

16th September 2018

Security of Payment: Consultation Paper
Department of Finance, Services and Innovation
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Adjudicate Today response to the proposal for “deemed” statutory trusts in the Building and Construction Industry

We commend and thank the NSW Government for this opportunity to provide feedback on the ‘deemed’ statutory trusts (trust) consultation paper.

Definition of Money subject to a “deemed” statutory trust

In our consultation with industry stakeholders and adjudicators, there is uncertainty as to the money which will be subject to a trust. Particularly, whether the trust includes money which is being claimed for payment but is not paid into the trust.

The trust proposed by both the Murray and Collins Reviews does not and cannot include payments claimed but not paid into the trust.

The Bill should clearly define money subject to the trust. We suggest:

***“Money to be held in trust is all money for which a progress claim has been certified and a payment made in respect of that claim. The contractor, subcontractor, sub-subcontractor and/or supplier who receives that payment will hold the payment in trust for those to whom it is rightfully due.*”**

The beneficiaries of the trust are those who have made a claim which has been certified for goods and services provided to the project and the money for the claim paid into the trust.”

Recommendation 85 of the Murray review provides:

“A deemed statutory trust model should apply to all parts of the contractual payment chain for construction projects over \$1 million. The deemed statutory trust model outlined in the Collins Inquiry provides a suitable basis”.

At page 311 under the heading “Support for specific recommendations of the Collins Inquiry”, Mr Murray outlines the basis of the Collins recommendation:

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“In establishing a deemed statutory trust model, the specific recommendations of the Collins Inquiry, which I consider relevant, and which I endorse, are as follows.

“Any payment by a principal to a head contractor or by a head contractor to a subcontractor on account of, or in respect of, any work done or materials supplied by the head contractor, any subcontractor, sub-subcontractor or supplier whether as a result of a favourable adjudication under SOPA or not, shall be made and treated in the following way:

- any cheque drawn upon a bank account in favour of the head contractor in respect of such work shall be held on trust for the head contractor, subcontractor, sub-subcontractor and supplier; and
- the proceeds of any such cheques when banked will be held upon the same trust for the head contractor, subcontractor, sub-subcontractor and supplier;
- where moneys are paid by electronic transfer they will be deemed to be held in trust by the head contractor the instant they are received by electronic transfer from the principal.”

The statutory construction trust requirement should apply to all building projects valued at \$1 000 000 or more.

The statutory construction trust will be established for the purposes of paying the subcontractors and suppliers”.

Both Reviews are referring to income received into a trust, meaning:

- a) money paid by the principal into a trust account for a contractor as a consequence of a claim received by the principal and certified for payment by the superintendent/principal; and/or
- b) money paid by a contractor into a trust account for a subcontractor as a consequence of a claim received by the contractor and certified for payment by the contractor; and/or
- c) money paid by the subcontractor into a trust account for a sub-subcontractor as a consequence of a claim received by the subcontractor; and certified for payment by the subcontractor;
- d) and continuing down the contractual chain.

At page 298, Mr Murray quotes the summary by Mr Collins in response to opposition to the concept of a statutory trust:

“After many discussions with interested parties upon the subject of the introduction of the construction trust the overwhelming evidence demonstrates that opposition to the introduction of the construction trust is born out of misunderstanding. That is not too difficult to appreciate because the genius of the trust is that it is not an impediment yet at the same time it is the most effective guarantee against the loss of moneys that should have been passed on to the subcontractor. By far the greater part of the opposition to the construction trust may be put down in the view of the Inquiry to the perfectly understandable lack of knowledge in the building and construction industry of the trust device itself”.

As stated at page 12 of the consultation paper:

“The primary aim of this model is to ensure that when the time arrives for a progress payment in accordance with the relevant statutory provisions that the monies remain protected. Accordingly, a party, as the trustee, is required to be able to account for the monies at all times and ensure that it is available for payment to the beneficiaries in full, in response to a payment claim.

In addition, the party, as trustee, is obliged to only use the monies for their intended purpose. A separate, segregated bank account, is ordinarily (but not always) required to ensure a party fulfils its obligations as a trustee.”

Adjudicate Today is an Authorised Nominating Authority. Our responsibility is to nominate adjudicators to determine payment disputes in the building and construction industry.

In answering the thirty-one (31) questions posed, our focus is on the issues applicable to adjudication.

1 Do you support the proposal to establish deemed statutory trusts in the Act?

Yes.

In saying yes, we are assuming the proposal is as described by Mr Collins at page 150 of his report:

“Any moneys paid under a contract by an owner to a contractor, or by the owner or contractor to a subcontractor for work done or materials furnished, or both, for or about a building by any subcontractor, shall be held in trust by the contractor or subcontractor, as trustee, for those subcontractors who did work or furnished materials, or both, for or about the building, for purposes of paying those subcontractors.”

The Bill will require transitional provisions to allow time for education of industry participants. We propose a period of three (3) months for training and that the trust provisions apply only to new contracts made after the commencement of the amendments.

As previously observed, the Bill should carefully define ‘money’ that will fall within the purview of the trust.

2. What alternative reform(s) could be implemented?

None.

3. Do you support the proposal to apply a cascading ‘deemed’ statutory trust model?

Yes.

In addition, money paid from a trust in compliance with an adjudication determination should discharge all trustee duties and obligations, regardless of the outcome of any subsequent court or other dispute resolution proceedings.

4. What would be an appropriate point in the contractual chain to limit the requirement for ‘deemed’ statutory trusts?

None.

We support the Murray review recommendation that trusts should apply to all contracts made under a head contract with a value of \$1,000,000 or more.

Any head contract with a value of \$1,000,000 or more should provide that it is a contract to which trusts apply and require that statement be inserted in all contracts made under the head contract regardless of the value of that sub-contract. In the event of default, a penalty, expressed in penalty units, should apply.

We acknowledge strong industry support for no limitation i.e. the trust should apply to all contracts regardless of value. We are concerned that this may be too much for smaller subcontractors to immediately understand and implement and there will be many breaches of SOPA. We recommend, by way of compromise, that the \$1,000,000 threshold be subject to mandatory review by Mr Murray after two (2) years.

5. Do you support the proposal to apply the requirement for 'deemed' trusts to construction projects valued at \$1 million or more?

Yes, see response to question 4 above.

6. What would be an appropriate alternative monetary threshold?

An alternative monetary threshold is that there is no threshold and that trusts apply to all contracts made in the industry. However, the \$1,000,000 threshold should be implemented first and reviewed after operating for two (2) years. With the benefit of the review, government and industry participants will be better able to assess whether the monetary threshold should be removed.

7. Do you support the proposal to limit the application of the requirement to parties based on the value of their individual contracts?

No.

8. What would be an appropriate contract value?

Not applicable.

9. Do you support the proposal that the requirement for a deemed trust should arise immediately when the contract monies are received by the trustee?

Yes.

As previously discussed, money subject to the trust must be clearly defined and identifiable.

10. What would be an appropriate point in the contract lifecycle for the deemed statutory trust to be established?

When the money is received by the trustee.

11. Do you support the proposal that responsibility for managing 'deemed' trust monies is placed on the trustee?

Yes.

12. Do you support the proposal to allow trust monies on multiple construction projects to be held in a consolidated account?

Yes.

A trustee should be required to operate a single trust account which can accommodate multiple construction projects.

13. Should there be any further obligations applied to trustees and/or beneficiaries to support the efficient flow of monies in/out of accounts (for example, a requirement for transaction certificates of some form)?

Any payment from a trust account should state the name of the trust account from which the payment is made.

14. Do you support the proposal to not require auditing of trust records?

No.

If pooling or co-mingling of trust monies for multiple construction projects is allowed, the accounts should be subject to an annual audit.

If an individual trust account is required for each project, an annual audit of each account would not be necessary.

15. Do you consider that the compliance and enforcement powers proposed in the exposure draft bill are sufficient to support the operation of 'deemed' statutory trusts?

Regardless of whether co-mingled trust accounts or individual trust accounts are established, the compliance and enforcement powers of the exposure draft bill are supported.

16. What type of compliance and enforcement powers or framework would be preferred?

As proposed by the exposure draft bill.

17. Do you support the proposal to allow the trustee to withdraw funds from the account before a subcontractor has been paid?

No.

This provision is contrary to the object of the draft exposure bill. The second object is:

“(b) to reduce the period required to elapse after a head contractor or subcontractor makes a payment claim before payment of the claim becomes due and payable.”

It is also contrary to the speedier resolution of disputes as identified on page 24 of the consultation paper under the heading “Statutory trusts can create efficiencies”.

If trustees can dip into trust funds to pay themselves before all beneficiaries are paid, the trust will have little purpose. Certainly, the incentive to quickly settle all claims for payment will be lost. In all probability, the existing practice of using funds for cashflow, being funds which are owed to others, will continue. In the event of insolvency, it is most unlikely that funds to pay the legitimate claims would be available. Many of the benefits of the trust would be lost.

18. When should a trustee be permitted to withdraw funds?

A trustee should withdraw funds only after the claims of all subcontractors (beneficiaries of the trust) have been agreed or adjudicated and paid.

19. Do you support the proposal to allow funds to be distributed on a pro rata basis as a proportion of their payment claims?

In the event of insolvency, yes.

Other than insolvency, no.

In the event of a shortfall in funds, other than insolvency, the trustee should be obliged to make good the shortfall from their own resources. If the shortfall is a result of a payment dispute in which the trustee is the claimant, adjudication is available.

A shortfall in a trust account may arise for a legitimate reason. By way of example. The subcontractor has served a payment claim of the contractor who has certified (approved) payment and has added their margin into the payment claim they make on the principal. The principal refuses full payment because they allege “defect in work” or “liquidated damages”.

This shortfall of money in the trust should be covered from the trustee’s own resources until adjudication, or other dispute resolution option, determines the payment dispute.

20. What other model of distribution would be preferred?

None. Refer answer to question 19.

21. Do you support the proposal relying on the existing dispute resolution mechanisms in the Act?

Yes.

22. Are any new or amended mechanisms required?

As previously observed at question 3, money paid from a trust in compliance with an adjudication determination should discharge all trustee duties and obligations, regardless of the outcome of any subsequent court or other dispute resolution proceedings.

23. Do you support the proposal to allow the investment of ‘deemed’ statutory trust monies?

Yes, as provided by the Trustee Act 1925.

24. Are any further provisions necessary to support the operation of this proposal?

No.

25. Do you support the proposal to allow the beneficiaries to inspect the records of ‘deemed’ trust accounts?

Yes.

In our submission on the exposure draft bill, we note that a beneficiary seeking to exercise such a right may be subject to coercive or threatening conduct. We support immediate implementation of the Murray review recommendation 76:

“The legislation should make it an offence to use coercive and threatening conduct, whether directly or indirectly, in relation to a person’s statutory rights to, or claim for, a progress payment under the legislation.

Clause 32A of the Building and Construction Industry Security of Payment (Review) Amendment Bill 2017 (SA) provides a suitable model.”

26. Is there an alternative approach that would provide beneficiaries with a similar degree of awareness?

No, see response to question 25.

27. Do you support the proposal to apply executive liability to directors and other relevant persons for breaches?

Yes

In the discussion paper, we assume use of the term 'person' includes corporations. We note trustees can be corporations. The Bill should provide that executive liability applies to the directors and management of corporations as proposed in the discussion paper.

28. Do you consider these are the likely benefits associated with the proposal?

We agree with the description of likely benefits.

29. Are there any other significant benefits that are relevant?

None that come to mind.

30. Do you consider these are the likely costs associated with the proposal?

Yes.

A trustee who has certified a claim for payment and not received funds to cover the payment must cover the shortfall with their own resources. They are not relieved of their trustee obligations. If a payment claim is made by the trustee on the principal and is disputed, adjudication is available.

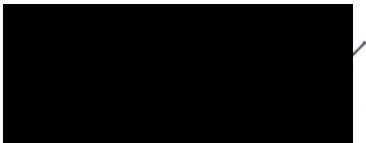
Claims which are the subject to a dispute cannot be included for certification nor drawn by any party. Thus, for example, the claim by a subcontractor which is disputed by the builder cannot be included in the claim made by the builder on the client.

31. Are there any other significant costs that are relevant?

No.

Adjudicate Today is available to discuss these and any related issues with government.

Yours sincerely

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Bob Gaussen

Owner