Article Information

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2020 Construction Law Year in Review: Legislative Changes, Security of Payment and Insolvency Reforms

2020 has been the year of uncertainty, press conferences and resilience but it leads into a year of opportunities with budgets at both Federal and State levels bringing much to be confident about in 2021.

This article provides a snap shot of some of the major developments in the industry and outlines:

1. *this year's important legislative changes;*
2. *key security of payments decisions;*
3. *relevant insolvency reforms; and*
4. *what to watch out for in 2021.*

1. **Legislative changes: security of payment in NSW, designers beware, and Cladding Safety Victoria**

New South Wales – Design and Building Practitioners Act 2020

The *Design and Building Practitioners Act 2020* (NSW) (**DBP Act**) came into force in June 2020 in response to the "*Building Confidence – Improving the effectiveness of compliance and enforcement systems for the building and construction industry across Australia*" report. This report highlighted the insufficient controls over documentation and compliance with the National Construction Code. The DBP Act is one of a suite of tools being implemented as part of the overhaul to regain public confidence and a customer-focused industry in the New South Wales building sector.

The DBP Act applies to "building work", which includes construction, alterations, additions, repairs, renovations and protective treatment.

A key part of the DBP Act is the introduction of a statutory duty of care and liability in circumstances where the ordinary principles of negligence may not have applied or the contract may have excluded liability, including for pure economic loss. Any person who carries out construction work now has a duty of care to exercise reasonable care to avoid economic loss caused by defects in or related to a building for which work is done, or arising from the construction work and that duty of care applies retrospectively to defects that have manifested in the past 10 years. Construction work includes:

1. building work;
2. the preparation of regulated designs and other designs for building work;
3. the manufacture or supply of a building product used for building work; and
4. supervising, coordinating, project managing or otherwise having substantive control over the carrying out of any work referred to above.

The duty of care is owed to each land owner and subsequent land owner, regardless of whether or not the construction work was carried out under a contract with the land owner or other arrangement. As such, most building work is captured, and designers and builders will be held liable for not complying with the Building Code of Australia (**BCA**).

You can read more about the *Design and Building Practitioners Act 2020* here.

Victoria – building practitioner regulatory reforms

The *Building and Environment Protection Legislation Amendment Act 2020* amends the *Building Act 1993* to grant to the VBA enhanced powers to consider the history of corporate behaviours of a practitioner or a director of a body corporate practitioner (i.e. an applicant or director of an applicant) in determining whether the applicant is a "fit and proper person" to be a registered practitioner. In doing so, the VBA is seeking to protect to the public against illegal phoenixing activity.

The VBA's new powers add to the existing regulatory framework which already requires various factors to be taken into account in determining whether the practitioner is a "fit and proper person".

The most significant change is the inclusion of a financial probity requirement which means that the VBA must take into account whether the applicant (or a director of the applicant) was a director or 'influential person' of another company within the two years preceding that other company being placed into external administration. The VBA may also consider any activity which meets the relevant criteria irrespective of the time at which the former company entered into external administration. The definition of influential person is similarly broad.

The VBA may refuse renewal or registration, or issue a show cause notice, if an investigation shows that a building practitioner has not met the updated 'fit and proper' standard due to activity tied to a company within the two years prior to that other company entering external administration.

You can read more about the amendments here.

New South Wales – security of payment reforms

The new *Building and Construction Industry Security of Payment Regulation 2020* (NSW) repeals and replaces the *Building and Construction Industry Security of Payment Regulation 2008* (NSW).

The key changes include the following:

- head contractors must now keep records in relation to a retention money trust account with separate ledgers for each subcontractor, which is to be provided to the subcontract at least every 6 months or more often as agreed;
- supporting statements are only required in relation to subcontractors and suppliers that are directly engaged by the head contractor;
- the Act will apply to owner occupier construction contracts from 1 March 2021; and
- an adjudicator must complete continuing professional development and must meet the eligibility requirements, being either:
    - a relevant qualification in architecture, building surveying, building and construction, project management, engineering or law in addition to 5 years relevant experience; or
    - 10 years relevant experience.

The new regulations are on top of changes to the *Building and Construction industry Security Payment Act 1999* (NSW) which saw among other things:

- the removal of reference dates;
- the addition of the requirement for payment claims to be endorsed under the Act; and
- clearer guidance around excluding companies in liquidation from having the benefit of the Act

Victoria – Cladding Safety Victoria

Cladding Safety Victoria Act 2020 (Vic) (**CSV Act**) and *Cladding Safety Victoria Regulations 2020* (Vic) commenced on 1 December 2020. The CSV Act established Cladding Safety Victoria (**CSV**), a body corporate, with the object of supporting Victorians to rectify non-compliant or non-conforming external wall cladding products on buildings to improve safety.

The CSV will:

- administer a cladding rectification program;
- make decisions relating to financial assistance for cladding rectification works; and
- provide guidance to owners corporations and owners in relation to cladding rectification work.

A municipal building surveyor may notify CSV of a building that they consider requires cladding rectification work and CSV will decide whether to grant or refuse financial assistance. The owner or owners corporation of a prioritised building will be invited by CSV to register for financial assistance for the cladding rectification work at which point CSV will decide whether to grant or refuse the financial assistance.

Controversially, the Act amends the *Building Act 1993* by extending the limitation period for a "cladding building action", being specified building actions in relation to non-compliant or non-conforming external wall cladding products. Consequently, a cladding building action may now be brought within 12 years after the date of issue of the occupancy permit if the building action became prohibited (i.e. time-barred) on or after 16 July 2019, but before 30 November 2021.

You can read more about Cladding Safety Victoria here.

2. **Security of payments: key cases**

TFM Epping Land Pty Ltd v Decon Australia Pty Ltd [2020] NSWCA 93

The recipient of a payment claim (i.e. the principal) challenged a judgment in favour of the builder under s 15(4) *Building and Construction Industry Security of Payment Act 1999* (NSW) (**NSW Act**) as a result of the principal not serving a payment schedule within 10 days of receiving the builder's payment claim, making it liable to pay the whole of the claimed amount.

The Court found that s 15(4) gives rise to a right to payment and that the legal questions to be determined are effectively done by way of a final judgment and not summary judgment.

The approach to determining the validity of a payment claim outlined in *Nepean Engineering Pty Ltd v Total Process Services Pty Ltd (In liq)* (2005) 64 NSWLR 462 was also affirmed. That is, the validity of a payment claim should be determined on the face of the claim. If a claim purports to claim for variations under the contract then that will be a valid claim on its face.

The appropriate course for a recipient of a payment claim to raise any defence to particular claims for payment is by way of a payment schedule. If it fails to do so, it will not be open to it to do so afterwards because s 15(4) prohibits such a respondent from raising contractual defences.

Additionally, this judgment settled a controversy as to whether a payment claim served by a head contractor will be invalidated if it is not accompanied by a supporting statement as required by s 13(7) of the NSW Act, or if the supporting statement is otherwise defective or misleading. The Court found that a head contractor's payment claim will not be invalidated by a failure to provide a valid supporting statement. Instead, the Act provides that penalties may be imposed on a head contractor and as such, the only proper consequence which can be inferred is a penalty and not the invalidity of the payment claim.

A recipient of a payment claim should act prudently in serving a payment schedule within time, which identifies all the contractual defences to a payment claim. If the recipient fails to do so then it will face a very high bar in challenging the claimant's right to payment.

Façade Designs International Pty Ltd v Yuanda Vic Pty Ltd [2020] VSC 570

In this case, which deals with similar "on the face of the claim" principles in the Victorian context, the defendant failed to provide a payment schedule in response to the plaintiff's payment claim. The plaintiff then sought judgement under s16(2)(a)(i) of the *Building and Construction Industry Security of Payment Act 2002* (VIC) (**Vic Act**).

The defendant attempted to argue that the claim was invalid for failure to adequately identify construction work, and further that as the claim contained an excluded amount (a claim for interest), the Court is precluded from entering summary judgement on any part of the claim. The Court rejected these arguments.

The Court must assess the validity of a payment claim for the purposes of entering judgement under s16(2)(a)(i). In doing so, the Court will consider the payment claim document on its face and must only considers extrinsic materials referred to in the claim or relevant to the context of the contract, the latter pertaining to objectively determining whether a reasonable building practitioner in the position of the recipient would understand the payment claim to reasonably identify the particular work in respect of which the claim is made. Similarly, excluded amounts are to be assessed on the face of the claim (e.g. interest claims), can be severed from the claim (as was done in this case), and do not prevent the Court entering judgement.

You can read more about this case here.

1155 Nepean Highway Pty Ltd v Promax Buildings Pty Ltd [2020] VSCA 253

The plaintiff in this case did not provide a payment schedule in response to the defendant's payment claim, nor did it provide a response to the defendant's s18(2) notice, and the defendant proceeded to adjudication to recover the whole amount of the payment claim.

In considering whether an adjudicator can draw an adverse inference as a result of not providing a payment schedule, the Court distinguished between an adverse inference based on the absence of an adjudication response compared to the plaintiff's earlier failure to serve a payment schedule. The Court found that as a matter of common sense, a recipient of a payment claim who does not respond to it might rationally be thought to have no basis upon which to contest it.

Consequently, the Court found it "permissible for an adjudicator to infer, based on the failure of a recipient of a payment claim to provide a payment schedule, that the recipient was not in a position to contest the claim". Another timely reminder for principals to ensure they respond to payment claims within time.

Parrwood Pty Ltd v Trinity Constructions (Aust) Pty Ltd [2020] NSWCA 172

Distinguishing the facts in the High Court's decision in *Southern Han Breakfast Point Pty Ltd (in liq) v Lewence Construction Pty Ltd* (2016) 260 CLR 340 (**Southern Han**), the NSW Court of Appeal found that the statutory entitlement to make a progress claim cannot be modified or extinguished by an exercise of powers under the contract (i.e. by suspending payment entitlements). This is because once a reference date arises under the NSW Act, a claimant's payment entitlements are preserved in respect of that reference date, notwithstanding any contractual mechanisms a respondent may use to suspend the claimant's payment entitlements.

This case highlights the NSW Court of Appeal's resolve to ensure that any entitlements to payment given to a claimant under the NSW Act are to be preserved despite any contractual attempts to suspend the claimant's rights to payment.

A reference date arose on 25 August 2019 and the claimant served its payment claim on 6 September 2019. However, on 3 September 2019, which was a date before the claimant had served its payment claim, but after the relevant reference date, the respondent exercised its right under the contract to take the work out of the claimant's hands which suspended the claimant's contractual payment entitlements. Relying on *Southern Han*, the respondent argued that the effect of taking the works out of the claimant's hands and the subsequent suspension of payments was that the claimant was no longer entitled to make a progress claim.

The NSW Court of Appeal found in favour of the claimant and held that the statutory entitlement to make a progress claim could not be modified or extinguished by an exercise of powers under the contract by the respondent. The present set of facts were distinguished from *Southern Han* where the claimant had sought to rely on a reference date that had arisen after the valid service of a take out notice.

VCON v Oliver Hume & Anor [2020] VSC 767

The Supreme Court of Victoria was given the opportunity to consider the 'excluded amounts' regime which is unique to the Vic Act. It follows the decision in *Shape Australia Pty Ltd v Nuance Group (Aust) Pty Ltd* [2018] VSC 808, in which it was held that a party may not attempt to recover liquidated damages levied in a previous payment claim period, as this is an excluded amount.

The principal made a demand on bank guarantees on the basis that there were amounts payable by the contractor. The contractor subsequently included the amounts for which recourse was had in its payment claim, arguing that recourse to this money was unlawful. The adjudicator determined that this part of the payment claim could not be taken into account as it was an 'excluded amount' akin to liquidated damages.

Stynes J rejected an argument that the bank guarantees had been drawn down in order to reduce the payment to the contractor and were prohibited under the security of payment legislation because the bank guarantee mechanism was a matter arising under the contract. Her Honour also rejected submissions that the liquidated damages were not an excluded amount on the basis as they were an element of a claim for work performed under the contract and that there was an issue estoppel, observing that there was "no way to characterise the LD claim other than as an attempt to recoup monies converted on account of liquidated damages."

Importantly, her Honour found that section 47 of the Vic Act expressly preserves the entitlement for parties to have recourse to bank guarantees and that this does not "have the effect of excluding, modifying, restricting or otherwise changing the effect of a provision of the Act".

BCS Infrastructure Support Pty Ltd v Jones Lang Laselle (NSW) Pty Ltd [2020] VSC 739

The Supreme Court of Victoria has held that although the methods of service that are set out in section 50 of the *Building and Construction Industry Security of Payment Act 2002* (Vic) do not expressly include cloud-based methods of service, "the methods of service provided for are in addition to and do not limit or exclude the common law or the provisions of any other applicable legislation with respect of the service of notices."

However, Her Honour Stynes J considered that uploading the payment claim to the cloud-based information system (e.g. Dropbox) was "a very poor method of delivery" for reasons that included, in the circumstances, it was not the obvious choice of delivery for a payment claim, it had not been consistently used for service of previous payment claims, email could have been used and indeed email had been used to serve payment claims previously.

Further and critically, in order to effectively serve another party, the Court found that that party must actually receive the payment claim which in this instance required logging on to the cloud-based information system, identifying the correct file and opening it. As such, it was held that it was not unreasonable that the payment claim had not been paid or a payment schedule prepared as it had not been properly received.

EHome Construction Pty Ltd v GCB Constructions Pty Ltd [2020] QSC 291

The Supreme Court of Queensland considered s 75 of the *Building Industry Fairness (Security of Payment) Act 2017* and when, if at all, a 'final payment' may be made in circumstances where a construction contract does not include any provision for reference dates after termination.

In this instance, an application was made seeking a declaration that a payment claim was void for being out of time in circumstances where the claim was submitted about one month after termination of the contract.

The Court found in this case, and whenever a contract does not include any provision for reference dates after termination, a final reference date must exist and a final payment claim may be made "6 months after the completion of all construction work to be carried out under the construction contract".

Citi-Con (Vic) Pty Ltd v Trojan Built Pty Ltd [2020] VSC 557

While the Vic Act does not provide a definition of a final payment claim, Stynes J has held that the question of whether a payment claim is a final payment claim or a progress payment claim should be determined objectively to the standard of a reasonable person having the background knowledge that should reasonably be ascribed to the parties at the time the relevant document was served.

In this case, Stynes J found that the relevant payment claim was not a final payment claim and considered the following factors:

- the covering email referred to the document as a "Payment Claim" and there was no suggestion that it was a final payment claim;
- the document was titled and referred to within the document as a "Payment Claim", not a final payment claim;
- service of the document was consistent with the contractual provisions relating to progress payments;
- the contract was still on foot;
- practical completion had not yet been certified; and
- the claimant had continuing obligations under the contract, particularly under the defects liability provisions, that were relevant to the final accounting between the parties.

Finally, Stynes J also held that the inclusion of a claim for the return of retention moneys is not determinative of the status of the payment claim.

In light of this decision, both claimants and respondents should be mindful that a final payment claim should clearly state that it is a final payment claim and be consistent with all requirements for final payment under the contract.

3. **Insolvency in 2021**

From 1 January 2021, the *Corporations Act 2001* will introduce a new restructuring process and an altered insolvency process for small companies with less than $1 million in liabilities. This is likely to have implications for many subcontractors in the construction industry. Given the likely influx of insolvencies due to insolvent trading relief provisions expiring on 31 December 2020, it is hoped that the amendments will assist many small businesses to restructure and continue to operate despite this year's business interruptions.

Companies, directors and people who have been directors in the preceding 12 months will be restricted from accessing this process more than once in the currently proposed 7 year period.

Restructuring Process

The new restructuring process allows small companies to continue to trade under the control of its owners in the ordinary course of business whilst also being a quicker and less complex process. Eligible small businesses can declare to their creditors an intention to access the regime up until 31 March 2021. Once a declaration is made, the small business has up

to 3 months to undertake the restructuring process.

In order to be eligible for the restructuring process, small businesses must:

- have liabilities not exceeding $1 million;
- not already be restructuring, under administration, executed a deed of company arrangement that has not yet terminated or have a liquidator appointed; and
- not have a director, or individual who has been a director in the previous 12 months, who has also been a director of another company that has been under restructure or the subject of simplified liquidation in the last 7 years. There is an exemption for directors of related body corporates subject to restructuring or simplified liquidation within the previous 20 business days.

Once a company is under restructuring, it must ensure that it continues to:

- pay all employee entitlements that are payable, including superannuation contributions; and
- give documents required under taxation laws.

Simplified Liquidation Process

The existing liquidation process will continue to apply, but small companies will have some concessions for voluntary winding up. The changes are aimed at reducing time and cost by reducing the investigative, meeting and reporting requirements.

The changes include the following:

- the liquidator must adopt the simplified liquidation process within 20 business days of a triggering event, which includes the passing of a special resolution to voluntarily wind up the company;
- there are no meetings of creditors;
- the circumstances in which a liquidator can seek to clawback unfair preference payments from a creditor that is not related to the company are reduced; and
- creditors can opt-out of the simplified liquidation process.

Frustratingly, the Regulations which will largely guide the simplified processes are yet to be finalised and released ahead of the 1 January 2021 commencement date, and so it is difficult to state with certainty how the new processes will operate in all practicality.

However, given the prevalence of insolvencies in the construction industry, it is hoped that being able to engage in a cheaper, simpler and more streamlined restructuring process will result in better outcomes, especially for subcontractors and their creditors.

4. **Watch this space: appeals, demands and security of payments in WA**

On appeal – Façade Designs International Pty Ltd v Yuanda Vic Pty Ltd [2020] VSC 570

Yuanda Vic Pty Ltd has sought leave to appeal the Court's finding that, in determining whether a claim contains an excluded amount, it is sufficient for the Court to examine only the face of the payment claim and any supporting documentation.

Creditor's statutory demands

The *Corporations and Bankruptcy Legislation Amendment (Extending Temporary Relief for Financially Distressed Businesses and Individuals) Regulations 2020* extended the period to comply with a creditor's statutory demand from 21 days to the longer of 21 days or 31 December 2020. Accordingly, as of 1 January 2021 a debtor will only have 21 days to pay a valid creditor's statutory demand.

With insolvencies significantly below average in 2020, additional financial due diligence in contracting will be required.

Western Australia – Security of Payment reforms

The *Building and Construction Industry (Security of Payment) Bill 2020* (WA) (**Bill**) seeks to replace the *Construction Contracts Act 2004* (WA) and has currently had its second reading speech in the Legislative Council. As a result of the prorogation of Parliament in the state, the Bill is now on pause until after the state election on 13 March 2021, however if passed, the Bill will:

1. introduce timeframes within which a progress payment becomes payable being:
    1. (from a principal to a head contractor) – 20 business days after a payment claim is made; or
    2. (to a subcontractor) – 25 business days after a payment claim is made;
2. restrict the mining exemptions to the WA Act;
3. create a deemed retention trust scheme, which applies irrespective of any contract term to the contrary. Money can only be withdrawn from the trust accounts where there is a contractual entitlement to do so and so cannot be used for alternative purposes.

Conclusion

While this year has proved challenging in its own right, the updates to case law and legislation outlined in this article illustrate the importance of staying up to date even during periods of state and industry-wide shutdown. We look forward to a more normal 2021, where we will monitor the effects of these changes to the building and construction industry as well as identifying new developments to the legal and industrial framework.