



# Regulatory Impact Statement

Building and Construction Industry Security of Payment  
Regulation 2020 – June 2020



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## Executive summary

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The consultation draft *Building and Construction Industry Security of Payment Regulation 2020* (the **proposed Regulation**) is proposed by the Hon Kevin Anderson MP, Minister for Better Regulation and Innovation, whose portfolio responsibilities cover building regulation in New South Wales.

The *Building and Construction Industry Security of Payment Regulation 2008* (the **current Regulation**) sets out the administrative functions supporting the *Building and Construction Industry Security of Payment Act 1999* (the **Act**). The NSW Government intends to remake the current Regulation as it is scheduled to lapse under the sun-setting provisions of the *Subordinate Legislation Act 1989* on 1 September 2021.

The proposed Regulation would repeal the current Regulation. Once the proposed Regulation is finalised, the final *Building and Construction Industry Security of Payment Regulation 2020* will commence on 1 September 2020, with a transitional period provided for some reforms.

In 2018, the Act was reviewed to enhance the level of protection provided to subcontractors to ensure that they obtain payment for completed work for supplied goods or services, and to improve national consistency in security of payment legislation.

The *Building and Construction Industry Security of Payment Amendment Act 2018* (the **Amendment Act**) was assented on 28 November 2018, providing for a new payment structure, faster payments for contractors and subcontractors and enabling disputes over payments to be resolved quickly and fairly. These reforms commenced on 21 October 2019 to introduce a simpler and stronger system of securing payments for subcontractors.

Implementing the proposed Regulation is the final step in completing the review to deliver a more secure system of contractor payments within the New South Wales building and construction industry.

The proposed Regulation is remade under the Act with changes that are designed to:

- reduce regulatory requirements without compromising subcontractor payments;
- provide greater protections for retention money;
- improve administrative efficiency in the retention money trust regulatory framework; and
- provide clarity about adjudicator eligibility, aimed at having more consistent outcomes for parties to a dispute.

The main changes in the proposed Regulation will:

- reduce the project value threshold from \$20 million to \$10 million for retention money trust account requirements;

- remove annual reporting requirements for retention money trust accounts;
- introduce an obligation to provide retention money trust account records to subcontractors whose money is held in trust; and
- introduce qualification and eligibility requirements for adjudicators.

This Regulatory Impact Statement (**RIS**) has been prepared as part of the making of the proposed Regulation to identify and assess direct and indirect costs and benefits to ensure that the proposed Regulation is necessary, appropriate and proportionate to risk. The RIS sets out the rationale and objectives of the proposed Regulation and the various options for achieving the objectives. It also provides a discussion on important aspects of the proposed Regulation and seeks feedback from stakeholders and the community. This RIS should be read with the proposed Regulation.

The proposed Regulation will be available for a four-week consultation period. Submissions are invited on any of the matters raised in the discussion or anything else contained in the proposed Regulation. All submissions will be considered and evaluated, and any necessary changes will be made to address the issues identified before the proposed Regulation is finalised.

The process for submitting comments is explained in the following section below.

# Consultation process

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## Making a submission

Interested organisations and individuals are invited to provide a submission on any matter relevant to the proposed Regulation, whether or not it is addressed in this RIS. You may wish to comment on only one or two matters of particular interest, or all of the issues raised. Matters covered by the principal Act are not the subject of the consultation process.

To assist you in making a submission, an optional online submission form will be available on our website at <https://www.fairtrading.nsw.gov.au>. However, this form is not compulsory, and submissions can be in any written format.

Submissions can be made by email and the Department requests 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). More information on how you can make your submission accessible is at <http://webaim.org/techniques/word/>.

Please forward submissions by:

Email to: [SecurityofPaymentPolicy@customerservice.nsw.gov.au](mailto:SecurityofPaymentPolicy@customerservice.nsw.gov.au)

Mail to: Security of Payment Regulation 2020  
Policy and Strategy, Better Regulation Division  
Locked Bag 2906  
LISAROW NSW 2252

**The closing date for submissions is 5pm Friday, 24 July 2020.**

We invite you to read this paper and provide comments. You can download the RIS and the proposed Regulation from [www.fairtrading.nsw.gov.au](http://www.fairtrading.nsw.gov.au). Printed copies can be requested from NSW Fair Trading by phone on 13 32 20.

### **Important note: release of submissions**

All submissions will be made publicly available. If you do not want your personal details or any part of your submission 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*). It is

also a statutory requirement that all submissions are provided to the Legislation Review Committee of Parliament.

### **Identified stakeholders**

This RIS has been provided directly to some stakeholder organisations. A list of these stakeholders is provided at **Appendix 3**.

### **Evaluation of submissions**

All submissions will be considered and assessed. The proposed Regulation will be amended, if necessary, to address issues identified in the consultation process. If further information is required, targeted consultation will be held before the proposed Regulation is finalised.

### **Commencement of the Regulation**

After the Minister for Better Regulation and Innovation has finalised the Regulation, it will be submitted to the Governor for approval.

Once approved by the Governor, the Regulation will be published on the official NSW Government website for online publication of legislation at [www.legislation.nsw.gov.au](http://www.legislation.nsw.gov.au) and in the NSW Government Gazette. Information on how to access the Gazette is available on the NSW Parliamentary Counsel's website.

It is proposed the Regulation will commence on **1 September 2020**.



## Need for government action

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On 21 October 2019, significant changes commenced to the security of payments sector through the Amendment Act. These changes sought to address poor payment practices and the high incidence of insolvencies in the building and construction industry. They also sought to facilitate prompt payment, preserve cashflow and resolve disputes quickly and efficiently. To complement these changes, the Government is seeking to review the current Regulation to finalise the outcome of the holistic review of security of payment legislation.

The *Subordinate Legislation Act 1989* provides for the automatic repeal of statutory rules (regulations) after they have been in force for five years. The automatic repeal of the current Regulation was previously due to be repealed on 1 September 2020 unless remade. In response to the COVID-19 pandemic, the *COVID-19 Legislation Amendment (Emergency Measures) Act 2020* which commenced on 25 March 2020, postponed the repeal of several regulations, including the current Regulation to 1 September 2021. The current Regulation is now due to be repealed on 1 September 2021 unless remade.

The re-write of the current Regulation:

- seeks to provide greater protection to subcontractors and promote cashflow and transparency within the contracting chain
- will extend existing trust obligations for retention money to provide protections to more construction projects
- reduces regulatory burden on industry by removing the need to report annually on the operation of retention money trust accounts
- aims for more consistent outcomes for parties in adjudication by introducing qualifications and eligibility requirements for adjudicators.

For these reasons, it is considered in the best interest of the industry to proceed with the proposed Regulation as soon as possible to enact these vital changes.

Accordingly, despite the one-year extension provided by the postponed repeal date, the NSW Government is proceeding with the finalisation of the proposed Regulation by 1 September 2020, rather than 2021.

The issues canvassed in this RIS do not represent the final Government position on the amendments but provide an opportunity for discussion with building and construction stakeholders, adjudicators and the general community.

# Objective and rationale of the Regulation

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## Objective of government intervention

The primary objective of the proposed Regulation is to provide the legislative support and administrative detail for the operation of the Act. The objects of the Act are to:

- ensure that anyone who carries out construction work (or who supplies related goods and services) under a construction contract is entitled to receive, and is able to recover, progress payments relating to the carrying out of that work and the supplying of those goods and services;
- grant a statutory entitlement to such a payment regardless of whether the relevant construction contract makes provision for progress payments; and
- establish a procedure to recover a progress payment to ensure payment, including how any disputed claims are adjudicated.

Regulations are integral to the effective operation of the Act. While the primary objective of the proposed regulation is to support the operation of the Act, the complementary objectives of the proposed Regulation are to:

- prescribe the qualifications, skills and experience required for adjudicators;
- provide clarity for adjudicators about when they may be ineligible to perform their duties;
- establish a new threshold for capturing projects where retention moneys must be held in trust accounts;
- reduce regulatory burden associated with reporting requirements for retention money trust accounts;
- provide subcontractors with visibility over trust account records of retention money held on their behalf; and
- strengthen compliance and enforcement by prescribing penalty notice amounts for offence provisions in the Act and supporting regulations.

## Options for achieving objectives

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Three options were assessed for achieving the objectives of the proposed Regulation. These include:

### **Option 1: Take no action**

Taking no action means the current Regulation would lapse under the *Subordinate Legislation Act 1989* on 1 September 2021 and the proposed Regulation would not be made. This would result in no regulation to support the Act.

### **Option 2: Maintain the status quo**

The proposed Regulation would not be made. Instead, the current Regulation would be remade with no changes to existing provisions. Maintaining the status quo would result in fewer benefits that could otherwise be realised by streamlining the regulation and reducing business costs associated with annual reporting.

### **Option 3: Make the proposed Regulation**

The proposed Regulation would retain some existing provisions from the current Regulation, where appropriate, and amend the requirements for retention money trust accounts. Annual reporting requirements for these trust accounts would be removed and replaced with a new obligation for trust account records to be provided to subcontractors where money is held in trust for them. In addition, complementary changes have been proposed to reduce the project value threshold from \$20 million to \$10 million for complying with retention money trust account requirements. These changes will provide transparency and protection to subcontractors on the operation of these trust accounts, while managing regulatory burden on the sector.

The proposed Regulation would also introduce qualifications and eligibility requirements for adjudicators to provide greater clarity about determining the suitability of an adjudicator.

### **Criteria used to assess the regulatory options**

The following criteria, which relate to the regulatory objectives, is used in the evaluation of the three options:

- the extent to which the option supports the objectives of the Act;
- the cost effectiveness of each option, in terms of costs and benefits to businesses, impacts on community and government; and
- the extent to which the option contributes to the overall efficiency of the regulatory system.

The NSW Productivity Commission's Guide to Better Regulation notes that when considering the costs and benefits of different options, compliance costs, economic, social and environmental

impacts should be considered. The Guide to Better Regulation can be found at <https://www.productivity.nsw.gov.au/better-regulation>.

# Impact assessment of options

## Preferred option

After analysing the costs and benefits of each option to the community, industry and government, the option that supports the objectives of the Act and contributes to the overall efficiency of the regulatory system is **Option 3 – Make the proposed Regulation**. The proposed Regulation will provide the legislative support and administrative detail needed to facilitate the operation of the Act, with considerable benefits to the community, industry and the government.

## Summary of costs and benefits of each option

A summary of the costs and benefits for all three options is shown in **Table 1**. This shows that **Option 3 – Make the proposed Regulation** has the highest overall benefit to the industry, community and government.

Option	Likely costs	Likely benefits	Overall benefit
<b>Option 1</b> Take no action	Medium	Low	Negative
<b>Option 2</b> Maintain the status quo	Medium	Medium	Neutral
<b>Option 3</b> Make the proposed Regulation	Medium	High	Positive

Table 1: Summary of costs and benefits for each option

## Assessment of Option 1 – Take no action

### Costs

Industry costs would be incurred if the current Regulation is able to automatically lapse. Without the provisions provided in the current Regulation, the intention and detail of the Act would not be clear, which would lead to an increase in the number of disputes. This would result in greater costs to individuals and organisations due to the time and money spent dealing with problems when disagreements arise. **The overall cost to industry has been assessed as medium.**

Community costs would be moderate. Taking no action would result in reduced community confidence in the industry, forfeiting the ability for government to provide protection to small businesses and subcontractors. Retention money trust accounts have the effect of protecting subcontractors from payment defaults and misuse of funds and reduce the incidence of insolvency of third parties in the contract chain. Money held in trust is more greatly protected as it cannot be seized or frozen during bankruptcy and managed through controls on the withdrawal of funds. The existence of retention trusts can also lead to a speedier resolution of disputes, as money that is held in trust cannot be withdrawn from the trust account until all beneficiary claims have been met.

Further, under this option, enforcement under the Act would require court action to penalise any wrongdoing, without the ability to issue penalty infringement notices. **The overall cost to the community has been assessed as medium.**

Government costs would increase as the government's regulatory responsibilities would continue under the Act. Without the requirements for head contractors to establish retention money trust accounts, disputes and payment defaults would result in an increase in the number of complaints received by Fair Trading. Additional staffing and resources would be required to effectively deal with the increased number of complaints. There would also be direct costs associated with small businesses going out of business, affecting families and society, which could have flow on effects to government through increased social security and welfare payments. Allowing the current Regulation to lapse would also remove the ability for penalty notices to be issued by Fair Trading. All breaches of the Act would need to be pursued through the courts, resulting in a substantial increase in compliance costs. This would make it difficult to discourage any illegal behaviour in the industry including bribery, conflicts of interest and misconduct. **The overall cost to government has been assessed as high.**

**The overall costs associated with Option 1 – Take no action have been assessed as medium.**

## **Benefits**

Industry benefits would be varied. For a small portion of the industry currently required to hold retention money, some savings would be achieved through the removal of retention money trust requirements. Specifically, this part of the industry would benefit financially from not being required to establish trust accounts and undertake annual reporting on the operation of these accounts. However, these benefits would be offset by the significant reduction in benefits that arises for a larger portion of the industry from the removal of existing protections for retention money. Subcontractors will face a higher risk that money retained on their behalf is not available at the end of the project. **The overall benefit to industry has been assessed as medium.**

Community benefits would be minimal. The current Regulation sets out the retention money framework, including critical obligations for managing retention money. Without these obligations, subcontractors within the construction industry would lose existing protections relating to payments. The loss of this protection could lead to more insolvencies and the collapse of small businesses, having a profound impact on other parties in the contractual chain, as well as client,

families and the community. Public confidence in the industry would also likely be reduced. **The overall benefit to the community has been assessed as low.**

Government benefits would be minor and primarily relate to the savings achieved in time and resources in not having to remake the current Regulation or managing the responses to reporting requirements. However, these benefits would be outweighed by the costs associated with handling more complaints for non-payment to subcontractors. Comparatively, the industry is known for having poor payment practices and a high incidence of insolvency. Complaints would be escalated without the protection of retention money trust accounts for payments to subcontractors. There would also be reputational cost to the government of not adequately protecting the public or implementing the recommendations of independent reviews relating to the sector, such as the *Independent Inquiry into Construction Industry Insolvency* (the **Collins Inquiry**) in 2012 and the *Review of Security of Payment Laws by John Murray AM* (the **Murray Review**) in 2017. **The overall benefit to government has been assessed as low.**

**The overall benefits associated with Option 1 – Take no action have been assessed as low.**

## Conclusion

The Act cannot function as intended without a supporting Regulation. Taking no action would result in the current Regulation lapsing on 1 September 2021, with no replacement Regulation being made. This option would significantly reduce protection for small businesses and subcontractors.

Further action by the government would be required to enact these functions, such as amending the Act to enshrine the requirements of the current Regulation. This would reduce the capacity to amend the requirements quickly to respond to problems that may arise, or to address changes in industry practices. For these reasons, **Option 1 – Take no action is not the preferred option.**

## Assessment of Option 2 – Maintain the status quo

### Costs

Industry costs would be high, arising from the indirect costs of the missed opportunity to reduce red tape and administrative burden that would otherwise be provided by the proposed Regulation. The proposed Regulation removes the requirement for head contractors to provide the Secretary with an annual report on retention money trust accounts. It has been estimated that the cost to provide the annual report is between \$3,000 and \$10,000, depending on the complexity of the accounts. Stakeholders have expressed concerns that the annual reporting requirements are onerous, and

head contractors have been encouraged to take out bank guarantees in place of retention money trust accounts. 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. By maintaining the status quo, the current reporting requirements would continue to exist. **The overall cost to industry has been assessed as high.**

Community costs are likely to be moderate. As the legislative scheme deals with subcontractors, the community costs relate to costs imposed on industry who would otherwise be protected by the benefits of the proposed Regulation. Despite the protections afforded by the current Regulation, the proposed Regulation provides an opportunity to increase protection to industry and small businesses by lowering the threshold of projects required to hold retention money trust accounts. It also introduces penalties for corporations that do not comply with trust account requirements and establishes eligibility requirements for adjudicators. These benefits would also have an impact on the livelihoods of individuals employed by the industry, indirectly benefiting the community. **The overall cost to the community has been assessed as medium.**

Government costs would likely be moderate. Maintaining the current Regulation represents a lost opportunity for the government to improve the regulatory framework and provide greater protection for subcontractors. The government would suffer reputational risk by not revising the regulatory framework to be consistent with the recommendations of independent reviews undertaken into the sector. The administrative and financial costs of the administration of the current Regulation would be similar if the current Regulation was remade without amendment. **The overall cost to industry has been assessed as medium.**

**The overall costs associated with Option 2 – Maintain the status quo have been assessed as medium.**

## **Benefits**

Industry benefits are likely to be moderate as the primary benefit of this option is the savings achieved by not having to transition into the new requirements of the proposed Regulation. Members of the industry could continue operations under existing practices. This would be offset by the continued costs associated with the annual reporting requirements. Proceeding with this



option would avoid any new regulatory impact. **The overall benefit to industry has been assessed as medium.**

Community benefits relate primarily to the benefits that would be afforded to industry. These benefits would flow on to individuals who are employed by the sector and indirectly affect the community. The current Regulation would continue to provide the existing benefits, and time and effort would be saved in not having to adapt to any new legislative requirements. This option would still provide the necessary administrative mechanisms to support the Act. However, the benefits of increasing protection for small businesses resulting from the lower threshold of projects requiring retention money trust accounts under the proposed Regulation would be not be realised. **The overall benefit to the community has been assessed as medium.**

Government benefits would be primarily limited to the administrative savings that could be achieved. Proceeding with this option would mean that guidance and advice material provided by Fair Trading would not need to be updated. There would be no requirement to publicise any legislative changes. Fair Trading staff would not need to be re-trained on the new legislation. However, this option would not improve any existing issues, and complaints and disputes would still need to be managed. **The overall benefit to government has been assessed as medium.**

**The overall benefits associated with Option 2 – Maintain the status quo have been assessed as medium.**

## **Conclusion**

Remaking the current Regulation in its present form would not impose any new costs on industry or the community. However, it would fail to respond to the recommendations made by independent reviews into the sector and would not result in any significant benefits or improvements to the sector. Enhancements provided by the proposed Regulation would not be realised. This would have an overall negative impact on industry, community and the government. For these reasons, **Option 2 – Maintain the status quo is not the preferred option.**

## Assessment of Option 3 – Make the proposed Regulation

### Costs

Industry costs are likely to be varied. The current Regulation requires head contractors to pay retention moneys into a trust account for construction projects valued at least \$20 million. The proposed Regulation will reduce this value to at least \$10 million for contracts entered into from 1 January 2021. Lowering the project value threshold will require more head contractors to establish trust accounts.

It is expected that any increase in the regulatory burden associated with this requirement will be offset by the removal of the annual reporting requirements which have been estimated to cost businesses up to \$10,000, depending on the complexity of the accounts. It is noted that while the proposed Regulation will commence on 1 September 2020, the proposed Regulation provides that annual reporting will not be required to be submitted for the 2019/20 financial year.

The potential cost impacts to industry will relate to understanding the new requirements, establishing trust accounts and reflecting these requirements in their business practices. **The overall cost to industry has been assessed as medium.**

Community costs would be minimal. Capturing projects at a lower threshold will require more head contractors to establish retention money trust accounts. Where head contractors have not been captured by this requirement in the current Regulation, there may be a chance that this may have a flow-on effect such as delays in construction of developments by more projects falling into the lower threshold and the requirement to establish retention money trust accounts. Conversely, an increase in the number of projects that must establish retention money trust accounts will ensure that more money is protected for the benefit of small businesses, while providing steady cashflow within the community. **The overall cost to community has been assessed as low.**

Government costs would be moderate. The government would incur initial administrative costs to educate industry about the changes under the proposed Regulation, and to monitor and audit authorised nominating authorities and adjudicators against the new eligibility requirements. The costs would be offset by the removal of the annual reporting requirements. It is noted that although the information provided by reporting requirements would no longer be readily available through mandatory reporting, efficiencies would be gained through targeted auditing of retention money trust accounts based on risk profiles of businesses. **The overall cost to government has been assessed as medium.**

**The overall costs associated with Option 3 – Make the proposed Regulation have been assessed as medium.**

## **Benefits**

Industry benefits would largely be derived from extending trust obligations for retention money to better protect small businesses and subcontractors. The industry is known as having a high incidence of insolvency and relatively poor payment practices. Given the hierarchical nature of contracting in the industry, insolvency by a single entity often impacts a range of other parties in the contractual chain. Subcontractors at the base of the contractual chain are particularly vulnerable as they are likely to be small businesses with a reduced ability to withstand unplanned financial losses. The reduction in the project value threshold for retention money trust requirements from at least \$20 million to at least \$10 million will provide the benefit of protecting a greater number of subcontractors and small businesses in the industry.

The annual reporting obligations under the current Regulation will not be required in the proposed Regulation. The benefit of removing this requirement will be the reduction in red tape for head contractors, providing financial savings and reduction in time spent preparing and procuring reports.

Subcontractors will be entitled to inspect the retention money trust account records held by the head contractor. This will increase transparency in the management practices of head contractors for retention money trust accounts and provide subcontractors with greater confidence that retention money is being appropriately held on trust and that such moneys will be available to them when rightfully due.

Industry perception of adjudicators will be strengthened through the new eligibility requirements for adjudicators, requiring them to be suitably qualified and experienced before being able to carry out the resolution of payment claim disputes for construction contracts. This requirement could also have the effect of minimising the number of court hearings for disputes, reducing the overall burden on the courts through fewer matters. **The overall benefit to industry has been assessed as high.**

Community benefits would be achieved through increased consumer protection. Retention money trusts provide protections that are necessary to ensure that money from the head contractor reaches the intended person. Without these trusts, subcontractors and small businesses that are not paid for supplied services or materials would struggle with debts and may become insolvent if payments are not made or delayed. This impact has flow on effects to the community, regional

areas and the general public, both in terms of impact on livelihoods as well as potential delays in the intended use or occupation of commercial and residential buildings. Reducing the value of projects from at least \$20 million to at least \$10 million will expand the range of projects that would be required to establish trust accounts, providing further protections to more subcontractors and small businesses. **The overall benefit to the community has been assessed as medium.**

Government benefits would be realised by ensuring the legislation is functioning effectively and is supporting the objectives of the Act. Corporations will be subject to significant penalties if they fail to establish retention money trust accounts for subcontractors. Executive liability offences will be extended to directors to encourage directors to take reasonable steps to ensure compliance with legislative obligations. The proposed Regulation will provide subcontractors with a right to inspect retention money trust records, which is likely to incentivise greater levels of self-regulation. This will allow Fair Trading to adopt a risk-based compliance program and conduct investigations where necessary. The proposed Regulation will also provide comprehensive enforcement provisions that will enable the regulator to more effectively carry out compliance and enforcement actions, while reducing red tape. **The overall benefit to government has been assessed as high.**

**The overall benefits associated with Option 3 – Make the proposed Regulation have been assessed as high.**

## Conclusion

This option enables the proposed Regulation to meet the regulatory objectives of the Act and provides a more streamlined and consistent approach to regulating the building and construction industry. This option addresses several weaknesses in the current Regulation and provides the greatest benefit to the industry, community and government, outweighing any new costs. The cost impact of the proposed Regulation would be partly offset by the red tape reduction measures in reducing compliance burdens on industry. For these reasons, **Option 3 – Make the proposed Regulation is the preferred option.**

# Discussion of the proposed Regulation

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Submissions are welcome on any aspect of the proposed Regulation or any other relevant issue, whether or not raised in this RIS. This section will outline discussion points to provide greater context for the key provisions contained in the proposed Regulation.

A summary of the proposed Regulation is provided in **Appendix 2**.

A list of questions posed in this chapter with a reference to the page number is provided in **Appendix 4**.

## Part 1 Preliminary

### Clause 2 – Date of commencement

The current Regulation is due to be automatically repealed on 1 September 2021 under the *Subordinate Legislation Act 1989* following its postponement in response to the COVID-19 pandemic.

Clause 2 provides that the proposed Regulation will commence on 1 September 2020. It is considered appropriate to continue with the remake of the Regulation in 2020, rather than 2021 because of the benefits that will be realised through the proposed Regulation.

The proposed Regulation will extend existing trust obligations for retention money to provide protections to more construction projects. It will also reduce regulatory burden on industry by removing the need to report annually on the operation of retention money trust accounts. By introducing qualifications and eligibility requirements for adjudicators, the proposed Regulation aims to produce more consistent outcomes for parties in adjudication. For these reasons, it is considered to be in the best interest of the industry to proceed with the proposed Regulation and enact these changes as soon as possible.

Accordingly, despite the one-year extension provided by the postponed repeal date, the NSW Government is proceeding with the finalisation of the proposed Regulation by 1 September 2020.

- 1. Is the commencement date of 1 September 2020 for the proposed Regulation appropriate? Why or why not?**

### Clause 4 – Application of Act

Section 7(5) of the Act provides that the Act does not apply to any construction contract, or class of construction contracts, that are prescribed by the regulations. Clause 4 of the proposed Regulation

prescribes 'owner occupier construction contracts' as a class of construction contract to which the Act does not apply.

The Act defines an owner occupier construction contract to mean a construction contract for the carrying out of residential building work within the meaning of the *Home Building Act 1989* on such part of any premises as the party for whom the work is carried out resides or proposes to reside in.

This effectively means that builders who carry out construction work in the residential sector can't make a statutory payment claim against an owner occupier, even though subcontractors who carry out work on the same project can make such claims against the builder. This can put builders in a difficult financial position in circumstances where the owner occupier doesn't pay the builder, but the builder is still obliged to pay the subcontractors.

The Act has always excluded these construction contracts and during the review of the Act, some stakeholders expressed support for abolishing this exemption. The removal of this exemption was also a recommendation in the Federal Review of Security of Payment laws by Mr John Murray AM. However, other stakeholders expressed concern about the adverse impacts on owner occupiers who would lack experience and expertise to understand and comply with the requirements under the Act.

To allow further consideration and consultation on this reform, the Act was amended to remove the exemption and replicate it in the Regulation. When the Regulation was amended following the review, 18 submissions were received when it was exposed for public consultation, of which only 11 directly commented on the substance of the amendments. Of the 11, 6 expressed support for the Regulation as amended, while 5 specifically expressed concern over the exemption.

The exemption has been maintained in the proposed Regulation, however feedback is sought on whether it should be maintained. Feedback is also sought on whether additional consumer protection safeguards would be needed if the exemption was removed. For example, using powers under the *Home Building Act 1989*, requirements could be imposed on contracts entered into with owner occupiers to do residential building work that requires information explaining obligations under the security of payment legislation, i.e. how the owner occupier can reply to payment claims and the time periods that apply. These requirements would only apply to contracts caught by the Home Building Act which has threshold requirements (contracts for small jobs where the contract price is between \$5,000-\$20,000 and other contracts for jobs where the contract price exceeds \$20,000).

2. Do you support maintaining the exemption for owner occupier construction contracts? Why or why not?
3. If the exemption is removed, are additional consumer protection safeguards required? Why or why not? If so, what safeguards do you suggest and please provide comment on the suitability of imposing contract requirements under the *Home Building Act 1989*, noting the threshold requirement.

## Part 2 Trust accounts for retention money

### Division 1 – Preliminary

#### Clause 6 – Application of Part – projects with a value of at least \$10 million

Section 12A(1) of the Act enables the proposed Regulation to make provision for, or with respect to requiring retention money to be held in trust for the subcontractor entitled to the money. It also enables the proposed Regulation to require the head contractor that holds retention money to pay the money into a trust account (a **retention money trust account**).

It is proposed that the amended clause will extend trust obligations for retention money to a broader scope of construction projects.

The current Regulation requires head contractors to pay retention money into a trust account for construction projects valued at least \$20 million. Clause 6 of the proposed Regulation will reduce the threshold for projects from a value of at least \$20 million to projects with a value of at least \$10 million for contracts entered into from 1 January 2021.

The Murray Review and the Collins Inquiry supported the expansion of retention money trust requirements to all contracting parties under security of payment legislation. Both reports argued that the administrative burden of a trust was critical to countering the situation of head contractors misusing and withholding retention moneys duly owed to subcontractors.

During the recent review of the Act, stakeholders expressed divergent views on this reform proposal. Those stakeholders in support of extending the retention money trust requirement to the entire contracting chain supported removing the threshold requirement altogether. On the other hand, stakeholders who opposed lowering the threshold amount felt that the proposal would lead to additional administrative burden on a greater portion of the sector.

The proposed reforms moderate the impact of imposing trustee obligations on small businesses by retaining a threshold for contracts valued at least \$10 million. However, the reform is consistent with the policy intent of recommendation 81 of the Murray Review in that it seeks to expand the use of trusts for retention money.

To offset the increased regulatory burden that could arise from the proposed \$10 million threshold, the annual reporting requirements relating to the operation of retention money trust accounts will no longer be required.

- 4. Do you support a reduction in the retention money trust account threshold from \$20 million to \$10 million? Why or why not?**

### **Division 2 Trust account requirements**

Clause 8(2) of the proposed Regulation creates a new obligation for head contractors to deposit trust money into the retention money trust account as soon as possible after receiving the money. The head contractor must ensure that the money is paid into and retained in a trust account established with an approved authorised deposit-taking institution (**ADI**).

Although it is preferable that retention money is deposited directly into the trust account at the time of the transaction, there may be circumstances where this is not possible (for example, where a payment is made to the contractor instead of directly to the account). In this instance, a head contractor would be expected to deposit the money into the trust account within 7 days after receiving the retention money.

- 5. Are there any reasonable circumstances in which retention money could not be deposited into a trust account within 7 days?**
- 6. Is the suggested timeframe of 7 days to deposit money into a trust account appropriate? If not, what is a more appropriate timeframe?**

### **Division 3 Records and information**

The head contractor must keep certain records related to the retention money trust account. Under clause 16(2) of the proposed Regulation, the head contractor will be required to keep a separate ledger for retention money held for each subcontractor. Clause 16(3) of the proposed Regulation sets out the type of information that must be in the ledger. A subcontractor must be provided with a copy of the ledger at least once every 3 months, or as often as agreed in writing between the two parties, provided it is at least once every 12 months.

Head contractors will no longer be required to submit annual reports on the operation of retention money trust accounts to Fair Trading. It has been estimated that the cost of conducting the report ranges from \$3,000 to \$10,000, depending on the complexity of the accounts. Streamlining the



reporting requirements by replacing the annual reports with the requirement to provide copies of ledgers, will moderate the regulatory burden on head contractors.

The revised record and information requirements will promote transparency in the management of retention money trust accounts. Subcontractors will also be provided with greater confidence that retention money is being appropriately held and that such moneys will be available to them when rightfully due. Head contractors may also be incentivised to self-regulate on the understanding that subcontractors can inspect retention money trust records more regularly.

The proposed Regulation will not include the power for an authorised officer to require information or offences for provision of false or misleading information, which are set out under clauses 15 and 17 of the current Regulation. These provisions have been removed from the proposed Regulation as sections 32G and 32P of the Act already provide for similar powers and their inclusion would have a duplicative effect.

**7. Is there any reason why a subcontractor should not be provided with a copy of the ledger for retention money?**

**8. Is the timing proposed for providing copies of the ledger reasonable? If not, why?**

### Penalties for trust accounts

Section 12A of the Act enables the Regulation to prescribe an offence for failure to comply with retention money trust account requirements punishable by a penalty not exceeding 1,000 penalty units. The proposed penalty amounts have been specifically designed to deter non-compliant conduct and to increase accountability in the management of retention monies.

The following maximum penalty units have been included in the proposed Regulation, reflecting the relative seriousness of each offence.

Clause	Penalty	Maximum penalty units for a corporation	Maximum penalty units in any other case
8(1)	Head contractor not holding money in trust account	1,000	200
8(2)	Head contractor not paying money into a trust account within 7 days	1,000	200
9	Head contractor not establishing a trust account or notifying Secretary within 14 days	1,000	200
10	Head contractor withdrawing money from a trust account	1,000	200

Clause	Penalty	Maximum penalty units for a corporation	Maximum penalty units in any other case
13	Head contractor failing to notify of an overdrawn trust account	1,000	200
14	Head contractor failing to notify of closure of trust account	1,000	200
16	Head contractor failing to retain trust account records	1,000	200

**9. Do you support the proposed maximum penalty units for these offences? If not, why?**

## Part 3 Miscellaneous

### Supporting statements

Under section 13(7) of the Act, it is an offence to serve a payment claim without the supporting statement. A supporting statement means a statement that is in the form approved by the Secretary and, without limitation, includes a declaration that any subcontractors have been paid all amounts that have become due and payable in relation to construction work. Currently, details relating to the supporting statement are set out under clause 19 of the current Regulation.

Clause 18 of the proposed Regulation has carried over clause 19(4) from the current Regulation only, which provides that the supporting statement requirement relates only to those subcontractors or suppliers directly engaged by the head contractor. The remainder of existing clause 19, which sets out the amount due and payable, will now be specified in the Secretary's approved form. Those filling in the form will need to take care when declaring that they have paid all amounts due and payable to ensure that they do not falsely declare information, which is an offence under the Act.

### Adjudicator eligibility

Authorised nominating authorities (**ANAs**) are responsible for receiving adjudication applications and appointing adjudicators for payment claim disputes. An ANA's function provides an important support and advisory service to parties in relation to the adjudication procedure under the Act.

Some stakeholders raised concerns about the function and effectiveness of ANAs during the NSW review of the Act. These concerns were echoed in the Murray Review. The Murray Review noted that most stakeholders believed that a minimum mandatory set of skills and experience would provide a benchmark for the quality expected of adjudicators and would support consistency in

their decision-making. To this end, the Murray Review recommended that minimum eligibility requirements for adjudicators should be specified in legislation.

One of the key reforms included in the Amendment Act empowered the Minister to make an enforceable Code of Practice to address concerns about ANAs. The Code of Practice, which is currently being developed, will outline and clarify expectations, responsibilities and obligations of ANAs when undertaking their function. A failure to comply with the Code will be an offence and grounds for withdrawing authorisation.

In September 2019, a draft Code of Practice (the **Code**) for ANAs was released for public consultation. The Code set out the required qualifications, expertise and experience for a person to be eligible to be an adjudicator in relation to a construction contract. The Murray Review acknowledged that leaving the training and accreditation of persons eligible to become adjudicators to ANAs was not conducive to producing the standard of competency expected by the industry.

At that time, stakeholders were given an opportunity to provide feedback on the Code, including the proposed qualifications, expertise and experience set out in the Code. Following consideration of submissions on the Code and in accordance with section 18(1)(b) of the Act, clause 19 of the proposed Regulation sets out the proposed qualifications and experience that adjudicators will be required to meet. These requirements have been further refined in response to stakeholder views on the qualifications and experience first proposed by the Code.

A person will be required to have one of the following:

- a degree or diploma in architecture, building surveying, quantity surveying, building and construction, construction management, engineering or law conferred by an Australian or foreign university or tertiary institution, with at least 5 years' experience in the administration and management of construction contracts or in the resolution of disputes in connection with construction contracts, or
- at least 10 years' experience in the management of construction contracts or in the resolution of disputes in connection with construction contracts.

In addition, under clause 19(2) of the proposed Regulation, a person would not be eligible to be an adjudicator if:

- the person has not completed the required continuing professional development (**CPD**); or
- a reasonable person would conclude that the person has an actual or perceived conflict of interest, or the person would not adjudicate impartially.

Under the current Regulation, ANAs monitor and manage adjudicator competency on a discretionary basis.

CPD is an important form of development that can be used to ensure adjudicators to stay up to date with new building requirements and standard practices across industry, maintain or improve skills, and better understand legislative responsibilities.

Under clause 19(4) of the proposed Regulation, all adjudicators will be expected to complete CPD requirements specified by the Secretary's guidelines (the **guidelines**). The CPD requirements have been included in the form of guidelines, rather than under the proposed Regulation, as they can be modified with greater flexibility and can be used more quickly to adapt to and reflect changes to industry practice. Upon commencement of the proposed Regulation, the guidelines will be published on the department's website.

The guidelines will set out the minimum necessary CPD points that must be met each year and the education and training activities that can be undertaken in order to achieve these points.

Under the proposed Regulation, ANAs will still be responsible for monitoring that the CPD requirements have been met. An adjudicator must maintain records of CPD completion and provide evidence to the ANA in order to maintain their eligibility as an adjudicator.

To help industry adjust to the new CPD requirements, a transitional provision has been included in the proposed Regulation meaning that CPD will only become mandatory from 1 September 2021.

The guidelines are provided as an attachment to the RIS for comment. Questions 10, 11 and 12 of this RIS seek feedback on the guidelines.

### **Renewal period for ANAs**

Clause 20 of the proposed Regulation will require the authorisation of nominated authorities to be renewed every 5 years. Existing authorisations will be in force for a period of 5 years from commencement of the proposed Regulation unless withdrawn by the Minister.

- 10. Are the proposed qualifications and experience appropriate for adjudicators? Why or why not?**
- 11. Should it be mandatory for all adjudicators to have specific qualifications and experience? If not, why?**
- 12. Do you agree with the number of CPD points that must be undertaken by an adjudicator? If not, why?**
- 13. Are the CPD education and training activities for adjudicators appropriate? If not, what types of CPD activities would be more appropriate?**
- 14. Do you agree with the proposed transitional period for CPD of 1 September 2021? If not, what is a more suitable transitional period?**
- 15. Is the 5-year period proposed for renewal of an ANAs authorisation suitable? If not, why?**

## **Repeal and savings**

The repeal date of the current Regulation is 1 September 2021. It is proposed to bring forward the commencement date of the proposed Regulation to 1 September 2020 to complete the package of reforms implementing the outcomes of the review of the Act. Commencing the reforms by 1 September 2020 also has the added benefit of removing the obligation on head contractors, who were required to operate a retention money trust account during the 2019/20 financial year, to report.

It is acknowledged that the proposed commencement date may impact industry by requiring a greater portion of industry to establish retention money trusts for contracts valued over \$10 million. Accordingly, the proposed Regulation provides a transitional period to allow industry to adapt to the new requirements and postpones the applicability of the \$10 million threshold requirement to contracts entered into on or after 1 January 2021.

The \$20 million threshold will continue to apply for construction contracts that are entered into on or after 1 May 2015 and on or before 31 December 2020. Practically, this means that any existing contracts or contracts entered into before 31 December 2020 with a value of \$10 million will not be required to establish a retention money trust account for the project. During this time, trust accounts will continue to be required for projects with a value of at least \$20 million.

**16. Is the date proposed for the reduction in project value suitable? If not, why?**

## Appendix 1 – Regulation making powers

Regulation making power in the Act	Clause in proposed Regulation
<p><b>Section 4(1) Definitions</b></p> <p>Permits the Regulation to expand the meaning of <i>exempt residential construction contract</i>.</p>	<p>Nil – not proposed to expand the meaning of the term.</p>
<p><b>Section 4(1) Definitions</b></p> <p>Permits the Regulation to expand the meaning of <i>recognised financial institution</i>.</p>	<p>Nil – not proposed to expand the meaning of the term.</p>
<p><b>Section 5(1)(g) Definition of “construction work”</b></p> <p>Permits the Regulation to expand or limit the meaning of <i>construction work</i>.</p>	<p>Nil – not proposed to expand or limit the meaning of the term.</p>
<p><b>Section 6(1)(c) Definition of “related goods and services”</b></p> <p>Permits the Regulation to expand or limit the meaning of <i>related goods and services</i>.</p>	<p>Nil – not proposed to expand or limit the meaning of the term.</p>
<p><b>Section 7(5) Application of Act</b></p> <p>Permits the Regulation to exempt any construction contract or class of construction contracts from the application of the Act.</p>	<p><b>Clause 4</b></p> <p>Excludes owner occupier construction contracts from the application of the Act.</p>
<p><b>Section 12A Trust account requirements for retention money</b></p> <p>Permits the Regulation to set out a framework for retaining and managing retention money and retention money trust accounts.</p>	<p><b>Clause 6</b></p> <p>Sets out the project value threshold for when retention money is to be held in trust (at least \$10 million) and a method for calculating the project value.</p> <p><b>Clause 8</b></p> <p>Creates obligations for a head contractor to hold retention money in a trust account.</p> <p><b>Clause 9</b></p>

Regulation making power in the Act	Clause in proposed Regulation
	<p>Prescribes the requirements for setting up a retention money trust account, including notification to the Secretary.</p> <p><b>Clause 10</b></p> <p>Prohibits the withdrawal of retention money from a trust account outside prescribed circumstances and outlines the methods for withdrawals.</p> <p><b>Clause 11</b></p> <p>Prescribes what can be done with interest earned on retention money trust accounts.</p> <p><b>Clause 12</b></p> <p>Prohibits the use of retention money for the purposes of paying a head contractor's debts.</p> <p><b>Clause 13</b></p> <p>Prescribes notification requirements in the event that a retention money trust account becomes overdrawn.</p> <p><b>Clause 14</b></p> <p>Requires a head contractor to notify the Secretary if a retention money trust account is closed</p> <p><b>Clause 15</b></p> <p>Provides protection for approved ADIs from liability and prevents claims against the trust money for liability of the head contractor to an ADI.</p> <p><b>Clause 16</b></p> <p>Sets out the record keeping requirements for a head contractor for retention money trust accounts.</p>



Regulation making power in the Act	Clause in proposed Regulation
<p><b>Section 18(1)(b) and(2)(b) Eligibility criteria for adjudicators</b></p> <p>Permits the Regulation to prescribe qualifications, expertise and experience for a person to be eligible to be an adjudicator in relation to a construction contract, and the circumstances in which a person is not eligible to be an adjudicator.</p>	<p><b>Clause 19</b></p> <p>Prescribes the eligibility requirements for an adjudicator, including the qualifications necessary to adjudicate construction contracts, and the circumstances in which a person is not eligible to adjudicate a construction contract.</p>
<p><b>Section 28(1) Nominating authorities</b></p> <p>Permits the Regulation to prescribe the circumstances under which the Minister may grant or withdraw a person’s authority to nominate an adjudicator for the purposes of the Act.</p>	<p><b>Clause 20</b></p> <p>Prescribes that a nominating authority’s authorisation is in force for a period of 5 years. It also provides that an existing authority will remain in force for a period of 5 years from commencement of the proposed Regulation, unless withdrawn sooner by the Minister.</p>
<p><b>Section 29(5)(b) Adjudicator’s fees</b></p> <p>Permits the Regulation to prescribe additional circumstances in which an adjudicator would be entitled to be paid fees and expenses.</p>	<p>Nil – no additional circumstances proposed.</p>
<p><b>Section 31(d1) Service of documents</b></p> <p>Permits the Regulation to prescribe additional methods to serve documents on a person.</p>	<p>Nil – no additional methods proposed.</p>
<p><b>Section 34B(2) &amp; (4) Penalty notices</b></p> <p>Permits the Regulation to prescribe penalty notice offences and the amount payable for each offence.</p>	<p><b>Schedule 1</b></p> <p>Sets out the penalty notice offences and the amount payable for each offence for an individual and corporation.</p>
<p><b>Section 34D(1) Liability of directors etc for specified offences by corporation—offences attracting executive liability</b></p> <p>Permits the Regulation to prescribe certain offences as executive liability offences.</p>	<p><b>Clause 7</b></p> <p>Prescribes clauses 8(1), 8(2), 10, 13, 14 and 16 as executive liability offences.</p>

Regulation making power in the Act	Clause in proposed Regulation
<p><b>Section 35 Regulations</b></p> <p>General power to make regulations for, or with respect to, any matter</p> <p>Permits the Regulation to exempt specified persons or matters, or specified classes of person or matters from any provisions of the Act.</p> <p>The Regulation may also prescribe information that must be provided to a subcontractor when entering into a construction contract and create offences with a penalty not exceeding 100 penalty units.</p>	<p>Nil – no additional powers proposed.</p>

## Appendix 2 – Summary of the proposed Regulation

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### **Part 1 Preliminary**

**Clauses 1 and 2** provide the name and date of commencement of the proposed Regulation.

**Clause 3** sets out definitions of terms used in the proposed Regulation.

**Clause 4** excludes owner occupier construction contracts from the operation of the Act.

### **Part 2 Trust accounts for retention money**

**Clause 5** sets out definitions of terms used in Part 2.

**Clause 6** sets out the project value threshold for when retention money is to be held in trust (at least \$10 million) and a method for calculating the project value.

**Clause 7** prescribes offences against clauses 8(1), 10, 13, 14, 16, 17(4) and 18 as executive liability offences.

**Clause 8** creates obligations for a head contractor to hold retention money in a trust account.

**Clause 9** prescribes the requirements for setting up a retention money trust account, including notification to the Secretary.

**Clause 10** prohibits the withdrawal of retention money from a trust account outside prescribed circumstances and outlines the methods for withdrawals.

**Clause 11** prescribes what can be done with interest earned on retention money trust accounts.

**Clause 12** prohibits the use of retention money for the purposes of paying a head contractor's debts.

**Clause 13** prescribes notification requirements in the event that a retention money trust account becomes overdrawn.

**Clause 14** requires a head contractor to notify the Secretary if a retention money trust account is closed.

**Clause 15** provides protection for approved ADIs from liability and prevents claims against the trust money for liability of the head contractor to an ADI.

**Clause 16** sets out the record keeping requirements for a head contractor for retention money trust accounts.

### **Part 3 Miscellaneous**

**Clause 17** prescribes bodies and persons to be a 'recognised financial institution'.

**Clause 18** clarifies the requirement for a head contractor to provide supporting statements only for subcontractors or suppliers directly engaged by the head contractor.

**Clause 19** prescribes the eligibility requirements for an adjudicator, including the qualifications necessary to adjudicate construction contracts, and the circumstances in which a person is not eligible to adjudicate a construction contract.

**Clause 20** prescribes that a nominating authority's authorisation is in force for a period of 5 years. It also provides that an existing authority will remain in force for a period of 5 years from commencement of the proposed Regulation, unless sooner withdrawn by the Minister.

**Clause 21** provides an exemption from the operation of Division 2A of the Act (related to claimant's rights against principal contractor) for a person in the capacity of principal contractor under an owner occupier construction contract.

**Clause 22** provides a repeal and savings provision to preserve any act, matter or thing that had effect immediately before the repeal of the current Regulation and a transitional period for Part 2 of the proposed Regulation.

**Schedule 1** sets out the penalty notice offences and the amount payable for each offence for an individual and corporation.

## Appendix 3 – List of stakeholders

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The following key stakeholders have been provided with a copy of the proposed Regulation and this RIS:

Adjudicate Today

Adjudication Forum

Australian Building & Construction Dispute Resolution Service

Australian Constructors Association

Australian Property Institute NSW

Australian Small Business & Family Enterprise Ombudsman (ASBFEO)

Australian Solutions Centre

Civil Contractors Federation

Expert Adjudication

Housing Industry Association

The Law Society of NSW

Master Builders Association

Masters Electricians Association

Master Plumbers Association

Multiplex

National Electrical and Communication Association

Office of the Small Business Commissioner

Property Council of NSW

Resolution Institute

Society of Construction Law Australia

Urban Development Institute of Australia

Urban Taskforce

## Appendix 4 – List of questions from the RIS

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4. Do you support a reduction in the retention money trust account threshold from \$20 million to \$10 million? Why or why not?	23
5. Are there any reasonable circumstances in which retention money could not be deposited into a trust account with 7 days?	23
6. Is the suggested timeframe of 7 days to deposit money into a trust account appropriate? If not, what is a more appropriate timeframe?	23
7. Is there any reason why a subcontractor should not be provided with a copy of the ledger for retention money?	24
8. Is the timing proposed for providing copies of the ledger reasonable? If not, why?	24
9. Do you support the proposed maximum penalty units for these offences? If not, why?	25
10. Are the proposed qualifications and experience appropriate for adjudicators? Why or why not?	28
11. Should it be mandatory for all adjudicators to have specific qualifications and experience? If not, why?	28
12. Do you agree with the number of CPD points that must be undertaken by an adjudicator? If not, why?	28
13. Are the CPD education and training activities for adjudicators appropriate? If not, what types of CPD activities would be more appropriate?	28
14. Do you agree with the proposed transitional period for CPD of 1 September 2021? If not, what is a more suitable transitional period?	28
15. Is the 5-year period proposed for renewal of an ANAs authorisation suitable? If not, why?	28

16. Is the date proposed for the reduction in project value suitable? If not, why?

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