

# Constuction LegalUpdate

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## Recent amendment to Building and Construction Industry Security of Payment Act 1999 places greater power in Subcontractors' hands

A new amendment to the *Building and Construction Industry Security of Payment Act 1999* (Act) will give greater power to Subcontractors, most importantly the ability to "freeze" monies owed to the Contractor above them.

As is well known, one of the main functions of the Act is to provide Contractors with a fast-track means to obtain payment, via an adjudication process, with the aim of protecting the contractor's cash-flow. The *Building and Construction Industry Security of Payment Amendment Act 2010* (Amendment Act) will extend the reach and potency of this regime in favour of Subcontractors. Under the *Contractors Debt Act 1997*, where a "middle" Contractor has failed to pay its Subcontractor, the Subcontractor may serve a "debt certificate" on the Principal Contractor, obliging the Principal Contractor to pay the Subcontractor directly (out of money that would otherwise have been paid by the Principal Contractor to the defaulting Contractor). A debt certificate may be obtained by a Subcontractor following receipt of a court judgment in its favour in relation to the debt, or where an adjudication certificate received under the Act has been filed in court as a judgment for a debt.

Now, as a result of the Amendment Act, a Subcontractor may, as part of an adjudication against a Contractor, require a Principal Contractor to withhold money owed by it to the Contractor. The new section 26A of the Act provides that where a Subcontractor has served an adjudication application on a Contractor under the Act, the Subcontractor may also serve a "payment withholding request" on the Principal Contractor, requiring it to withhold payment from the Contractor sufficient to cover the Subcontractor's claim. If the Principal Contractor fails to comply with this request, he will become jointly and severally liable with the Contractor for the amount owed to the Subcontractor.

The purpose of this new mechanism is to enable Subcontractors to secure payments owed to them by a defaulting Contractor. However, the obvious concern for Contractors is that Subcontractors may use this new entitlement as a means of imposing greater commercial pressure on Contractors with respect to forcing settlement of claims. Under the "old" regime, where a Subcontractor included spurious claims in an adjudication application, a Contractor might choose to contest those claims as part of the adjudication process. Now however, the Contractor faces a scenario where potentially large amounts of its cash-flow are frozen throughout the adjudication process, irrespective of whether the amounts relate to bona fide Subcontractor claims

or are purely spurious. Even where the Contractor is ultimately successful in the adjudication process, it appears the money may remain frozen for 20 or more business days following the adjudicator's determination (refer to section 26B(3) of the Act as amended). Needless to say, this is a significant period of time to do without payment for a Contractor that may not have substantial cash reserves to cover the shortfall.

The amendments are also of concern from a Principal Contractor point of view. As mentioned above, a Principal Contractor may become jointly and severally liable, with the Contractor, to the Subcontractor for the amount claimed. Clearly, Principal Contractors must ensure their administrative and accounts functions are operating efficiently in order to avoid this situation. More importantly however, Principal Contractors must be concerned that Subcontractors will now have the ability to potentially impose severe cash-flow pressure on important Contractors, perhaps to the detriment of the project.

The Amendment Act received assent on 29 November 2010 but had not yet commenced as at the date of this update. However, the amendments will apply retrospectively and thus may impact upon adjudication applications served before commencement of the amendments.

CBP will be providing further detailed analysis of the effect of the amendments in the coming months.

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