

## Reinforcing Security of Payment in NSW

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Despite set backs in the Supreme Court, the NSW Government is firmly behind security of payment and has now strengthened security of payment for subcontractors by giving them the right to attach moneys in the hands of the head contractor's principal. What is being attacked is the practice by contractors of obtaining payment for work done by a subcontractor but not promptly passing on payment to the subcontractor. The practice is often referred to as 'using the subcontractor's money to finance the works'.

The *Building and Construction Industry Security of Payment Amendment Act 2010* (NSW) (the amending Act) commences on 28 February 2011 and applies to existing and future contracts. The amended Act will enable subcontractors to freeze money in the hands of the principal that is or will become payable to the head contractor. This article considers the implications for the three parties affected, namely, the claimant, the respondent and the principal.

Under the Act the person with whom the respondent contracts to provide work or materials is called 'the principal contractor' but in this paper the term 'principal' will be used.

### An example

The problem which the amendment addresses is best explained by an example. Assume that a subcontractor (the claimant) does \$10,000 worth of work for a head contractor (the respondent) and at the end of the month the subcontractor makes a progress claim. About the same time the respondent will make a progress claim against the respondent's principal for payment for that work. If, within 10 business days after being served with the claimant's payment claim, the respondent gives the claimant a payment schedule for less than the claimed amount, the claimant can immediately apply to an authorised nominating authority to have the payment claim adjudicated. At the same time as the claimant makes the adjudication application, the amendment enables the claimant to give a *payment withholding request* to the principal.

Upon receipt of the *payment withholding request*, the principal must retain \$10,000 from moneys due or subsequently becoming due from the principal to the respondent for work carried out by the claimant. If the claimant moves quickly, the claimant should be able to serve the *payment withholding request* before the principal has paid the respondent. When payment cycles are monthly, this should be easy. The effect is that the respondent will not be able to use the claimant's money for the respondent's own purposes.

### Background

A *payment withholding request* under s 26A of the *Building and Construction Industry Security of Payment Act 1999* NSW (the 'SOP Act') and an *attachment order* under s 14 of the *Contractors Debts Act 1997* NSW are almost identical in their effect. Both require a principal to withhold payment of money to the respondent.

The difference is that if the claimant elects to go to adjudication, the claimant serves a *payment withholding request* but if the claimant elects to go to court, the claimant asks the court for an *attachment order*. Before the amendment, the claimant could only freeze moneys in the hands of the principal if the claimant elected to go to court.

An *attachment order* under s 14 of the *Contractors Debts Act* and a *payment withholding request* under s 26A of the SOP Act only freeze moneys in the hands of the principal until the claimant's entitlement to the moneys is decided by a court. To obtain payment of those moneys from the principal the claimant must obtain a judgment and ask the court for a debt certificate under s 7 of the *Contractors Debts Act*.

Section 7(1A) of the *Contractors Debts Act* provides:

If an adjudication certificate within the meaning of the *Building and Construction Industry Security of Payment Act 1999* has been filed as a judgment for a debt in accordance with section 25 of that Act, the court may, by order made on the application by the person who filed the adjudication certificate, issue a debt certificate in respect of that debt under this section.

To obtain payment from the principal the claimant must serve on the principal a notice of claim in an approved form together with a copy of the debt certificate (s 6 of the *Contractors Debts Act*).

Section 17(1) of the *Contractors Debts Act* provides that proceedings under that Act cannot be taken more than 12 months after the debt becomes payable. In the case of an adjudication, it is not clear whether the debt becomes payable within the meaning of s 17(1) of the *Contractors Debts Act* on the due date for payment determined by the adjudicator or the relevant date under s 23 of the *Building and Construction Industry Security of Payment Act 1999* but this is unlikely to be a problem that will arise.

### **Ambit of the amendment**

The amending Act inserts sections 26A to 26F, section 34A and Schedule 2, Part 4 into the *Building and Construction Industry Security of Payment Act 1999* NSW ('the SOP Act'). The changes apply to existing adjudication applications as well as future adjudication applications.

A claimant may give the principal a *payment withholding request* at any time after lodging an adjudication application. However, the principal is not required by that *payment withholding request* to retain the money if 20 business days have elapsed since the principal was served with a copy of the adjudicator's determination of the payment claim to which that *payment withholding request* relates (s 26B(3)(d)). In counting the 20 business days, the date upon which a copy of the determination was served on the principal is not counted. The principal must allow 20 business days to pass and on the day after the 20<sup>th</sup> business day has expired, the principal is no longer required by that *payment withholding request* to retain any moneys.

Section 26B(5) provides that within 5 business days after the adjudicator's determination is served on the claimant (by the adjudicator) the claimant must serve a copy of the adjudicator's determination on the principal. The principal must not act on that. It is only for information. Even if the determination is that there is no progress payment due to the claimant, the principal must continue to withhold payment until 20

business days have elapsed after the principal is served with a copy of the determination (s 26B(3)(d)). It is always possible that within that period the claimant will commence another adjudication and serve another *payment withholding request*.

There is nothing to stop the respondent or the adjudicator from serving a copy of the determination on the principal. Time runs from service upon the principal irrespective of who effects service. There may be instances where the claimant has not paid the adjudicator and the determination has not been released. If the respondent believes that the adjudicated amount will be less than the retained amount, the respondent may pay the adjudicator in order to have the retained money released as soon as possible.

The reason why the principal must retain the moneys for 20 business days is to give the parties time to make applications to the appropriate court. Either party may seek orders from a court with respect to the adjudication determination. To actually have a right to recover moneys from the principal, the claimant must obtain a *debt certificate* from the court.

A *debt certificate* is a certificate issued by a court under s 7 of the *Contractors Debts Act 1997* NSW. The procedure is described at pp 223-225 of the Author's book *Adjudication in the Building Industry*, 3rd edn 2010 Federation Press, Sydney. The claimant serves the debt certificate on the principal and then from moneys retained, the principal must pay the claimant directly. If the principal has failed to retain the amount required by the *payment withholding request* the principal is liable to pay the claimant out of the principal's own moneys (s 11 of the *Contractors Debts Act* and s 26C of the SOP Act).

Sometimes a respondent obtains from the Supreme Court a declaration that an adjudicator's determination is void even though the adjudication application is valid. By the time that declaration is obtained, it will be too late for the claimant to withdraw the adjudication application (*Cardinal Project Services v Hanave* [2010] NSWSC 1367). Sometimes the Court will be far sighted enough to make it a condition of the declaration that the parties agree to an extension of time for the making of an adjudication determination but often this is not the case. Then there could be a valid adjudication application but no possibility of there ever being an adjudication determination.

In that event, if the respondent does not obtain an appropriate order from the Court, the principal's obligation to retain money continues (see s 26B(3) of the SOP Act). The limitation period in s 17 of the *Contractors Debts Act* does not apply and there is no limitation under the SOP Act on how long the principal must retain the money. This appears to be a drafting oversight. If the principal does pay it to the respondent or uses it to discharge an obligation of the respondent to the principal, the claimant can sue the principal (s 26C(1) of the SOP Act). It seems that under the *Limitation Act 1969* NSW, the right to sue the principal may last for six years.

Consequently, when a respondent seeks a decision from the Supreme Court declaring an adjudication determination void the respondent should ensure that an appropriate order is made with respect to any *payment withholding request* that the claimant may have served or might even thereafter serve on the respondent with respect to the adjudication application. There is no requirement that a copy of a *payment withholding request* be served on the respondent. Consequently, at the time of the Court makes the declaration the respondent might not even be aware that there is a

*payment withholding request*. Even after the adjudicator's determination is declared void the claimant may serve a *payment withholding request* on the principal.

It seems that where the principal is obliged to retain money pursuant to a payment withholding request and the respondent seeks a declaration from the Supreme Court as to the validity of the adjudicator's determination, it will sometimes be necessary for the respondent to join the principal in the proceedings. Presumably, the principal would file a submitting appearance. The additional expense might be avoided if the claimant agrees with the respondent that should the Court declare the determination void, the claimant will forthwith notify the principal that the claimant no longer requires the principal to withhold moneys pursuant to the *payment withholding request*.

In instances where the Court decides that the adjudication application was not valid (eg *Chase Oyster Bar v Hamo Industries* [2010] NSWCA 190), it follows that any *payment withholding request* based upon the adjudication application is also void. For the principal's protection, the principal might consider inserting into contracts the special conditions described below.

Sometimes the claimant will not know if there is a principal or who the principal is. Under s 26E of the Act the claimant may ask the adjudicator to request the respondent to provide information to the claimant as to the identity and contact details of the principal.

The Act does not prescribe a time for the supply by the respondent of the information. The adjudicator should state a time. If the claimant thinks that there may be more than one principal, the claimant can serve a *payment withholding request* on each person that the claimant believes is a principal.

The form of a *payment withholding request* is to be approved by the Director-General of the Department of Services, Technology and Administration (s 26A(2)). At the time of writing the Director-General has yet to approve the form of the *payment withholding request*. When the form is approved, all authorised nominating authorities will be informed.

Section 26A(3) of the Act provides that a *payment withholding request* must include a statement in writing by the claimant in the form of a statutory declaration declaring that the claimant genuinely believes that the amount of money claimed is owed by the respondent to the claimant. The claimant does not have to believe that there is money owed by the principal.

### **Obligations on a principal**

The 'principal contractor' (called 'the principal' in this paper and in the *Contractors Debts Act*) is defined in s 26A(4) of the SOP Act. The principal is the person, if any, one step up the contract chain from the respondent. If the head contractor to the Government, an owner or developer is the respondent in an adjudication application, the Government, the owner or the developer is the principal. If a subcontractor to the head contractor is a respondent in an adjudication application, the head contractor is the principal.

If served with a payment withholding request, the principal must act quickly to stop all payments to the respondent for work carried out or materials supplied by the

respondent until the principal can ascertain how much of those payments are for work or materials that the respondent engaged the claimant to carry out.

Out of money that is or subsequently becomes payable by the principal to the respondent, the principal must withhold sufficient to cover the amount claimed in the payment claim. There are some qualifications.

There are three ceilings on the amount to be retained. The principal is obliged to retain the smallest of the following:

- (A) the amount claimed in the payment claim the subject of the adjudication application, less any part payment made, s 26B(4);
- (B) the amount owed, or which subsequently becomes payable, by the principal to the respondent when or after the *payment withholding request* is served on the principal, s 26B(1); or
- (C) the amount that is or becomes payable by the principal to the respondent for or incidental to the work or materials that the respondent engaged the claimant to carry out or supply, s 26B(2).

A claimant may claim any amount but the amount which the principal must retain is only the amount that is payable by the principal to the respondent for the work or materials supplied by the claimant. For example, under the subcontract the claimant may claim \$1m for certain piling work. This is amount (A). Under the head contract the amount payable by the principal contractor to the respondent for the piling work may be only \$100,000. This is the amount (C). The principal is only required to withhold payment of \$100,000 even though the principal owes the respondent \$500,000. This is the amount (B). The amount by which (B) exceeds (C) is for work other than the work or materials carried out or supplied by the claimant. It may be for work carried out by other subcontractors to the respondent.

The obligation to retain money does not extend to all money payable by the principal to the respondent. It does not apply to money payable to the respondent for work carried out or materials supplied by subcontractors other than the claimant. The obligation applies not only to payment for the work indicated in the payment claim which is the subject of the adjudication. It also applies to payment for any other work carried out or materials supplied by the claimant under the subcontract. The application of the Act to refund by the principal of retention moneys and security deposits may present problems.

Where the respondent has a number of subcontractors working on a project, it might not be easy to ascertain how much of a progress payment or final payment relates to work or materials that the respondent engaged the claimant to carry out or supply. The principal will have to examine each valuation of the respondent's work (for the purpose of a progress or final payment) to see whether the valuation is of:

work carried out or materials supplied by the respondent to the principal contractor as part of or incidental to the work or materials that the respondent engaged the claimant to carry out or supply. (s 26B(2))

The money which is subject to the *payment withholding request* is not only the amount which represents the value of that work but 'money that is or becomes

payable ... for work' (s 26B(2)). That could include extra payable for delay, variations and, perhaps, damages.

Compare s 14(4) of the *Contractors Debts Act*. Under that section the principal who is served with an *attachment order* must withhold payment from any money that is or may become payable by the principal to the respondent under the contract concerned, not simply money for the particular work of the claimant.

Assume that on Project X the principal contractor engaged the respondent to construct scaffolding and on Project Y, under a separate construction contract, the principal also engaged the respondent to provide scaffolding. Assume that for each project the respondent under a separate construction contract engaged the claimant as a subcontractor to provide the scaffolding. If the claimant makes an adjudication application in respect of the subcontract for Project X, can the payment withholding request apply to moneys owed by the principal contractor in respect of Project Y as well as Project X?

The answer appears to be 'No'. The payment claim and adjudication will only be in respect of one of the subcontracts. Section 26B(2) provides:

The amount is only required to be retained out of money that is or becomes payable by the principal contractor to the respondent for work carried out or materials supplied by the respondent to the principal contractor as part of or incidental to the work or materials that the respondent engaged the claimant to carry out or supply.

Note the word 'incidental'. Assume that the claimant supplies bricks to the respondent and the payment claim is for \$1,000 for the value of the bricks. Assume that the amount payable by the principal to the respondent for the bricks is \$1,100. The extra \$100 represents the respondent's entitlement for profit and attendance. Assume that at the time of receipt of the *payment withholding request* (for \$1,000) the principal has paid the respondent \$500 and the principal owes the respondent \$600. It seems that the respondent must retain the \$600 even if \$100 of that could be said to be the respondent's entitlement for profit and overheads.

Now assume that the respondent's work involves building a house with the bricks. Assume that there are many subcontractors and the contract price is a lump sum. Progress payments by the principal to the respondent are payments on account of the lump sum price. It will not be possible to identify any particular amount that is payable by the principal to the respondent for the bricks. But, ultimately, part of the contract price for the house will represent money that is payable by the principal to the respondent for the bricks supplied by the claimant. In that situation it seems that the principal must withhold payment to the respondent of \$1,000.

Without the consent of the respondent or a notice from the claimant attaching a debt certificate under s 7 of the *Contractor's Debts Act 1997* the principal must not pay any amount to the claimant. If the principal has received *attachment notices* from several claimants then s 10 of the *Contractors Debts Act* deals with priorities. However, there is no similar provision in the SOP Act. If the principal receives a demand (for the money retained) from a receiver or an assignee of the respondent, then the principal should obtain legal advice. It could be that the amount was not due to the respondent at the time of receipt of the *payment withholding request* but was

due to the receiver or assignee. However, any right acquired by a receiver or assignee after the principal receives the *payment withholding request* would not appear to extinguish the obligation on the principal to continue to withhold payment until one of the events listed in s 26B(3) occurs.

If, before issue by the court of a debt certificate under s 7 of the *Contractors Debts Act 1997*, the respondent is placed in liquidation or made bankrupt, the claimant cannot obtain a debt certificate without special leave of the court. Commonwealth legislation, rather than the *Contractor's Debts Act 1997* and the *Building and Construction Industry Security of Payment Act 1999*, then applies to moneys withheld. If, while withholding money pursuant to a *payment withholding request*, the principal receives an attachment order (a garnishee order) from another creditor of the respondent, the principal would not be able to pay the creditor out of the moneys which the principal is required to withhold.

Sometimes the payment claim the subject of the adjudication applications is in respect of particular work, for example, particular variations alleged to be additional work, which is not expressly covered in the contract between the respondent and the principal. Must the principal withhold payment for work expressly covered by the contract between the principal and the respondent carried out by the claimant when the work the subject of the payment claim is additional work albeit related to the work expressly covered?

The answer to this question appears to be 'Yes'. Similarly, if the payment claim is for delay costs or damages, it seems that the *payment withholding request* can apply to payments by the principal for work or materials (provided by the respondent to the principal that the respondent engaged the claimant to supply) even though the respondent makes no claim against the principal for delay or damages.

If after being served with a *payment withholding request*, the principal is uncertain whether an amount due from the principal to the respondent should be paid to the respondent or be withheld, the principal should seek the opinion of the respondent and, if there is a difference of opinion, obtain legal advice. Of the two options, paying or withholding, the second involves less risk for the principal. If the principal wrongly withholds payment, the principal will probably be liable to pay interest to the respondent but if the principal pays the amount to the respondent, the principal could be liable to the claimant for the amount and possibly interest. Section 26C of the Act provides:

If the principal contractor discharges the principal contractor's obligation to pay money owed under a contract to the respondent in contravention of a requirement under this Division to retain the money, the principal contractor becomes jointly and severally liable with the respondent in respect of the debt owed by the respondent to the claimant (but only to the extent of the amount of money to which the contravention relates).

Despite the limitation in brackets, if the principal fails to pay the claimant the amount which the principal should have paid the claimant on receipt of the debt certificate, the principal could not be liable to the claimant for interest for late payment. The liability under s 26C arises without the need for a debt certificate under s 7 of the *Contractors Debts Act*.

If an amount becomes payable by the principal to the respondent and it must be retained pursuant to a *payment withholding request*, the principal cannot discharge its obligation to the respondent by setting off an amount that subsequently becomes due from the respondent to the principal (s 26C(1)). For example, if at 30 June the respondent is entitled to a progress payment from the principal of \$10,000 and the principal receives a *payment withholding request* for an amount of \$10,000 or more, the principal must retain the \$10,000. If subsequently, the respondent's work was found to be defective and only worth \$1,000, the principal must still retain the \$10,000.

There is no obligation on the principal to deposit in a trust account the money withheld. However, for accounting purposes, the principal should separately show the money withheld.

Even if in the next progress valuation the work is valued at \$1,000 or, because the respondent is liable to the principal for liquidated damages for delay, the next progress certificate shows that the respondent owes the principal money (and the principal does not owe the respondent any money), or the contract has been terminated by the principal on account of the respondent's breach of contract, it seems that when the respondent receives a notice of claim and debt certificate for \$10,000 under s 6 of the *Contractors Debts Act*, the principal must pay the \$10,000 to the claimant.

It seems that for the principal there is one only way around the problem. That would be for the principal to obtain a judgment against the respondent. When the principal obtains such a judgment, it seems that the \$10,000 is no longer an amount which is owed by the principal to the respondent. The previous debt merges in the judgment. It seems that the amount payable by the principal pursuant to the notice of claim and debt certificate under s 6 of the *Contractor's Debts Act* could not require the principal to pay the claimant any amount exceeding the amount owed by the principal to the respondent under the judgment.

Set off by the principal is best explained by examples from two different progress payment provisions in standard contracts. AS 2124-1986 General Conditions in clause 42.2 provides:

The amount due to the Contractor at the time for a claim for payment shall be the value of the work carried out by the Contractor in performance of the Contract to that time together with any moneys due to the Contractor under any other provision of the Contract or for breach of contract less –

- (a) amounts already paid under the Contract;
- (b) amounts which the Principal is entitled to deduct under Clause 42.3 or 42.10.

Clause 42.3 refers to retention moneys and clause 42.10 provides that the principal can deduct from moneys otherwise due to the contractor (the respondent) any moneys due from the contractor to the principal. The amount payable by the principal to the respondent is an amount calculated after making any set off.

Clause 42.1 of AS2124-1992 provides that the principal must pay the contractor the amount shown in the Superintendent's payment certificate. The amount payable is the

certified amount. So much of that amount as does not exceed any of the three ceilings described above, must be retained by the principal. The ceiling is not reduced by set offs (for example for defective work or liquidated damages for delay) subsequently claimed by the principal against the amount shown in the payment certificate. Effectively, the claimant has a priority over claims by the principal against the respondent arising after service of the *payment withholding request*.

If a person is served with a *payment withholding request* and the person is not (or is no longer) a Contractor in relation to the payment claim, the person must give written notice to the claimant within 10 business days after receiving the *payment withholding request* (s 26A(5)).

A person may have once been but is no longer a principal contractor (as defined in s 26A(4)) because, before receiving the *payment withholding request*, the person has paid all moneys due from that person to the respondent and no further moneys will become due. If a person is a principal at the time when the *payment withholding request* was served on the person, the person does not cease to be a principal because the person no longer owes money to the respondent because, for example, the person has paid the respondent or some other person at the direction of the respondent or has set off the debt against moneys owed by the respondent to the principal (s 26C(1)).

Section 26C deals with where the principal discharges the principal's obligation to pay money owed under the contract to the respondent. Clause 26C would not apply where the obligation is discharged by operation of law independently of any action of the principal, for example, by an order of a court or a lawful demand of a liquidator (of the respondent) or the Commissioner of Taxation (to pay the amount to the Commissioner).

### **Application to residential building work**

Section 7(2)(b) of the SOP Act provides that the SOP Act does not apply to a construction contract for the carrying out of residential building work (within the meaning of the *Home Building Act 1989* (NSW)) on such part of any premises as the party for whom the work is carried out resides in or proposes to reside in. If the contract between the principal and the respondent is a construction contract to which the Act does not apply by reason of s 7(2)(b), then the claimant cannot validly serve a payment withholding notice on the Principal. That Principal is exempt from the Act (*Building and Construction Industry Security of Payment Amendment Regulation 2011* (NSW)).

### **Penalties**

The amending Act introduces five penalties namely:

- (1) on any person who, within 10 business days after receiving a *payment withholding request*, fails to notify the claimant if the person is not (or is no longer) a principal for the claim (s 26A(5));
- (2) on the claimant if, within 5 business days after the adjudication determination is served on the claimant, the claimant fails to serve a copy of the adjudication determination on the principal (26B(5));
- (3) on the claimant if the adjudication application is withdrawn and the claimant fails to give written notice of withdrawal to the principal (who has been

- served with a *payment withholding request*) within 5 business days after it is withdrawn (s 26D(3));
- (4) on the respondent if, following a direction by the adjudicator, the respondent fails to provide information to the claimant as to the identity and contact details of any person who is a Contractor (s 26E(2)); and
  - (5) on the respondent if, in response to the adjudicator's direction, the respondent provides information which the respondent knows is false or misleading (s 26E(3)).

The maximum penalty for each of (1) and (2) is 5 penalty points. For each of (3) to (5) it is 10 penalty points. A penalty point is currently \$110 (s 17 of the *Crimes (Sentencing Procedure) Act 1999* (NSW)). It is extremely rare for a prosecution to be brought for these types of offences. A much more effective method of ensuring compliance would be to give the party who should have received the notice or information some monetary entitlement.

If the claimant withdraws an adjudication application under s 26(2)(a) of the Act and makes a new adjudication application under s 26(2)(b) the claimant must give any principal (who has been served with a *payment withholding request*) notice of the withdrawal (s 26D(3)). A *payment withholding request* based upon the original adjudication application (now withdrawn) would not apply to the new adjudication application. The claimant would have to serve a new *payment withholding request*. This should be done with the notice to the principal of withdrawal of the original adjudication application so that there is no day in between when the principal is not obliged to withhold payment.

### **Special Conditions**

The *Contractors Debts Act 1997* s 18 and the *Building and Construction Industry Security of Payment Act 1999* s 34 prohibit contracting out but a party who may become a principal (eg the Government, an owner, a developer or a head contractor) could include in its contracts provisions such as:

If [the principal] receives a *payment withholding request* under the *Building and Construction Industry Security of Payment Act 1999* (or a notice purporting to be a *payment withholding request*) requesting the principal to withhold payment to the [respondent]:

- (a) [the principal] will be entitled to obtain legal advice as to its obligations with respect to withholding payment;
- (b) [the respondent] will on demand reimburse [the principal] for the reasonable costs of obtaining that advice and implementing it;
- (c) if, in good faith, [the principal] withholds a payment to [the respondent] on account of a *payment withholding request* or a purported notice, [the respondent] will not hold [the principal] liable for damages or interest even if it should transpire that [the principal] was not entitled to retain the amount or to retain it for the whole period that [the principal] retained it;
- (d) if [the principal] is joined in any legal proceedings between [the respondent] and a person who serves a *payment withholding request* on [the principal] the respondent will on demand

- reimburse [the principal] for the reasonable costs of obtaining legal advice and participating in the proceedings;
- (e) moneys withheld on account of the *payment withholding request* or purported notice will not be regarded as retention moneys or security but for the purpose of calculating the [principal's entitlement to retention moneys and security, the amounts withheld will be included in the calculation of the sum upon which retention moneys and security are calculated.

Section 26D of the SOP Act provides some protection for the principal against claims by the respondent. While the statutory obligation to retain money continues, it acts as a defence to a claim by the respondent against the principal for the money (s 26D(1)). Any period during which the principal retains money pursuant to the obligation is not to be taken into account for the purposes of reckoning the period for payment by the principal of the respondent.

The respondent could not claim interest from the principal for the period during which the principal lawfully withheld payment. If the respondent made a claim under the *Building and Construction Industry Security of Payment Act 1999* against the principal, in calculating the due date for payment of the amount withheld, time for payment would not run during the period that the principal withheld payment in compliance with a valid *payment withholding request*.

There are instances where the Supreme Court has declared an adjudication application invalid. It is possible that a principal receives what purports to be a *payment withholding request* but the notice is void because the adjudication application is void. Even if, acting in good faith, the principal has withheld payment on the basis of a void *payment withholding request*, the principal could have a liability to the respondent. The principal's withholding of payment may be serious breach of contract. In that situation the Act provides no protection for the principal. Therefore, a party who may be a principal should consider a special condition to protect the party (see above).

There may be instances where the claimant and the respondent are engaged in litigation (eg over the validity of an adjudication application or a *payment withholding request*) and the principal is joined as a party. The principal would probably file a submitting appearance. See 'submitting appearance' in the index to the Author's book *Adjudication in the Building Industry*, 3rd edn. Nevertheless, the principal will probably incur legal costs. A special condition (including an indemnity for the legal costs) may prove useful (see above).

The principal should only make a payment to the claimant with the consent of the respondent or pursuant to a notice under s 6 of the *Contractors Debts Act 1997* attaching a copy of debt certificate from a court. If a payment is made pursuant to the court's debt certificate, the *Contractors Debts Act* provides protection for the principal.

When a contract between the principal and the respondent provides that the principal can retain moneys (retention moneys) from payments to the respondent, it may be prudent to have an express provision that moneys retained in accordance with a statutory requirements are not to be considered to be part of the retention moneys which the principal is entitled to retain (see above).

## **Termination of the obligation to retain moneys**

The principal's obligation to withhold money can be discharged (in whole or in part) if the respondent pays an amount to the claimant or, with the authority of the respondent, the principal pays an amount to the claimant (ss 26B(4) and 26B(3)(a)).

The principal is entitled to rely in good faith on a statement in a statutory declaration by the respondent that a specified amount claimed has been paid to the claimant (s 26D(4)). A prudent principal would check with the claimant before releasing any amount to the respondent.

The principal's obligation to withhold money is discharged if the adjudication application is withdrawn (s 26B(3)). The term 'withdrawn' is not defined. Withdrawal of a payment claim or the *payment withholding request* is not the same as withdrawal of an adjudication application. Section 26 of the SOP Act deals with withdrawal of an adjudication application. Once an adjudication application has been made, the claimant cannot withdraw it except under s 26. Once the application has been made, the respondent has an entitlement to have it adjudicated.

Section 26D(4) provides that the principal is entitled to rely in good faith on a statement in a statutory declaration by the respondent that an adjudication application has been withdrawn. Bearing in mind the very limited circumstances in which an adjudication application can be withdrawn (s 26), the principal may be well advised not to simply rely upon the statutory declaration but to check with the claimant or the authorised nominating authority.

However, the claimant can at any time notify the principal that the claimant withdraws the *payment withholding request*. At statement by the claimant to the principal that the claimant withdraws the payment claim would effectively be notice that the claimant withdraws the *payment withholding request*. However, the prudent principal would seek an express statement, preferably in writing from the claimant, that the claimant withdraws the *payment withholding request*.

If the claimant obtains a debt certificate from a court and gives the principal a notice of claim, the principal must comply with the notice and pay the amount required by the court's order. The obligation to retain money under the *Building and Construction Industry Security of Payment Act 1999* (s 26B(3)(c)) ceases upon receipt of the notice of claim under the *Contractors Debts Act 1997* but is replaced by the obligation under the *Contractors Debts Act*.

The amount payable in accordance with the notice of claim under s 6 of the *Contractors Debts Act 1997* may be more or less than the retained amount but the amount is nevertheless only payable out of moneys due from the principal to the respondent. Where the obligation to retain money under the *Building and Construction Industry Security of Payment Act 1999* is limited by the ceiling (C) referred to above, the amount payable pursuant to the debt certificate is payable out of any money owed by the principal to the respondent under the contract between the principal and the respondent. That is the ceiling (B) referred to above.

If the obligation to retain money has not earlier ceased for one of the reasons covered, then it ceases when 20 business days have elapsed since a copy of the adjudicator's

determination was served on the principal. How the 20 business days is calculated is covered above.