



Finance,
Services &
Innovation

Security of Payment Reforms – Implementation

Options Paper – December 2018



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Introduction

The *Building and Construction Industry Security of Payment Amendment Act 2018* (the Amendment Act) was assented to on 28 November 2018. The Amendment Act contains reforms to the *Building and Construction Industry Security of Payment Act 1999* (the Act) to promote cash flow in the supply chain, increase transparency of payments and provide greater protections to subcontractors. The changes are the result of extensive consultation with a broad range of stakeholders in the building and construction sector.

Key reforms include:

- reducing the maximum time a head contractor has to pay a subcontractor from 30 business days to 20 business days,
- creating a new payment structure so subcontractors can make a payment claim at least once per month for work and make a final claim if a contract is terminated, and
- increased compliance and enforcement powers for Fair Trading.

The Amendment Act has not commenced. Some of the reforms require subordinate legislation and administrative changes before they can be implemented. Other reforms are likely to impose significant changes to industry practices which means that it would be appropriate to provide a transitional period before they commence. This Paper proposes various options for commencing each reform and seeks feedback on that approach. This Paper is being released now to ensure that the Amendment Act can commence as soon as reasonably possible.

Fair Trading would also like to use the opportunity to seek initial feedback on the matters that will be included in the amending Regulation. This feedback will be used to assist in the drafting process and allow for an exposure draft amending Regulation to be released for public comment in early 2019.

Have your say

We invite you to read this paper and provide comments. You may wish to comment on only one or two matters of particular interest, or all of the issues raised.

We prefer to receive submissions by email and request that any documents provided to us are produced in an 'accessible' format. Accessibility is about making documents more easily available to those members of the public who have some form of impairment (visual, physical,

cognitive). Further information on how you can make your submission accessible is contained at <http://webaim.org/techniques/word/>.

If you do not wish for your submission or any part of your submission to be published, please indicate this clearly in your submission together with reasons. Automatically generated confidentiality statements in emails are not sufficient. You should also be aware that, even if you state that you do not wish certain information to be published, there may be circumstances in which the Government is required by law to release that information (for example, in accordance with the requirements of the *Government Information (Public Access) Act 2009*).

How to lodge your submission

You can provide a submission by email to securityofpayment2018@finance.nsw.gov.au or by post to the following address:

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

Submissions close **COB 28 January 2019**.

Next steps

All submissions received will be acknowledged. Once the consultation period has closed, feedback will be analysed and all potential options assessed. More information about the progress of the implementation of the Security of Payment reforms will be made available from time to time on Fair Trading's website at www.fairtrading.nsw.gov.au.

Commencement options

Fair Trading has considered the potential impact of each reform in the Amendment Act and various commencement options.

Reforms commenced with minimal transitional period

The following reforms have been identified as reforms which do not require either subordinate legislation or significant preparation time by industry stakeholders. Accordingly, it is considered that this set of reforms could commence in early 2019.

Investigation and enforcement

The Amendment Act provides for a more robust investigation and enforcement framework by implementing the standard suite of investigation and enforcement powers used in other laws administered by Fair Trading. Specific reforms include the standard powers for authorised officers to gather information and enter premises for investigating, monitoring and enforcing compliance, and administering the Act (clauses 34 and 37). Further, the statutory limitation period for commencing offence proceedings will be extended to two years (clause 35).

Increased penalty units for offences

These reforms will update penalty units for offences under the Act, ensuring that the penalties provide an effective deterrent to the commission of an offence (clauses 13-14, 21, 23 and 25).

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 (or both) for individuals
S 26A (5)	Not notifying changed circumstances	50 pu for corporation
S 26B (5)	Not serving copy of adjudicator's determination	10 pu for individuals
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	
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Executive Liability offences

Directors and people involved in the management of companies will be held responsible for the commission of corporate offences. The reforms will apply accessorial liability to all offences under the Act which are capable of being committed by a corporation (clause 35). The reforms will also apply executive liability to the offences in section 13 for non-compliance associated with supporting statements (clauses 15 and 35).

Supreme Court power to sever

New powers will enable the Supreme Court, where appropriate, to sever part of an adjudicator's determination affected by jurisdictional error and, in the process, confirm the balance to be enforceable (clause 33).

Prohibiting a corporation in liquidation from making payment claims

Reforms will prevent a corporation in liquidation from serving or enforcing a payment claim, ensuring the Act operates consistently with the object of promoting cash flow (clause 33).

Extended circumstances for releasing withheld money

This reform will permit the release of withheld money where an adjudication application is withdrawn, or an adjudicator fails to determine the application within timeframes, and a new adjudication application is not made (clause 22).

Miscellaneous reforms

This reform will clarify that an authority to nominate adjudicators may be granted subject to conditions (clauses 25-26). Other reforms clarify language for service of notices (clauses 16, 28-29 and 30-32).

When could these reforms commence?

Preferred option

A commencement date of February 2019 is proposed to ensure that the sector benefits from the changes contained in the reforms as soon as would be reasonably practicable, while providing a short transitional period to allow for the holiday season. The administrative nature of the reforms means that there would be minimal impacts likely to necessitate a longer transitional period.

Questions for comment

- 1. Is the proposed start date for these reforms feasible?**
- 2. Are there reasons why these reforms should start later?**

Reforms with a transitional period

The following reforms have been identified as reforms which are likely to have a direct impact on industry practices and where it would be appropriate to provide preparation time before commencement. It is proposed that these reforms could commence in the middle of 2019.

Progress payments and payment claims

The Amendment Act contains a series of reforms to overhaul sections 8 and 13 to simplify and clarify the entitlement to a progress payment and the process for recovering it.

Specifically, section 8 is amended to provide that a person who, under a construction contract, has undertaken to carry out construction work or to supply related goods and services is entitled to receive a progress payment (clause 4). This entitlement will no longer be triggered by a "reference date", a term that will be abolished from the Act. Instead, the entitlement is simply triggered by the fact that a person has undertaken to perform work or supply goods and services under a construction contract.

Section 13 is amended to set out how a person who is or who claims to be entitled to a progress payment under new section 8 can recover a progress payment (clauses 9-10 and 12). The aim is to ensure that a person who has undertaken to carry out construction work or to supply related goods and services is entitled to make a payment claim for every named month, or more frequently if provided for under the construction contract.

Further, section 13 establishes an entitlement to make a payment claim in circumstances where a contract has been terminated.

Due dates

This reform reduces the maximum payment period for payments from a head contractor to a subcontractor from 30 to 20 business days, better aligning it with the industry practice of 30-day payment terms (clause 7).

Payment claim endorsement

This reform re-inserts the requirement that a payment claim must include an endorsement that it is a claim being made under the Act (clause 11).

Miscellaneous adjudication reforms

This reform will make the date of receipt of the adjudication response the trigger for commencing the 10 business day deadline for an adjudication determination under the Act (clause 18).

Additional reforms provide a new process for a claimant to withdraw their adjudication application (clause 17). Prior to an adjudicator being appointed, a claimant may withdraw at any time with notice. After appointment, a withdrawal will be of no effect if a respondent objects and the adjudicator believes it is in the interests of justice to uphold the objection.

The reforms will also clarify that an adjudicator is responsible for serving an adjudication determination on the parties (clause 19-20).

When could these reforms commence?

Preferred option

A commencement date of 1 June 2019 is proposed as these reforms will have a direct impact on industry practice. Accordingly, it would not be appropriate to commence these reforms without providing industry with reasonable time to prepare for their commencement. It is anticipated that a commencement date would be proclaimed in February 2019, providing industry with at least a 3-month transitional period from proclamation.

Questions for comment

- 3. Is the proposed start date for these reforms feasible?**
- 4. Are there reasons why these reforms should start earlier or later?**

Reforms requiring subordinate legislation before commencement

The following reforms have been identified as requiring subordinate legislation or administrative changes before they commence. Accordingly, it is proposed that these reforms should commence late in 2019. This would provide time to develop the subordinate legislation and allow the sector to prepare for its commencement.

Removal of ‘owner-occupier’ exemption

Reforms will remove the existing ‘owner-occupier’ residential building work exemption from the Act to allow it to be refined or removed if required in future (clauses 1-3 and 5-6). The exemption will be transferred to the Regulation.

Inspection of trust records by subcontractors

This reform will allow regulations to 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 (clause 8).

Prescribing information for subcontractors

This reform will allow regulations to prescribe information to be given to a subcontractor (clause 36). This information would assist subcontractors to better understand the operation of the Act and the processes involved in making claims and pursuing adjudication.

Code of Practice for Authorised Nominating Authorities (ANAs)

This reform provides the Minister with the ability to make a Code of Practice to be observed by an ANA in relation to its activities under the Act (clause 27).

Reducing the threshold for retention money trust requirements

This proposed reform does not originate from the Amendment Act and is discussed in more detail in the next chapter. It has been referenced here as it will form part of the package of reforms identified above and is therefore relevant when considering commencement.

When could these reforms commence?

Preferred option

A commencement date of December 2019 is proposed. This date would give the necessary time to make regulations and administrative changes (i.e. develop the Code of Practice), consult

and proclaim a commencement date by September 2019. Such a proposed commencement date would provide industry with a 3-month transitional period to prepare for the reforms before they commence.

Questions for comment

- 5. Is the proposed start date for these reforms feasible?**
- 6. Are there reasons why these reforms should start earlier or later?**

Application of amendments

As a general rule, the Amendment Act currently provides that each of the above reforms will not apply to a construction contract entered into prior to commencement. For example, if the reform amending due dates commenced on 1 June 2019, any contracts entered into prior to this date would require subcontractors to be paid within 30 business days. All contracts entered into from 1 June 2019 would require subcontractors to be paid within 20 business days.

Despite this, the Amendment Act does allow for this general rule to be altered or disapplied in relation to specific reforms if this was considered appropriate. Any variation from the general rule would need to be done by regulation.

In response to feedback received from stakeholders as part of the consultation on the Amendment Act, it is understood that the general rule is the preferred approach for the majority of the reforms. This ensures that when the parties are negotiating the terms of a contract, they are doing so with certainty about how the law will apply during the life of the contract. However, the Department is conscious that there may be reasons why stakeholders would instead prefer that certain reforms apply to all contracts they are administering from a particular period in time, regardless of when the contract was entered into. For example, an organisation may face difficulties if they are required to apply different progress payment requirements to different contracts due to the changes that may be necessary to information-technology systems used to manage and process those payments.

Additionally, there may be little deleterious impact from applying the reforms to existing contracts, for example, the reforms to ensure payment dates may be made if a contract is terminated.

Questions for comment

- 7. Do you support the reforms only applying to a construction contract entered into after commencement?**
- 8. Are there specific reforms which you would consider to be more appropriate to apply to contracts entered into prior to commencement? If yes, why?**
- 9. Are there specific reforms that you would not support being applied to contracts entered into prior to commencement? If yes, why?**

Proposed reforms to the Regulation

The following reforms are proposed to the *Building and Construction Industry Security of Payment Regulation 2008* (the Regulation). It is anticipated that these reforms will be drafted and available for consultation in May 2019. Stakeholders are welcome to comment on these proposed reforms in their submissions.

Reducing the threshold for retention money trust requirements

It is proposed that clause 5 of the Regulation is amended to extend the existing trust obligations for retention money to provide protections to a greater number of 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 considered this provision to be unnecessarily burdensome.

To moderate any increased regulatory burden associated with reducing the threshold, it is proposed to remove the annual reporting requirements in clause 16 of the Regulation.

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 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 proposed 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

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.

Questions for comment

- 10. Do you support maintaining a threshold to limit the application of the retention money trust obligations or should it be removed?**
- 11. Do you support reducing the threshold for retention money trust obligations from \$20 million to \$10 million?**
- 12. Is there another amount you consider appropriate for the threshold? Why?**
- 13. Do you support extending the retention money trust obligations to the entire contracting chain and not just limiting the obligation to head contractors?**
- 14. Do you support removing the annual reporting requirements in clause 16 of the Regulation?**
- 15. What is an appropriate transitional period to allow for industry to prepare for the proposed changes to the retention money trust obligation?**

Inspection of trust account records

This proposed 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.

It is proposed that clause 14 of the Regulation is amended to make provisions 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 proposed 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 in trust and that such moneys will be available to them when rightfully due.

The proposed 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.

Questions for comment

16. Do you support the inspection of retention money trust account records?

17. Do you support inspection being subject to an appropriate fee?

18. Should the Regulations prescribe a maximum fee to be imposed? If yes, what do you think an appropriate maximum fee would be?

Prescribing penalty notice offences

The Amendment Act will provide an authorised officer with the ability to issue a penalty infringement notice to a person or corporation where it has contravened the Act or the Regulation.

This reform 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.

The offences subject to penalty infringement notices need to be set out in the Regulation. It is proposed that the following offences in the Act and Regulation will be subject to penalty infringement notices:

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

Questions for comment

19. Do you support the offences listed above being subject to a penalty infringement notice?

20. Do you support the proposed penalty notice amounts for these offences?

21. Are there any other offences which you consider appropriate for a penalty infringement notice? If yes, what penalty notice amount would you consider appropriate?

Increased penalty units for offences

It is proposed to update penalty units for the following offences under the Regulation, ensuring that the penalties provide an effective deterrent to the commission of an offence.

Offence	Description	Maximum penalty in penalty units (pu)
CI 6(1)	Head contractor not holding retention money on trust	1,000 pu for corporation
CI 7(3)	Not notify Secretary of matters	200 pu for individuals
CI 8	Head contractor withdrawing from trust account for non-legitimate purpose	
CI 11	Head contractor fails to notify of overdrawn trust account	
CI 12	Head contractor fails to notify of closure of trust account	
CI 14	Head contractor fails to retain trust account records	
CI 15(3)	Failing to provide information in response to request	
CI 17	Providing false or misleading information	

Questions for comment

22. Do you support increasing the value of the penalty unit for the offences listed above?

23. Do you support the proposed penalty notice amount for these offences?

Executive Liability offences

Directors and people involved in the management of companies will be held responsible for the commission of corporate offences. It is proposed to apply accessorial liability to all offences under the Regulation which are capable of being committed by a corporation. It is also proposed to apply executive liability to the following offences under the Regulation:

Offence	Description	Penalty units
CI 8	Head contractor withdrawing from trust account for non-legitimate purpose	1,000 pu for a corporation 200 pu in any other case
CI 11	Head contractor fails to notify of overdrawn trust account	
CI 12	Head contractor fails to notify of closure of trust account	
CI 14	Head contractor fails to retain trust account records	
CI 15	Failing to provide information in response to request	
CI 17	Providing false or misleading information	

Questions for comment

24. Do you support accessorial liability applying to all offences under the Regulation which are capable of being committed by a corporation?

25. Do you support executive liability applying to the offences listed above?

26. Are there any other offences in the Regulation which you consider executive liability should apply to?

27. Do you support the proposed penalty unit amounts listed above for these offences?

Proposed administrative changes

The following reforms are administrative in nature and have been included for completeness. These reforms will be progressed concurrently with the amending Regulation but are subject to a separate consultation process.

Prescribing information for subcontractors

The Amendment Act allows the regulations to prescribe information to be given to a subcontractor. This information would assist subcontractors to better understand the operation of the Act and the processes involved in making claims and pursuing adjudication. Fair Trading will work with stakeholders to develop the format and content of such information.

Code of practice for authorised nominating authorities

The Amendment Act will provide the Minister with the ability to make a Code of Practice 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.

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.

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. Fair Trading will work with stakeholders throughout 2019 to develop the Code of Practice.