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Constructive Notes®

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A Rolling Stone Gathers No Moss – the Slippery Path of Adjudication Applications

by Beau Mollinger, Solicitor and David Rodighiero, Partner

A recent decision in the New South Wales Supreme Court case of *John Holland Pty Ltd v Made Contracting Pty Ltd [2008] NSWSC 374* considers an applicant's ability to withdraw an adjudication application once it has been lodged under the *Building and Construction Industry Security of Payments Act* 1999 (NSW) ("BCISPA").

The facts

The plaintiff, John Holland, and Made Contracting, the first defendant entered into a contract where Made Contracting undertook architectural welding and fabrication and other works for the sum of $344,473 plus GST.

A payment claim by Made Contracting on 30 May 2007 was made pursuant to s 13 of the BCISPA. Some two weeks later the John Holland served a payment schedule pursuant to s 14 of the BCISPA proposing a scheduled amount of nil.

On **28 June 2007**, the final day allowable under the BCISPA, Made Contracting applied to John Holland for adjudication of the payment claim pursuant to s 17. Made Contracting's application on 28 June 2007 did not contain any submissions in respect of its application. Section 17(3) of the BCISPA states that an adjudication application:

> *"may contain such submissions relevant to the claim as the claimant chooses to include."*

On **29 June 2007** (one day *after* the application for adjudication) Made Contracting separately served John Holland with submissions in respect of the adjudication application. Because the submissions ought to have been included with or accompanied any adjudication application, service of the submissions was outside the prescribed time under s 17(3)(c) and s 17(5) of the BCISPA by **one day**.

On 3 July 2007 the Adjudicator (who was the second defendant in the case) communicated acceptance of the adjudication application. In its submissions in response John Holland, it contended that Made Contracting's submissions ought not be considered by the Adjudicator by reason of their lateness.

On 6 July 2007 the Adjudicator informed Made Contracting that as the submissions were late, it could proceed with the application without the benefit of the submissions, or choose to file again at a later date. Made Contracting subsequently sought to withdraw its application for adjudication.

Confusion followed between the parties as to the validity of the withdrawal. Having noted the withdrawal, the Adjudicator did not issue a determination and subsequently the time for provision of a determination under s 21(3) of the BCISPA lapsed. Made Contracting then formally attempted withdrawal under s 26 of the BCISPA. A short time thereafter Made Contracting filed a new application with fresh submissions.

The validity of this second application, and the Adjudicator's decision in favour of Made Contracting was in question at trial.

The court's decision

The court read Made Contracting's right to serve a fresh application and submissions strictly within the context of s 26(1), which provided two circumstances in which a claimant could withdraw an application, specifically:

(a) when a claimant fails to receive a notice of acceptance from the Adjudicator within four business days of application; and

(b) failure of an Adjudicator to issue determination under section 21(3).

The attempts at withdrawal

The court considered that the express provisions in s 26(1) excluded, by implication, a withdrawal in any other circumstances - including any time before the determination is mandated for delivery.

The Adjudicator had correctly rejected Made Contracting's informal withdrawal as a nullity because it did not fall within s 26(1)(a). However, Made Contracting's formal withdrawal was notified after the time for a s 21(3) determination had expired, without the Adjudicator issuing a determination. It was this that proved to be the key issue of contention in the case.

To be enlivened, s 26(1)(b) required the Adjudicator to "fail" to issue a determination. The court considered this to be synonymous

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Partrick Mead, Partner

with "does not". In this regard the court observed *"the Adjudicator is under a statutory duty to determine the application according to law within the time stipulated"*.

The Judge therefore held that early informal attempts to withdraw the application were invalid, however, a later formal attempt by Made Contracting would succeed because the precondition of s 26(1)(b) had been satisfied.

Estoppel

John Holland then submitted that Made Contracting had caused the Adjudicator to withhold any determination, and therefore represented a withdrawal *outside the operation of the BCISPA* which ought to prevent Made Contracting from relying on section 26(1)(b) to formally withdraw and reissue a fresh application. John Holland submitted that the previous invalid attempts to withdraw, and the Adjudicator's notice that it would make no determination had been sufficient to mislead John Holland that there was no further action required on its part and that the issue had been settled outside the BCISPA. John Holland further claimed that it was denied an opportunity to compel the Adjudicator to make a determination under the BCISPA.

This argument was rejected as the Adjudicator was still entitled under the BCISPA to deliver a determination and merely did not[1]. Additionally, John Holland's arguments were rejected because the Adjudicator's notice of a decision not to issue a determination did not give commentary on the validity of the purported informal withdrawal upon which the decision was based.

The court considered that the BCISPA alone prescribed the circumstances for an applicant's valid withdrawal and any attempt to draw upon a right outside the BCISPA to effect withdrawal would fail;. His Honour Justice Nicholas stated:

> *"In my opinion, it follows that, upon the appointment of an Adjudicator, a claimant who no longer wishes to pursue an adjudication application cannot oppose its determination."*

Fresh application – considering previously excluded submissions?

As Made Contracting's fresh application contained substantially the same submissions that were rejected from consideration under the former application, John Holland claimed that the fresh submissions had been improperly relied upon.

This was on the basis that the Adjudicator could only consider submissions "duly made" in support of the claim. Accordingly, it was submitted that any new application under s 26 of the BCISPA was confined to the same documentation as the previous application for adjudication – and in this case the relevant submissions were served out of time and therefore invalid.

The court took a dim view of this approach, and instead determined that a new application under s 26 of the BCISPA had the effect of extending any time period under s 17 of the BCISPA for serving submissions. Moreover, the court held that the submissions could be amended or replaced; an applicant was not confined in any way to the same subject matter of submissions either.

Conclusion

In conclusion, Made Contracting were successful in defending its fresh application and the Adjudicator's determination found in its favour. This case is an example of how the courts will strictly interpret the prescribed process of adjudication. It demonstrates that once a claim has been commenced by way of application, it may prove to be an unstoppable process – rolling only until a statutory default in the procedure or until a determination is made by the Adjudicator. For this reason it is important that a potential claimant considers very carefully both the timing and content of applications for adjudication under the BCISPA or any reciprocal and identical legislation in other state jurisdictions.

1. See s 21(5) of the BCISPA which states that an Adjudicator can make a determination notwithstanding a party's failure to provide submissions.

Appointment of Principal Contractors in Queensland – Does My Client Need One?

By Clayton Payne, Associate and Ebru Upcin, Solicitor

Laws in Queensland impose obligations on the end users of construction work. This can potentially create difficulties for both builders and their clients.

The *Workplace Health and Safety Act 1995* (Qld) (**the Act**) requires a client commissioning "Construction Work" to appoint a "Principle Contractor" to oversee such work for workplace health and safety purposes. This obligation attaches to all Construction Work, constituting a "Prescribed Activity"[1], exceeding an estimated final price of more than $80,000.

Construction Work has been given a new broader meaning under the Act and includes work to alter, repair, refurbish, disassemble or decommission and work connected with site preparation.

A Principal Contractor is generally appointed by the client. However, with respect to "Prescribed Construction Work", the Principal Contractor will be the person who is in control of that type of work.

Prescribed Construction Work includes appropriate work on a structure that is a single dwelling such as a detached house or one or more attached dwellings, each being a building separated by a fire-resisting wall. This includes a row house, terrace house, town house or villa unit and a non-habitable building, being a private garage, carport, shed or the like.

The term "maintenance" is however not included in the definition of Construction Work. According to departmental commentary concerning this legislation[2]

> *Repair is work to bring an existing structure back into service following a failure of the structure; or part of the structure or the structure reaching a state in which it is no longer fit for its intended purpose.*
>
> *Maintenance is work to prevent a structure reaching a point where "repair" is required. Maintenance may involve disassembly or decommissioning of the structure or part of the structure.*

Work to disassemble and decommission a structure is also contained within the definition of Construction Work.

The client will be taken to be the Principal Contractor should the client fail to appoint one. It is important to note that prior to the commencement of Construction Work, an appropriate form must be used by the client to appoint the Principal Contractor and a copy of the form must be given to the Principal Contractor and to the Chief Executive of Workplace Health and Safety Queensland.

The Act prohibits the client from appointing more than one Principal Contractor except when the client obtains the written approval of the Chief Executive.

However, should the client appoint two or more Principal Contractors for the Construction Work at the one time without the Chief Executive's written approval, then all Principal Contractor appointments will cease and the client will be taken to be the Principal Contractor until another Principal Contractor appointment is made.

Those appointed as Principal Contractors for Construction Work have broad statutory responsibilities including obligations to:

- prepare a written construction safety plan;
- prepare a relevant work statement;
- sight evidence that induction has been carried out with workers before the Construction Work starts; and
- erect signs.

Contractors appointed as Principal Contractors should be aware of their statutory obligations to ensure that there are appropriate systems and plans as well as relevant training regimes in place for each relevant workplace. Therefore:

- failure to appoint a Principal Contractor;
- failure to appoint a Principal Contractor using the correct form; and
- failure to provide a copy of the form to the Chief Executive,

may all lead to penalties under the Act.

The question as to how the calculation of $80,000 of Construction Work is arrived at under the Act is also liable to lead to difficulties. Some have suggested attempting to split each piece of work into component parts to avoid the work falling under relevant provisions of the Act. Such an approach would appear to be dangerous and potentially constitutes avoidance. In particular, the Act provides that "Estimated Final Price" is the aggregate of the overall final project price rather than the price of individual contracts. Therefore any situation giving rise to such an issue requires careful thought and expert advice.

[1] A "Prescribed Activity" includes certain demolition work and asbestos removal work.

[2] New workplace health and safety laws fact sheet, "*What is construction work under the new definition*?", Queensland Government, Department of Industrial Relations website.

Security of Payment for Suppliers

By Patrick Mead, Partner

In light of the current financial climate, it seemed timely to revisit an issue considered previously in *Constructive Notes*, that being the rights and remedies of a supplier to a building project which has other participants impacted by insolvency concerns.

A situation may arise where a supplier of building materials to a project finds itself owed funds by a contractor whose contract is terminated in consequence of solvency concerns and is in turn placed into administration.

The supplier of the building materials has often provided those materials to the contractor in accordance with its standard credit terms. The materials are subsequently incorporated into the works, often prior to payment of those materials to the supplier.

Not uncommonly, the supplier of those materials seeks to afford itself some protection for payment within its credit terms by including what is commonly known as a "Romalpa Clause". Such a clause will ordinarily state that the goods supplied remain the property of the supplier until payment in full is received and that until full payment is made the customer holds the goods as bailee. Such a clause often goes on further to provide that while holding the goods as bailee, a fiduciary relationship exists between the customer and supplier and that if the customer sells any of the goods, it does so as fiduciary agent of the supplier.

In such circumstances the question arises whether, by virtue of such a clause, the contractor will hold any funds received by it (by its administrators) in payment of any outstanding progress claims, on trust for the supplier.

Analysis

The description in the suppliers credit terms of the contractor as fiduciary agent of the supplier, suggests that the contractor is obliged to subordinate its own interests in a sale, and also supports an argument that the parties thereby intended that the supplier has the right to trace any proceeds of a sale by the contractor.[1]

The case of *Associated Alloys Pty Ltd v ACN 001 452 160 Pty Ltd (in liq) (formerly Metropolitan Engineering and Fabrications Pty Ltd)*,[2] demonstrates that in some cases it is legally possible for a Romalpa Clause in a contract for the sale of goods, to produce the consequence that the borrower holds such a part of the proceeds of a construction process utilising the seller's goods as it relates to the use of those goods, in trust for the seller and a trust of that kind, if effective, is not struck down as an unregistered charge void against an administrator under s 266(i) of the *Corporations Act* 2001 (Cth).

Whether that result is produced or not, principally turns upon the careful construction of the words used in the Romalpa Clause and the application of those words to the particular facts of the case.

In the Associated Alloys Pty Ltd case, the relevant provision of the Romalpa Clause provided:

> *"[5] in the event that the [buyer] uses the goods/product in some manufacturing or construction process of its own or some third party, the [buyer] shall hold such a part of the proceeds of such manufacturing or construction process as relates to the goods/product in trust for the [seller]. Such parts shall be deemed to equal in dollar terms the amount owing by the [buyer] to the [seller] at the time of the receipt of such proceeds*".

Whether such words are sufficient to impose upon the contractor, an obligation to hold any part of the proceeds it receives from the principal upon trust for the supplier may turn on a number of matters including the necessity for there to be a "sale" by the contractor of the kind referred to in the Romalpa Clause. Commonly the contract by which the contractor "on-sells" the building materials will not constitute a "sale" within the legal context of that word, but rather would be a contract for work and materials. This type of contract has been regularly distinguished from a sale.

On the other hand, while a simple resale by the contractor of building materials purchased from the supplier could result in the contractor holding the proceeds of sale as a "fiduciary agent", perhaps on trust for the supplier, it may be extremely difficult to attribute an intention to the parties that the contractor would hold any particular progress payment on such a trust. Similarly, a progress payment is likely to include one payment as the value of the work done (including materials supplied) over a period, rather than simply the price of the materials supplied.

Assuming a clause was otherwise effective to constitute the contractor as trustee of the proceeds, to construe the clause as extending beyond a "sale" to a contract by the contractor for the performance of work and associated

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supply of materials would either constitute the contractor as the trustee of the whole proceeds of the progress payment for a period in which some of the supplier's material was supplied, or would require an implication that only some part of the proceeds of the progress payment, in some way attributable to the supply of the supplier's material, was held on trust for the supplier.

Either of these constructions would involve the unintended consequence that the contractor would hold the entire payment on trust for the supplier in circumstances where there is no criterion for determining how much of a particular progress payment is to be held on trust.

It also seems inherently unlikely that any contractor would assume an obligation to keep all or any part of the proceeds of any progress payments separate from its own money to the detriment of its own cash flow, making it very difficult to infer the relevant intention in circumstances where the clause does not in terms provide for such a trust.

Conclusion

Even if the supplier were either a nominated supplier of the principal or, perhaps more relevantly, if the contractor had a right under its contract to separate payment with respect to on or off-site materials (which may encapsulate the supplier's goods), it seems that this would only impact on the outcome, if the effect of that arrangement was to constitute a "sale" of the goods. While ordinarily any payment for on or off-site materials would still be on account only (falling within the overall payment referable to the contract for work and materials), if it were that the contractor received a separate payment for off-site materials (pursuant to which property in those goods passed to the principal), it may be sufficient in this instance to constitute a sale in the relevant sense.

Only if such a circumstance were encountered, would there appear to be a sound basis to assert rights as a preferential creditor against the administrators of a contractor. In those circumstances, an undertaking could be sought from the administrator to set aside any funds recovered by the contractor from the principal referable to the supply of the supplier's goods, on trust for that supplier.

1. *BHP Steel Ltd v Robertson (Aust) Pty Ltd [2002]* NSW SC 336 per Barrett J at 9-11
2. [2000] HCA 25

News Flash!

Carter Newell's Construction & Engineering team was recently recognised as a **leading Brisbane practice** in *ALB Building and Construction Law State of the Market* article.

"*Carter Newell was another firm that received glowing praise from clients for its all-round abilities in the area and 'close attention to client care'.*

Patrick Mead *was particularly mentioned by clients and peers alike for his 'esoteric knowledge of the industry', with one prominent client noting he was the lawyer of choice on contractual issues.*

David Rodighiero *was noted for his strong skills with clients saying he was a 'leader in litigation matters*'.

ALB Building and construction law state of the market, ALB issue 6.8, pg 36 – 45, August 2008

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