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A CASE STUDY UNDER THE NEW CONSTRUCTION INDUSTRY SECURITY OF PAYMENT REGULATIONS – JOHN AND SARAH

Facts

John and Sarah have decided to build their own home in New South Wales. They enter into a contract with ABC Building Pty Ltd, a licensed home builder. The contract is a standard form HIA Residential Building Contract.

The construction price is $750,000.00, with the progress payments defined to be:

Stage	Percentage	Amount
Deposit Non-refundable	5%	$37,500.00
Floor Slab Complete Floor slab poured	15%	$112,500.00
Roof Frame Complete Wall and roof framing complete	20%	$150,000.00
Enclosed Complete All frames straightened. Windows temporarily nailed off. Electrical, gas and plumbing rough in complete. Front and back entries are able to be enclosed. Majority of weatherproofing elements are in place	25%	$187,500.00
Fixings Complete All internal architraves, skirtings, doors, cupboards and detailed joinery installed. Plasterboard finished, sanded and cornices fixed	25%	$187,500.00
Practical Completion The building works are complete except for minor omissions and defects that do not prevent the building works from being reasonably capable of being used for their usual purpose	10%	$75,000.00
TOTAL	**100%**	**$750,000.00**

John and Sarah have contributed the deposit from their savings, with the balance of the construction costs being provided by a bank under a mortgage.

Construction commences, and the Floor Slab, Roof Frame and Enclose Complete stages are all completed without issue, and ABC Building are paid from the bank.

At the conclusion of the Fixings Complete stage, ABC Building issue their progress claim for Fixings Complete in the amount of $187,500.00 and also claim for $54,000.00 worth of "variations", itemised as:

- rock encountered prior to pouring floor slab – $25,000.00
- client selections and finishes changed at request of client – $8,000.00
- changes to electrical design – $12,000.00
- sub total - $45,000.00
- Builders margin @ 20% - $9,000.00
- TOTAL - $54,000.00.

The progress claim is a valid payment claim within the meaning of the *Building and Construction Industry Security of Payment Act* 1999 (NSW) ("**Act**").

John and Sarah arrange a meeting with ABC Building to discuss the variations, but do not otherwise provide a response in writing to the progress claim, within 10 business days of receipt.

ABC Building's rights under the Act

As John and Sarah have not provided a 'payment schedule' within the meaning of the Act, ABC Building can:

1. elect to proceed to adjudication. Before they may commence this step, they must issue John and Sarah with a notice under section 17(2) of the Act advising that they have a further 5 business days to issue a payment schedule, or the matter will be taken to adjudication; or
2. may sue in Court, as the failure to issue a payment schedule operates as an admission on behalf of John and Sarah for the full value of the progress claim (being the full value claimed for both fixed stage and the variations); and
3. may suspend work upon 2 business days' notice to John and Sarah (section 27 of the Act).

ABC Building elect to suspend work and sue in Court.

John and Sarah's options

The Security of Payment Scheme is a "pay now, argue later" scheme.

Under section 15(1)(a) of the Act, because they did not issue a payment schedule, John and Sarah became liable to pay the whole of the claimed amount on the due date for payment.

Now that ABC Building has sued John and Sarah in Court, section 15(4)(b) of the Act provides that John and Sarah cannot bring any cross-claim and they cannot raise any defence in relation to matters arising under the contract.

Examples of 'defences arising under the contract' would include that ABC Building did not obtain confirmation in writing of their variations (as they are contractually obligated to do), an argument that the amounts claimed for the variations are exorbitant or that the quantities claimed are inaccurate.

In short, other than successfully proving ABC Building engaged in misleading and deceptive conduct, John and Sarah's only option is to pay the full amount claimed, and if they dispute that the money is actually owing, after making payment they can sue ABC Building for restitution.

What happens if John and Sarah can't pay?

Under section 27 of the Act, ABC Building are entitled to suspend work and are held harmless from any damages incurred by John and Sarah as a result of that suspension. That will include things like rent, or liquidated damages.

If John and Sarah can't pay, they have no available rights at law to force the construction to recommence, or to avoid their obligation to pay the claimed amount in full.

If John and Sarah fail to pay, ABC Building are within their rights to commence enforcement action, up to and including having a trustee in bankruptcy appointed, who would presumably sell the property with the result being the bank would be paid in full (as a secured creditor) and ABC Building would be paid in full, and John and Sarah would be left financially destitute.