

# Security of Payment

## Discussion paper

December 2015



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## Purpose

Ensuring security of payment for subcontractors in the building and construction industry is a complex problem, with no simple solution.

The failures of prominent construction companies including Walton Construction, Carmichael Builders Pty Ltd and Glenzeil Pty Ltd highlights the need for consultation and strategies to safeguard payments.

A key difficulty in addressing the problem is the large number of different factors that can influence the payment process. These include:

- contractual agreements
- commercial relationships
- supply chain arrangements
- the financial position of the parties involved
- business behaviour and ethics
- management and allocation of risk
- external market forces
- investment and funding arrangements; and
- relevant laws, such as contract, tax and company laws.

To improve security of payment for Queensland subcontractors, the State Government made an election commitment to review the issue and undertake detailed and comprehensive consultation with stakeholders in the building and construction industry.

This government is now delivering on this commitment by releasing and seeking industry feedback on this Security of Payment discussion paper. In order to improve security of payment for subcontractors, this discussion paper looks at the weaknesses within legislation and the current system. It also identifies a number of options that may go towards safeguarding payments. The options provided should not be seen as standalone options but rather as modular strategies, any combination of which, may improve on the status quo. When reading this discussion paper, a holistic view should be taken of the likely combined effects of the proposed options.

To determine the most suitable pathway to improving security of payment for subcontractors, the Government is taking a collaborative approach with industry. The Government alone cannot solve the problem. Rather, Government and industry must work together to bring about change. Your experience will help to formulate realistic and practical strategies that will inform genuine change and improvement.

## Privacy and confidentiality

The Department of Housing and Public Works (department) is seeking input for the review of the security of payment framework in Queensland including the 2014 amendments to the *Building and Construction Industry Payments Act 2004* (BCIP Act).

All personal information collected will be treated in accordance with the *Information Privacy Act 2009*. The department may contact you for further consultation regarding the review.

The department will not disclose or publish, in full or part, any submissions in response to this discussion paper except as required under the *Right to Information Act 2009*.

## Disclaimer

This discussion paper has been released to seek feedback on the issue of security of payment in the building and construction industry and does not represent legal advice. The State of Queensland makes no statement, representation, or warranty about the accuracy or completeness of any information contained in this discussion paper. The State of Queensland disclaims all responsibility and all liability (including without limitation, liability in negligence) for all expenses, losses, damages and costs any person might incur as a result of the information being inaccurate or incomplete in any way for any reason.

## Responding to the discussion paper

You can respond to issues in this discussion paper via the Get Involved website: [www.getinvolved.qld.gov.au](http://www.getinvolved.qld.gov.au) or alternatively in writing by post or email.

A hard copy of the survey questions is available on the Get Involved website, the department's website or by contacting the department via email [securityofpayment@hpw.qld.gov.au](mailto:securityofpayment@hpw.qld.gov.au).

For written submissions, please number your responses to correspond with the questions identified on page 22.

Submissions close at **5pm, Thursday 31 March 2016** and will not be accepted after this date.

Submissions will only be accepted if they include your, name, address and telephone number.

Written submissions can be sent by:

- Email: [securityofpayment@hpw.qld.gov.au](mailto:securityofpayment@hpw.qld.gov.au)  
Security of Payment discussion paper (as email subject line)
- Post:  
Security of Payment discussion paper  
GPO Box 2457  
Brisbane QLD 4001

## Background

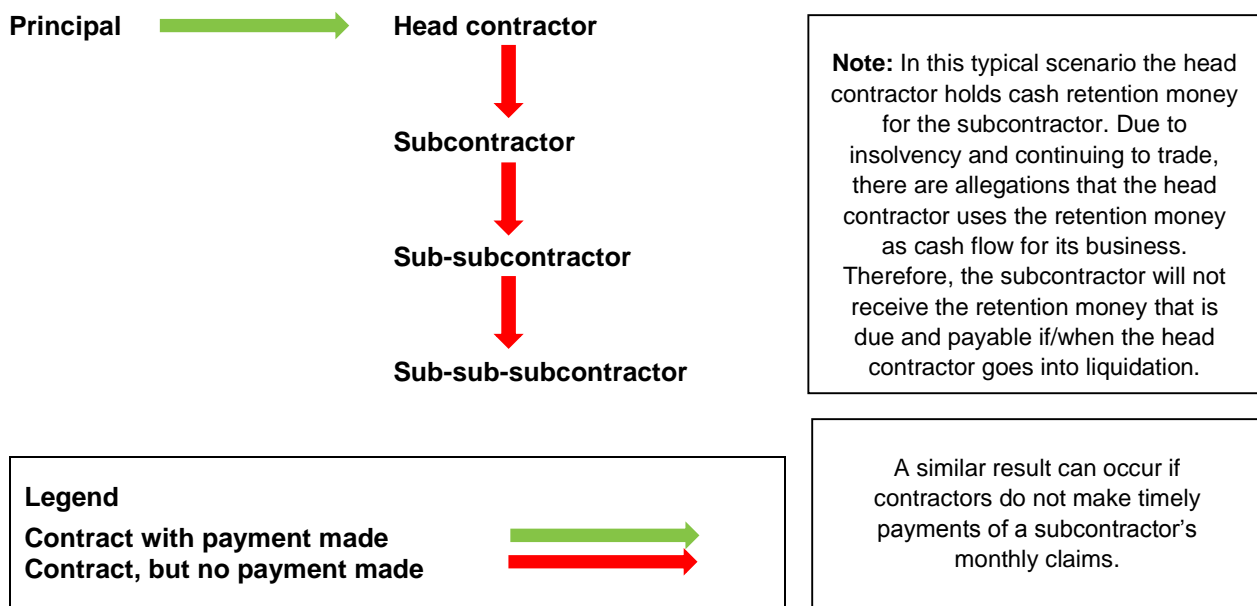
In 2014, the Queensland Building and Construction Commission (QBCC) released a *Better Payment Outcomes discussion paper*. It sought feedback on options to improve security of payment. This discussion paper builds on the information received through that consultation, and seeks feedback from a wider cross-section of the building and construction industry. This paper addresses the calls from industry that further consultation is needed and that further initiatives should be canvassed.

## The current system

The key problems are:

- insolvency in the contractual chain that leave subcontractors unpaid for work they have already completed. This is a problem for both large scale head contractors and smaller businesses
- retention money being used as cash flow by contractors and head contractors, instead of being kept aside for defects
- protracted and unjustified delays in payment for work done
- a lack of financial management skills in the industry.

Diagram 1 depicts these current problems.

**Diagram 1: Current contractual chain problems**

**Explanation:** Head contractor becomes insolvent and the entire contractual chain below does not get paid for the work that they have done. Additionally, the head contractor uses the retention money it holds for the subcontractor for its own business's cash flow. As a result, the subcontractor is never paid this money despite having earned it. The retention money can often represent all of a subcontractor's profit margin.

These problems are discussed in more detail below.

## Cash flow/payment process

The building and construction industry in Queensland traditionally uses a system of cascading payments from a head contractor down the contractual chain to all subcontractors. Subcontractors can wait for substantial periods of time to be paid for work or services provided. The lag time between completion of work and payment puts a high strain on the (often small) business's cash flow, which puts subcontractors at risk of becoming insolvent.

Further, it is reported that head contractors often delay payment for as long as possible to supplement their own business's cash flow. This deferred payment system and inflated cash flow hides the fact that a company may otherwise be insolvent.

In addition, subcontractors are at risk of insolvency when firms higher in the payment chain become insolvent. For example, it is reported that the collapse of head contractor Walton Construction in 2013 led to approximately 600 contractors in Queensland failing to be paid \$30 million, and many subcontractors became insolvent.

When firms above a subcontractor become insolvent, subcontractors are unsecured creditors, which means they are often not paid by a liquidator for the work they have done. This is because unsecured creditors are the last category to be paid. The Australian Securities and Investments Commission (ASIC) made a submission to the Senate Standing Committee on Economics (Senate Committee) in its inquiry into Insolvency in the Australian Construction Industry. That submission indicated that, in the period 2009 – 2014, the construction industry experienced the highest number of external administrator appointments of all industry sectors, except for the business and personal services sectors. The ASIC submission also indicates that where an external administrator is appointed, the



estimated return for unsecured creditors in the vast majority of cases is less than 11 cents in the dollar. This was the outcome, for example, in 97% of cases in the period 2013 – 2014.

## System of retention money

Retention money is money earned by a subcontractor through the progressive completion of work. Retention money is held by the head contractor/contractor to secure the subcontractor's performance obligations under the construction contract. For example, retention money is used to pay for costs associated with:

- late completion of work
- work not complying with contractual requirements
- remedying defects
- non-completion because of the insolvency of the subcontractor.

Retention money is generally held by a head contractor until the end of a contract's defects liability period. Retention money can be used in two ways:

- if any defects, or an issue identified above, occur within the defects liability period the contractor can use the retention money; or
- at the end of the defects liability period, if no defects or issues raised above arise, the contractor pays the retention money to the subcontractor who has already earned it.

Retention money represents only a small portion of the total project price. With this said, retention money is important as it can often represent the entirety of a subcontractor's profit for a contract. Therefore, it is crucial that this money is received by subcontractors for the work they have provided.

It has been suggested that retention money is not always returned to subcontractors as head contractors/contractors use the retention money as part of their working capital. This makes it difficult to access the funds to rectify incomplete or defective work, and difficult to pay subcontractors when all milestones have been met.

Further, if the head contractor/contractor becomes insolvent then retention funds are lost to liquidators and are not given to subcontractors despite the subcontractor having already earned the money.

## Contract terms

There are a number of protections in place for subcontractor payment for government building projects. This is through the Government's Capital Works Management Framework (CWMF) administered by the department. These protections include special requirements and contract conditions as well as a system of prequalification for building contractors and consultants known as the Prequalification (PQC) System.

There are specific measures that address security of payment within standard building contracts developed and maintained by the department include specific measures to address security of payment through special conditions, including:

- contractors are required to inform subcontractors regarding the existence of the BCIP Act and *Subcontractors' Charges Act 1974* (SC Act)

- requiring contractors to provide statutory declarations to confirm that workers and subcontractors have been paid what is due and owing to them with each payment claim
- paying the contractor within the timeframes prescribed in the *Queensland Building and Construction Commission Act 1991* (QBCC Act)
- for larger contracts, at the request of the contractor, making payments directly to a worker or subcontractor.

The PQC System attempts to provide for security of payment for subcontractors on government building projects in Queensland by requiring that:

- all contractors undertaking contracts for projects expected to exceed \$500,000 must be selected from the PQC System
- a formal financial capacity assessment of the preferred tenderer is undertaken for all government building projects exceeding \$500,000 in value.

The CWMF requires government departments to use standard building contracts developed by the department.

Unfortunately private sector contracts are not given the same amount of protection and standardisation.

It has been argued that there are inconsistencies and incompatibilities between subcontracts and principal contracts. For example, strict reporting deadlines may exist in the subcontract but not in the principal contract which makes it difficult for a subcontractor to meet timeframes. In a competitive sector, contract variations may not be easily negotiated. Additionally, loss of profit clauses are only available for certain types of contracts.

Feedback suggests that some contracts have complex processes for recovering progress payments. This aligns with the comments that some head contractors/contractors delay payment of progress payments for as long as possible.

## Education and business management

The Senate Committee's recent investigations into Insolvency in the Australian Construction Industry indicate that the industry's financial management and business skills must be improved, particularly in smaller business. This is generally because individuals start as owner operators, then expand into a business with employees, often without learning how to manage the business effectively.

## Current legislation and policies

In Queensland, there are two pieces of legislation and a QBCC policy which deals with security of payment for subcontractors.

### ***Building and Construction Industry Payments Act 2004 (BCIP Act)***

The BCIP Act establishes a statutory based right to payments and a system of adjudication to ensure construction payment disputes are resolved quickly. If necessary, the court system can be used as a final measure. Under the BCIP Act, adjudication is available to persons who enter into a written or oral contract to carry out construction work or supply related goods and services. While this Act provides subcontractors with a right to payments it does not guarantee the payments.



***Subcontractors' Charges Act 1974 (SC Act)***

The SC Act establishes a statutory mechanism by which a subcontractor, in certain circumstances, can secure payment of monies owed under their contract with a contractor. This is only effective when monies are payable to a subcontractor and when there are monies payable by the head contractor to the defaulting contractor. This process is beneficial as it freezes money payable by the head contractor to the subcontractor via a statutory charge. This means the money is on hold until a court resolution is reached.

***Queensland Building and Construction Commission Act 1991 (QBCC Act)***

The QBCC Act regulates the building industry and establishes a licensing and regulatory system for the conduct of building work in Queensland. The QBCC Act also includes specific requirements for domestic building contracts, other building contracts and disciplinary provisions when a licensee fails to pay a subcontractor.

Under this Act, the Queensland Building and Construction Board is able to make policies governing the administration of the Act e.g. the Minimum Financial Requirements Policy (MFR Policy). The MFR Policy contains strict requirements for licensees to manage debts appropriately or risk losing their licence. It also permits the QBCC to take action as soon as there is an undisputed debt owing for an extended period, and also requires licensees to report to the QBCC when their assets decrease by a specified percentage.

The above measures aim to improve security of payment, however, there are still some gaps in the current system.

## Options

To address these gaps, below are potential options for improving security of payment for subcontractors. We encourage you to provide us with your feedback on these options.

### Option 1—Project Bank Accounts

This option would introduce Project Bank Accounts (PBAs) for the building and construction industry, initially as a trial on government projects. Pending the outcome of the trial, PBAs could be used on private contracts.

A PBA is a trust account that is normally set up by the principal (the employer or person/entity requesting the work) and a head contractor. The account is set up with a banking institution to facilitate the prompt payment of progress claims by contractors.

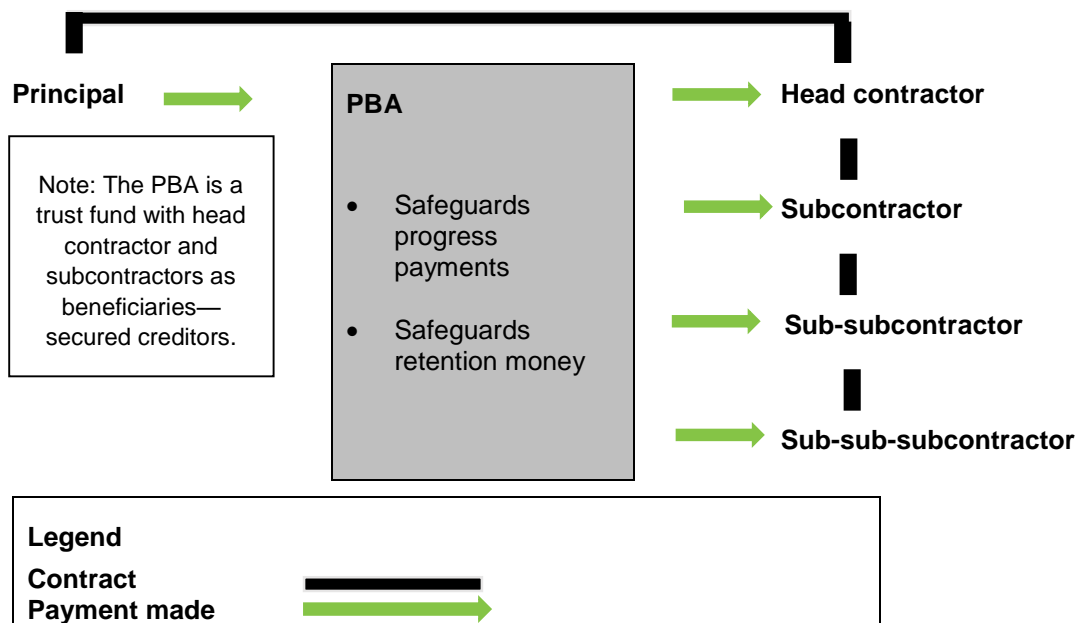
In this proposed option, subcontractors will submit their payment claims to the head contractor. The head contractor then submits a progress payment claim to the principal for the work done. This claim sets out the amount due to each subcontractor, and the amount due to the head contractor. The principal verifies the work has been completed, through the superintendent. When this has been verified, the principal counter signs the progress payment claim, and the principal makes the payment for the work done into the PBA.

The two signatures of the principal and the head contractor on the progress payment claim give the bank authority to disperse the funds in the PBA in accordance with the amounts in the progress payment claim. That is, the bank pays the head contractor and all subcontractors from the PBA at the same time by transferring money from the PBA directly into the bank accounts of the head contractors and subcontractors. This means there is no longer a contractual chain where the head contractor receives the payment for a subcontractor, and passes it down. In the event a payment claim needs to be reduced or delayed, the BCIP Act provisions apply.

While PBAs are primarily used in government projects, they can similarly be used on private projects, as is the case on some projects in Victoria. PBAs have been used on projects with a value of only \$1.5 million so may be suitable for both small and large scale projects.

A key feature of the PBA is that it is a trust fund, so the money paid into it—in accordance with the progress payment claim—is held on trust, with the head contractor and subcontractors as beneficiaries. In the event of insolvency, the money is held safely for the subcontractor as a secured creditor. This means that if a head contractor becomes insolvent, subcontractors will not be at risk of not being paid, because the head contractor cannot access the funds held in the PBA for the subcontractor.

Diagram 2 on the following page illustrates how a PBA works.

**Diagram 2: Project bank account (PBA) model**

**Explanation:** In this model, instead of a chain of payments that is vulnerable to insolvency, everyone gets paid from the PBA at the same time. The PBA safeguards progress payments and retention money.

### Other jurisdictions

PBAs are being trialled in New South Wales (NSW), Western Australia (WA) and the Northern Territory (NT) for government projects.

In NSW, PBAs are being currently trialled on 7 projects, the smallest of which has a project value of approximately \$10 million.

WA was the first jurisdiction in Australia to commence a PBA trial, in November 2014. The WA trial will conclude in February 2016. The trial included projects ranging from \$1.5 million to \$27 million.

The NT is trialling a PBA on the \$90 million Tiger Brennan Drive project. The trial will be completed in June 2016.

In Victoria, some private sector projects currently use PBAs.

PBAs have been used effectively in England since 2007. In late 2009, England's Government Construction Board recommended PBAs be used by all public bodies for all future government contracts unless there were compelling reasons not to do so. Since that time, England has embraced the PBA model, and refined it considerably.

Highways England has used the largest number of PBAs, meeting and exceeding government targets for their use by delivering £4.5 billion of government contracts through PBAs in 2013-14. Highways England currently has over 35 PBA projects in operation.

In addition, PBAs are being trialled on government contracts in Northern Ireland and Scotland.

Several states in the United States of America use a trust approach which dictates how funds for subcontractors are treated by head contractors. This is achieved through legislative mechanisms. While there is no requirement for these funds to be kept in a separate trust account like a PBA, the funds are held on trust for the subcontractor as beneficiary. It is considered theft if a head contractor uses these funds before discharging obligations to the subcontractor as beneficiary, and criminal sanctions apply. A similar approach exists in Ontario province in Canada.

Advantages	Disadvantages
<ul style="list-style-type: none"> <li>• Create greater certainty of payment for subcontractors, and provide protection against head contractor insolvency, as funds in the PBA are trust money for the subcontractor as beneficiary, rather than monies that can be divided amongst all creditors.</li> <li>• Ensure that all parties—from the head contractor to each subcontractor—are paid simultaneously, speeding up the payment process for parties lower down in the supply chain and preventing contractors from holding money for as long as legally possible to supplement their own business's cash flow. This provides the following benefits: <ul style="list-style-type: none"> <li>- subcontractors can make savings through a reduced need for debt chasing and administration, and potentially through a reduction in their need to finance lengthy credit periods;</li> <li>- the potential to reduce quoted prices, because the certainty of payment means that subcontractors will not need to build in contingency costs in the event of delayed payments or insolvency of contractors above them in the contractual chain. (England has estimated a 2.5 per cent efficiency saving); and</li> <li>- money moving through the economy faster, which can lead to productivity gains throughout the building and construction sector.</li> </ul> </li> <li>• Increases transparency and accountability in the payment process.</li> <li>• Allow the head contractor to continue to effectively manage the project budgets and costs.</li> <li>• Can be used to safeguard retention money, as well as progress payments. This means that all of a subcontractor's funds are safeguarded by the trust for the subcontractor. In this way, PBAs absorb the benefits of the retention trust fund scheme approach.</li> <li>• Feedback to date from jurisdictions trialling and using PBAs has indicated that they are effective in securing payment for subcontractors.</li> <li>• The current system of cascading payments in the construction industry can permit companies to trade, even though they may actually be insolvent by using money that they are supposed to pay down the chain. PBAs will prevent this from happening.</li> </ul>	<ul style="list-style-type: none"> <li>• Due to being a very different model to the status quo some companies may struggle to understand and adapt to the concept.</li> <li>• Will initially only apply to Government contracts of a certain value. May extend to private contracts in the future.</li> <li>• PBAs may be perceived as only suitable for larger construction contracts due to the requirement to set up a separate PBA for each project.</li> <li>• PBAs may be perceived as increasing red tape in the building and construction industry as well as impacting prices due to the perceived extra administration required. However evidence from other jurisdictions, like England, indicates that once industry becomes familiar with the PBA process, the system will run smoothly and minimal administration is required.</li> <li>• Banks may be unwilling to offer PBAs because that type of account necessitates an undertaking by the bank not to use the bank's right to set off. That is, if a client owes a bank money, the bank can ordinarily take that money from the client's bank account with the bank. As the money in a PBA is held on trust for beneficiaries, this function is not available to the bank. Despite this, many Australian banks offer PBAs.</li> <li>• Legislative changes may be necessary if PBAs are to be used on non-government projects. It will take time to develop the appropriate legislative framework.</li> <li>• PBAs will not eliminate payment disputes and the associated delays in payment.</li> </ul>

**Have your say**

1. Would you support a project bank account trial on government projects? Why?
2. Do you think the use of PBAs in the private sector is feasible in Queensland? Why?
3. Do you think that the use of PBAs in the private sector would improve security of payment? Why?
4. Should there be a minimum amount necessary to use a PBA? If so, what value? Please specify.

## Option 2—Retention Trust Fund Scheme

This option proposes the use of a Retention Trust Fund Scheme (RTFS) to hold subcontractors' retention money in a secure manner.

A typical construction contract includes a form of performance-based security. This security is used to pay for costs associated with:

- late completion of work
- work not complying with contractual requirements
- remedying defects
- non-completion because of the insolvency of the subcontractor.

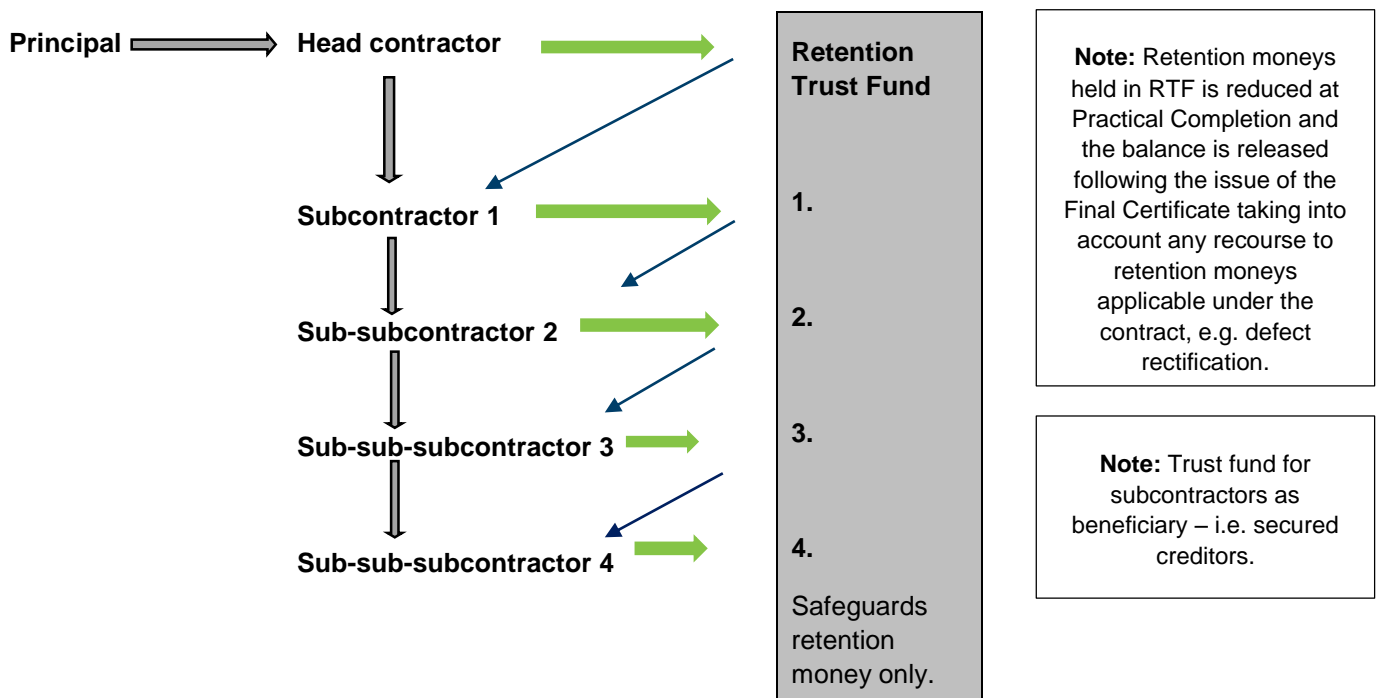
A RTFS requires a head contractor to hold retention money in an account with an authorised deposit taking institution—like a bank. Head contractors can only withdraw money from the trust account as set out in the terms of the contract, otherwise financial penalties apply. A RTFS prevents the head contractor from using retention money as cash flow. Subcontractors are beneficiaries of the trust account, and are seen as secured creditors. In the case that the head contractor/contractor becomes insolvent, the retention money is securely held in the RTFS. This means the money is secured and can't be accessed by liquidators. This is important as often retention money represents a subcontractor's entire profit margin of a project.

A RTFS places reporting obligations on head contractors. Head contractors must report when an account is established, closed and if an account is overdrawn, and the reason why. Penalties will apply for providing false or misleading information. A RTFS requires annual audits with results reported to government.

Financial institutions are obliged to report overdrawn accounts or dishonoured cheques, however, they are under no obligation to control or supervise transactions in relation to the account.

Legislation would be necessary to implement this proposal.

Diagram 3 illustrates how a RTFS operates.

**Diagram 3: Retention Trust Fund Scheme (RTFS) model**

**Explanation:** In this model, the contractual chain of payments is used. Only retention money is safeguarded in a trust account. Progress payments are still subject to insolvency in the contractual chain.

#### Legend

Contract and progress payment

Retention money paid by head contractor/contractor into retention trust fund

Retention money payment to subcontractor



There are two options for the management of the scheme.

#### **Option 2.1—Retention Trust Fund Scheme administered by Government**

This option comprises Government involvement as both an authorised deposit taking institution and a compliance and auditing body.

#### **Option 2.2—Retention Trust Fund Scheme with only compliance and audit provided by Government**

This option requires the private banking sector as the deposit taker with Government involved solely in the compliance and auditing functions.

#### **Other jurisdictions**

A RTFS similar to Option 2.2 was introduced in New South Wales in 2015. It applies to contracts for non-residential building projects worth over \$20 million.

In October 2015, New Zealand introduced a RTFS.



Advantages	Disadvantages
<ul style="list-style-type: none"> <li>• Holding retention money in trust for the benefit of a subcontractor enhances security of payment to the subcontractor who will be paid the money after the defects liability period. This money often represents the full amount of a subcontractor's profit.</li> <li>• This also benefits a contractor, as they can be sure that the retention money is held securely, in case it is needed to remedy any defects.</li> <li>• Introducing trust status for retention moneys will mean that contractors cannot use this to supplement their own business's cash flow because the funds will be secured in a trust account.</li> <li>• Financial institutions are obliged to report overdrawn accounts and dishonoured cheques to Government, which aids compliance.</li> </ul>	<ul style="list-style-type: none"> <li>• Safeguarding only retention monies in trusts may not significantly improve security of payment. This is because retention money does not represent the majority of payments in the construction industry. Progress payments must also be secured as these payments provide for the ongoing livelihoods of subcontractors from month to month.</li> <li>• This model will disadvantage companies who use retention money as working capital.</li> <li>• To be effective a RTFS will need to be supported by a compliance and audit regime, which will likely necessitate additional ongoing resources, which may impose additional costs on the regulator. This could potentially increase licensing fees.</li> <li>• This option will require legislative amendments and cultural reform within the building and construction industry.</li> </ul>

### Have your say

5. Would you support a RTFS? Why?
6. Should a minimum contract value be required before mandating the use of a RTFS? Why?
7. How would this scheme be best administered, and by who? Please provide your reasons.

## Option 3—Insurance schemes

### Option 3.1—Insurance scheme in place of retention money

The concept of retention money is similar in nature to an insurance scheme. For example, retention money is held by a contractor to essentially insure against: late completion of work by the subcontractor; a subcontractor's work not complying with contractual requirements; remedying defects in the subcontractor's building work; and non-completion because of the insolvency of the subcontractor.

This option proposes an insurance scheme to replace the concept and function of retention money.

The insurance scheme would eliminate the need for contractors to hold retention money, which would ensure that subcontractors would receive their retention money. This is important as it often represents the entirety of the subcontractor's profit.

For this option to be successful, legislative changes would be needed in order to prevent retention money clauses from being included in contracts. This would encourage reliance on the insurance scheme rather than continuing to use retention clauses.

This approach proposes an alternative to the traditional method of retention funds.

### Other jurisdictions

This approach does not exist in any other Australian jurisdiction.

Advantages	Disadvantages
<ul style="list-style-type: none"> <li>• This would allow contractors to receive their retention money, just as they receive the rest of their progress payments for work done, from head contractors.</li> <li>• Subcontractors would not have to wait until the end of the defects period to receive their retention money.</li> </ul>	<ul style="list-style-type: none"> <li>• The insurance scheme will mean retention monies will be paid to contractors with their progress payments. However, retention monies only comprise a small part of the security of payment problem, which means a significant improvement to security of payment would not be achieved.</li> <li>• This option may be seen as a disincentive for a subcontractor to complete work, or provide work free from defects, due to the presence of the insurance system.</li> <li>• An insurance scheme would necessitate additional resources, and may potentially be more expensive than the value of retention money.</li> <li>• This option will require significant legislative amendments and cultural reform within the building and construction industry.</li> </ul>

### Have your say

8. Is this a viable option for industry? Why?

## Option 3.2—Head contractor insurance scheme

This option proposes two sub-options for insurance schemes to provide protection for a subcontractor in the case of a head contractor/contractor insolvency.

### ***Option 3.2.1—Head contractor takes out comprehensive insurance for subcontractors***

This would require the head contractor to take out an insurance policy that would protect all subcontractors in the event of the head contractor becoming insolvent. This option would offer protection of both progress payments and retention money for subcontractors. For this option to be successful, legislative changes would be necessary to mandate insurance coverage prior to the engagement of subcontractors for a project.

The scheme would operate by the subcontractor making a claim directly to the insurer once evidence was brought forward of the contractors' inability to make payments.

The success of this option would hinge upon the affordability of the premium specified for insurance. The premium would depend upon the degree of risk of the contractor, contract scope and terms.

### Option 3.2.2—Head contractor takes out retention insurance for subcontractors

This option would see subcontractors providing retention money to a head contractor as occurs under the current framework, however, the head contractor would be required to take out insurance to cover the subcontractor's retention money in the event the head contractor becomes insolvent. This option would only protect retention money.

Advantages	Disadvantages
<ul style="list-style-type: none"> <li>These options would provide certainty that a subcontractor will be paid for work, regardless of whether a contractor becomes insolvent.</li> </ul>	<ul style="list-style-type: none"> <li>These options are a last resort for subcontractors and do not address the issue of why a contractor became insolvent in the first place.</li> <li>Legislation would require certainty that the head contractor was insolvent. This may mean a substantial delay between the time a payment/retention is due and the time a contractor is proved insolvent. This potentially lengthy period could still subject the subcontractor's cash flow to strain, and potentially subcontractor insolvency.</li> <li>Subcontractors may not be privy to the necessary documentation to prove contractor insolvency to the insurer.</li> <li>These options would increase project costs for head contractors in having to pay an insurance premium. This cost would be passed on to the principal contracting the work.</li> </ul>

#### Have your say

9. Is a head contractor insurance scheme a viable option? Why?

### Option 4—Federal legislative changes

This option proposes to change the balance of corporations law to better favour subcontractors. This option would seek to review relevant Commonwealth legislation including the *Corporations Act 2001 (Cth)* and the *Bankruptcy Act 1966 (Cth)* to grant subcontractors a priority payment in the event a head contractor becomes insolvent.

Such an option would require a collaborative approach with all states and territories by lobbying the Commonwealth Government to review and amend the legislation.

Advantages	Disadvantages
<ul style="list-style-type: none"> <li>This option would place subcontractors higher up the chain in being able to recover money from a liquidator.</li> </ul>	<ul style="list-style-type: none"> <li>This option would require extensive collaboration from all of the states and territories to effect the necessary legislative changes.</li> <li>The legislation would also require thorough consultation and is unlikely to be supported by other stakeholders including secured creditors.</li> <li>This approach would require a significant timeframe.</li> </ul>

**Have your say**

10. Do you support a review of legislation including the *Corporations Act 2001 (Cth)* and the *Bankruptcy Act 1966 (Cth)*? Why?
11. Do you see any major barriers to these changes operating effectively? Please provide your reasons.

**Option 5—Education**

This option proposes an education program to increase the financial and business skills of industry. This aligns with submissions to the Senate Committee. These submissions reveal that the building and construction industry lacks skills in financial management, particularly in smaller businesses.

Advantages	Disadvantages
<ul style="list-style-type: none"> <li>Better business practices would lead to a more resilient industry.</li> <li>Improved business management may decrease reliance on the use of retention moneys as cash flow.</li> </ul>	<ul style="list-style-type: none"> <li>While this approach is useful, it does not address the problem of insolvency of head contractors in the contractual chain, which continues to leave subcontractors vulnerable.</li> </ul>

**Have your say**

12. Do you think an education program is needed? Why? For what in particular?
13. Should the education program be voluntary or mandatory? Why?
14. Who do you think should take part in the education program? Why?
15. How do you think an education program should be implemented, and by whom?

## Amendments to the *Building and Construction Industry Payments Act 2004*

In addition to establishing the right to payments, the BCIP Act established an adjudication process to enable quick resolution of disputed or outstanding progress and final payments. This is important because if a subcontractor has not been paid, they may not have the financial resources to go to court. In 2014, amendments were made to the BCIP Act to:

- reallocate responsibility for assigning adjudication applications to an Adjudication Registry within the QBCC instead of through authorised nominating authorities;
- require adjudicators to decide if they have jurisdiction to make a decision;
- provide claimants with an opportunity to withdraw an adjudication application if desired;
- provide respondents with a second opportunity to lodge a payment schedule. A payment schedule sets out the money to be paid in response to a payment claim, and establishes if there is any dispute in the amount claimed;
- extend the statutory time allowed to respond to a complex claim (payment of more than \$750,000);
- amend the definition of 'business day' to reflect industry shutdown periods over Christmas and New Year. Therefore, the time between 22 December and 10 January does not count as business days under the BCIP Act;
- reduce the amount of time during which a payment claim can be made, generally from 12 months to 6 months;
- allow the provision of additional information to an adjudicator for complex claims, including reasons for withholding payment, and whether or not these matters were raised in the payment schedule; and
- allow for the consideration of additional matters in deciding the apportionment of payment of adjudicator's fees. These include the relative success of the parties and reasonableness of conduct of parties in the adjudication.

### Have your say

16. Do you think the 2014 amendments to the BCIP Act improved security of payment? Why?

17. Could the BCIP Act be improved? How?

## Minimum financial requirements policy

The Minimum Financial Requirements policy (MFR Policy) is made under the QBCC Act—this Act regulates the building industry and establishes a licensing and regulatory system for the conduct of building work in Queensland. The QBCC Act identifies the circumstances when proper grounds exist for taking disciplinary action against a licensee or former licensee (refer section 74B). These circumstances include where the licensee, or former licensee, fails to pay a subcontractor in compliance with a building subcontract. The MFR Policy commenced operation in October 2014 replacing the former Financial Requirements for Licensing Policy. The MFR Policy introduced more rigorous requirements for licensees to manage debts appropriately or face possible suspension or cancellation of their licence. Under the MFR Policy, the QBCC is permitted to take action as soon as there is an undisputed debt owing for a period beyond industry trading terms as defined in the policy.

The MFR Policy has been amended over time to provide additional protections to minimise the incidence of building and construction industry contractors becoming insolvent. A new version of the MFR Policy commenced on 9 October 2015 and replaces the version published in 2014.

The new policy contains changes including:

- a requirement that a licensee make a report to the QBCC if its Net Tangible Asset (NTA) position ever decreases by more than 30% from its NTA position as last reported to the QBCC;
- new provisions that will:
  - ensure that licensees are required by law to provide an audit report or review report to the ASIC or the Australian Securities Exchange (ASX). The licensee would also have to provide a copy of that report to the QBCC within 30 days of providing it to the ASIC or the ASX. This will ensure that the QBCC receives this important financial and audit information about licensees routinely;
  - clarify the format of the financial reporting required of a licensee when the QBCC has concerns that the licensee's financial circumstances may not satisfy the requirements of the MFR Policy; and
  - place stricter disclosure requirements on accountants where they provide a licensee's financial information to the QBCC based on qualified audited financial statements.

The previous Financial Requirements for Licensing Policy required licensees to provide a declaration or report to the QBCC regarding their financial position when their licence was due for renewal and whenever their NTA position decreased by more than 10% for more than one month.

#### **Have your say**

18. Should the NTA reduction trigger remain at 30%? If no, what is a reasonable figure? Please provide your reasoning.
19. Do you think the trigger event for reporting to the QBCC should continue to be defined by reference to a comparison of the licensee's NTA position from time to time with its last advised and QBCC accepted NTA position? Please provide your reasons.
20. Would some other comparison be more appropriate? What and why?
21. Would you support a review of the effectiveness of prompt payment provisions in the QBCC Act? Why?
22. Would you support harsher penalties for late or missing payments to subcontractors? Please provide your reasons.

## **Subcontractors' Charges Act 1974**

If a subcontractor is owed payment by a contractor higher in the contractual chain, in certain circumstances, the subcontractor can seek to recover this money from another contractor yet higher in the contractual chain than the contractor that owes the subcontractor. The subcontractor can put in place a statutory charge over the money the higher contractor intends to pay the defaulting contractor. Court action is required to secure the payment.

This means that even if a subcontractor isn't paid by a party it has a direct contract with, the subcontractor can quarantine payments owed to the defaulting contractor by other contractors, so that this money can be paid to the subcontractor. In this way, the SC Act gets around the flow on effects of insolvency in the contractual chain. The SC Act is only useful if the higher contractor has not yet paid the defaulting contractor.



The subcontractor is required to commence court action to secure the payment, if the claim is not accepted by the contractor.

The statutory charge gives the subcontractor priority of payment, ahead of both secured and unsecured creditors. The charge stops the higher contractor from paying money to a defaulting contractor and the higher contractor must retain that money or pay it into court. The monies are frozen pending final contractual resolution through the courts, which can be a lengthy and costly exercise.

The main difference between this Act and the BCIP Act is that under the SC Act, monies payable by the higher contractor to a defaulting contractor are secured straight away.

It has been suggested that this Act is hard to understand and use, with only minor non-compliances with the legislation resulting in claims being ruled invalid.

**Have your say**

23. How do you think the *Subcontractors' Charges Act 1974* is working?

24. What changes are necessary, if any, to the *Subcontractors' Charges Act 1974*?

## Other Suggestions

We are interested in any other option or suggestion you may have which may increase security of payment for subcontractors.

**Have your say**

25. Do you think we should consider other options? If so, what are these?

26. Do you have ideas about implementation of an option? If so, please provide relevant detail.

## Summary list of questions

1. Would you support a project bank account trial on government projects? Why?
2. Do you think the use of PBAs in the private sector is feasible in Queensland? Why?
3. Do you think that the use of PBAs in the private sector would improve security of payment? Why?
4. Should there be a minimum amount necessary to use a PBA? If so, what value? Please specify?
5. Would you support a RTFS? Why?
6. Should a minimum contract value be required before mandating the use of a RTFS? Why?
7. How would this scheme be best administered, and by who? Please provide your reasons.
8. Is this a viable option for industry? Why?
9. Is a head contractor insurance scheme a viable option? Why?
10. Do you support a review of legislation including the *Corporations Act 2001 (Cth)* and the *Bankruptcy Act 1966 (Cth)*? Why?
11. Do you see any major barriers to these changes operating effectively? Please provide your reasons.
12. Do you think an education program is needed? Why? For what in particular?
13. Should the education program be voluntary or mandatory? Why?
14. Who do you think should take part in the education program? Why?
15. How do you think an education program should be implemented and by whom?
16. Do you think the 2014 amendments to the BCIP Act improved security of payment? Why?
17. Could the BCIP Act be improved? How?
18. Should the NTA reduction trigger remain at 30%? If no, what is a reasonable figure? Please provide your reasons.
19. Do you think the trigger event for reporting to the QBCC should continue to be defined by reference to a comparison of the licensee's NTA position from time to time with its last advised and QBCC accepted NTA position? Please provide your reasons.
20. Would some other comparison be more appropriate? What and why?
21. Would you support a review of the effectiveness of prompt payment provisions in the QBCC Act? Why?
22. Would you support harsher penalties for late or missing payments to subcontractors? Please provide your reasons.
23. How do you think the *Subcontractors' Charges Act 1974* is working?
24. What changes are necessary, if any, to the *Subcontractors' Charges Act 1974*?
25. Do you think we should consider other options? If so, what are these?
26. Do you have ideas about implementation of an option? If so, please provide relevant detail.

## Glossary

ASIC	Australian Securities and Investments Commission
BCIP Act	<i>Building and Construction Industry Payments Act 2004</i>
MFR Policy	Minimum Financial Requirements Policy
NTA position	Net Tangible Asset position, under the MFR Policy
PBA	Project Bank Account
QBCC	Queensland Building and Construction Commission
QBCC Act	<i>Queensland Building and Construction Commission Act 1991</i>
RTFS	Retention Trust Fund Scheme
SC Act	<i>Subcontractors' Charges Act 1974</i>
Senate Committee	Senate Standing Committee on Economics

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