1,000 pu for corporation 200 pu or 3 months imprisonment for individuals
S 26A (5)	Not notifying changed circumstances	50 pu for corporation 10 pu for individuals
S 26B (5)	Not serving copy of adjudicator's determination	
S 26D (3)	Not giving notice of withdrawal of adjudication application	
S 26E (2)	Not providing identity and contact details of principal contractor	
S 26E (3)	Respondent providing false or misleading information	
S 32O	Failing to comply with notice or providing false or misleading information	1,000 pu for corporation 200 pu or 3 months imprisonment for individuals
Cl 6(1)	Head contractor not holding retention money on trust	1,000 pu for corporation 200 pu for individuals
Cl 7(3)	Not notify Secretary of matters	
Cl 8	Head contractor withdrawing from trust account for non-legitimate purpose	
Cl 11	Head contractor fails to notify of overdrawn trust account	
Cl 12	Head contractor fails to notify of closure of trust account	
Cl 14	Head contractor fails to retain trust account records	
Cl 15(3)	Failing to provide information in response to request	
Cl 17	Providing false or misleading information	

Appendix B

Proposed penalty notice offences and amounts

Offence	Description	Penalty notice amount
S 13(7)	Supporting statement not attached to payment claim	$2,200 for individuals $11,000 for corporations
S 26A (5)	Not notifying changed circumstances	$110 for individuals $550 for corporations
S 26B (5)	Not serving copy of adjudicator’s determination	
S 26D (3)	Not giving notice of withdrawal of adjudication application	
S 26E (2)	Not providing identity and contact details of principal contractor	
Cl 6(1)	Head contractor not holding retention money on trust	$2,200 for individuals $11,000 for corporations
Cl 7(3)	Not notify Secretary of matters	
Cl 8	Head contractor withdrawing from trust account for non-legitimate purpose	
Cl 11	Head contractor fails to notify of overdrawn trust account	
Cl 12	Head contractor fails to notify of closure of trust account	
Cl 14	Head contractor fails to retain trust account records	
Cl 15(3)	Failing to provide information in response to request	

Appendix C

Executive liability offences

Offence	Description	Penalty units	Penalty notice
S 13(7) (in Bill)	Supporting statement not attached to payment claim	1,000 pu for a corporation 200 pu in any other case	Yes
S 13(8) (in Bill)	Supporting statement is false or misleading		No
Cl 6(1) (proposed Regulation)	Head contractor not holding retention money on trust		Yes
Cl 8 (proposed Regulation)	Head contractor withdrawing from trust account for non-legitimate purpose		Yes
Cl 11 (proposed Regulation)	Head contractor fails to notify of overdrawn trust account		Yes
Cl 12 (proposed Regulation)	Head contractor fails to notify of closure of trust account		Yes
Cl 14 (proposed Regulation)	Head contractor fails to retain trust account records		Yes
Cl 15 (proposed Regulation)	Failing to provide information in response to request		Yes
Cl 17 (proposed Regulation)	Providing false or misleading information		No