

Security of Payments in Victoria - Its use as an effective payment tool in 2010.

A Summary of the Paper presented in the December 2009 BDPS News

Toby Shnookal

In the December 2009 BDPS News is a paper I wrote entitled “*The Building and Construction Industry Security of Payment Act 2002.*” That paper is mostly an introduction to adjudication for legal practitioners in Victoria, and to assist them to use the Act. In particular, it provided encouragement to use the Act as a result of the time lines it contains – something this paper will return to from the opposite perspective under the heading of Natural Justice. Also, this paper will discuss statutory demands and how they are being treated in the Courts when delivered on the back of an adjudication. That area of law would discourage an applicant from using the Act. So this paper provides a bit of balance with my first.

Another major theme to the first paper was something of a lament that the entitlement under the Act to a payment claim is not the same thing as the entitlement under the contract to a payment claim. The Act only enables an adjudicator to consider part of the contractual situation as it exists between the parties to the contract – excluded amounts cannot be considered. Thus, excluded amounts, which include liquidated damages and some variations, are all essentially put on the side of the shelf to be assessed later.¹ So, for example, in a job that runs very late the proprietor has to pay up the contract sum and then try and claw back liquidated damages later.² The main reason that I suggest this is an unfortunate arrangement, and in my first paper I contrasted this arrangement with the much better system in the UK (under s 109 of the *Housing Grants, Construction and Regeneration Act* which allows the entire dispute to be adjudicated) is to do with the overall role adjudication plays in settling disputes.

What I mean by this is that typically a party that starts an adjudication doesn't want to just be paid its progress payment, it wants to resolve the entire dispute. We all know adjudication is an interim decision, but we also know from experience that adjudication usually leads to a negotiated settlement of the entire dispute. What I argue in my first paper is that adjudication is a form of alternative dispute resolution, not just a statutory right to a payment claim. I argue that limiting what can be adjudicated is a fetter on adjudication as an ADR process.

Despite my concern that adjudication in Victoria cannot decide the entire dispute, I do want to debunk one myth. That is that the Victorian Act does not cover variations. In my experience most variations that are in dispute are generally within the operation of the Act in Victoria. I say that because my experience has been that most disputes are about *valuing* variation work. In that case, if the contract specifies the method of valuing variations, as they invariably do, then those variations are claimable as class

¹ See *Brady Constructions Pty v Everest Project Developments Pty Ltd* [2009] VSC 622 for a recent example of the problems that arise. Everest had to pay Brady an adjudicated amount, notwithstanding the Superintendent had certified Brady owed Everest taking liquidated damages into account. However Everest could not then recover liquidated damages on an interim basis on the Superintendent's determination (by calling on the bank guarantee) because its financial position was such that the Court was concerned that if it was permitted to cash the guarantee, it may not be able to repay the cash obtained.

² *Brady Constructions Pty v Everest Project Developments Pty Ltd*, *ibid*

one variations.³ All the rest can sum to 10% of the contract price before they are excluded. The Act is complicated in the way it is written, but it doesn't exclude all that many variation claims ordinarily.

So these were the themes in my first paper. The Act is a not particularly good form of ADR and could be much better, and there is a misconception that the Act is not that useful because of the way it deals with variations. Nevertheless it does work to resolve most disputes and should be used.

So this paper is about 4 new things. First, it will provide a quick update on the numbers of adjudications under the Victorian Act. Then it will discuss a little about *Grocon Constructors Pty Ltd v Planit Cocciardi Joint Venture*.⁴ Related to that, it will consider the relationship between Natural Justice and the way time runs during an adjudication and the English decision of *Dorchester Hotel Limited v Vivid Interiors Limited*.⁵ Then finally it will deal with enforcement, and in particular the recent cases on statutory demands and s. 52 of the *Trade Practices Act*.

Recent Victorian Statistics

The Building Commission has recently made available updated statistics.

Prior to 30 March 2007, when the Victorian Act was substantially amended, there were on average 26 applications for adjudication per year in this state. Since the amendment, we are now running at about 70 applications per year. It is a healthy improvement, until one observes that in NSW the number of applications is over 600 per year.

The detailed numbers are as follows: for the first 4 years, 105 applications (26 per year), for the next 3 years (post-amendment) 210 applications (70 each year).

Total adjudication <i>applications</i> to date (ie from Jan 2003)	315
Total adjudication <i>determinations</i> to date	223
Number of adjudication applications from Jan 2003 to 30 March 2007 (amendment date, not a real test but some indication)	105
Number of adjudication applications from 30 March 2007 to 30 March 2010	210

Grocon Constructors v Planit Cocciardi Joint Venture

This case is now the leading decision in Victoria about how the Act will be applied. It was decided on 25 September 2009. It concerned the construction of the new rectangular stadium, a stadium where apparently the outside is made up of

³ See s.10A(2)(e) of the Act

⁴ [2009] VSC 426

⁵ [2009] EWHC 70 [TCC]

architecturally interconnected pipes that will flash with lights and draw in Victorians to games contrary to our genetic coding.

Under the contract Planit Cocciardi was to provide shop drawings to Grocon, principally for the complex pipe sections of the roof. In April 2009 Planit delivered a payment claim that Grocon responded to in a payment schedule and the parties were thus in dispute about fees. The matter was referred to an adjudicator, O'Brien, who on 28 May 2009 awarded Planit \$544,841 together with the costs of the adjudication. Grocon applied for a review adjudication and paid the adjudicated amount into trust. The review adjudicator, Davenport, in his determination of 5 July 2009, confirmed the O'Brien determination and determined Grocon should also pay the adjudication determination fees.

Interestingly, three months prior to the payment claim being delivered by Planit, Grocon had commenced proceedings in the Supreme Court against Planit for damages caused by Planit failing to deliver drawings. Planit had counterclaimed on the basis of contractual variations, unconscionable conduct under the TPA and for a claim under quantum meruit. Within that proceeding the challenge to the adjudication determinations came before Vickery J and first, on 27 July 2009,⁶ he granted an injunction preventing Planit taking any action on the adjudication determination. The published injunction decision is interesting in itself. The mere fact His Honour was prepared to injunct enforcement of the adjudicators' determinations until he heard the application for judicial review is noteworthy.

The matter was sent to mediation, and I mediated it. No more need be said about that.

When the matter returned before Vickery J it was fully argued over 2 days, and 5 weeks later, his Honour published an 83 page judgement that is the current bible for practitioners in Victoria. There is a lot of good sense in the decision and, considered with His Honour's earlier decision in *Hickory Developments Pty Ltd v Schiavello (Vic) Pty Ltd*,⁷ provides considerable guidance as to how the Technology Engineering and Construction List is going to treat similar applications in the future.

Justice Vickery did not follow *Broydn Pty Ltd v Davenport*.⁸ He found certiorari is available against decisions of adjudicators. The reasoning for this, which occupies a considerable part of the judgment, is probably of greater interest to administrative lawyers than construction lawyers.

The length and detail of the judgment in this regard reflects the care taken by a single judge of the Victorian Supreme Court who has decided not to follow a unanimous decision of three judges of the Court of Appeal in NSW on similar legislation. In NSW, *Broydn* stands for the proposition that a jurisdictional error is the only grounds of review, and will only be entertained if the determination fails a three point test. There, adjudication determination will be void ab initio if:

- a) the basic and essential requirements of the Act for a valid determination are not satisfied;

⁶ [2009] VSC 339

⁷ [2009] VSC 156, [2009] VSC 339

⁸ [2004] NSWC 394

- b) the purported determination is not a bona fide attempt to exercise the power granted under the Act; or
- c) there is a substantial denial of the measure of natural justice required under the Act.

Justice Vickery, on the other hand, held that administrative review is available in Victoria. Therefore the facts as well as jurisdiction are open to be looked at. Theoretically a valid decision can be made by an adjudicator, but the Supreme Court might nevertheless still set it aside.

However, when one looks closely at what His Honour says, not much has changed at all. In terms of when a jurisdictional error might be found to have been made, His Honour makes it clear that in his opinion the Act confers on adjudicators jurisdiction to make incorrect decisions in relation to jurisdictional facts which will not be overturned on certiorari.⁹ That is just as it is in *Broydn*.

Further, although an error of fact on the face of the record is capable of judicial review, the test for whether or not a determination will be disturbed is that there must be *no probative evidence* supporting the finding. Although additional to the *Brodyn* tests, it is clearly a very hard test.

In terms of a review on the basis of procedural fairness (or natural justice) His Honour made a number of observations that suggests he might be more inclined to strike down an adjudication for want of procedure than the NSW courts¹⁰ but still, just as in *Brodyn*, the words he used were that a procedural error would have to be “a substantial denial of the measure of procedural fairness required by the Act”; just as has been described in *Broydn*.

Having set out in the judgment the test he considered he should apply, Justice Vickery applied it to the facts of the case. He applied a three stage test. First, he would look at whether there was a jurisdictional error. That is, whether the facts as found by the adjudicator supported the adjudicator having jurisdiction. Then he would look to see whether there was some evidence to support the fact findings made, and if there was, he would find there was no error of law on the face of the record. Then he would look to see whether the *Brodyn* tests were satisfied.

The decision does not change the legal landscape much. To summarise the decision right down, it is now clear that judicial review is available in Victoria. Adjudicators need to base their determinations on identified facts. But it doesn't have to be much. For example the adjudicator in *Grocon* determined there was no dispute resolution clause, an issue of relevance to the way the second class of variations provisions of the Act work. The contract contained a mandatory mediation provision which the adjudicator held was not a dispute resolution clause. The fact the adjudicator looked at the clause was all Vickery J required; he was not going to review whether or not in his opinion it was a dispute resolution clause or not.

⁹ at [116]

¹⁰ at [139] and [140]

Secondly, there are hints in the judgment that in Victoria procedural justice requirements might be higher than in NSW.

Natural Justice

Which brings us to the way time runs for the adjudication process in Victoria. As I explained in the paper published in the December edition of the BDPS News, there are some real advantages to using the Act as a result of the tight time lines it contains. The English case of *Dorchester Hotel Limited v Vivid Interiors Limited*¹¹ dealt with the time lines in an English adjudication and what they might mean for procedural justice. In that case Justice Coulson made some comments that sound a warning bell to those who unfairly press a time line advantages that the Victorian Act contains.

What happened was on 19 December, the Friday before Christmas, a claimant delivered the English equivalent of an adjudication application that was 90 pages long supported by 37 lever arch folders including, amongst other things, 6 substantial witness statements and 2 large expert reports. The adjudicator accepted the reference, but only on condition that a relatively small extension to the imposed time line was agreed. Dorchester said the time line was too tight and breached natural justice and made an application to the court.

The court had to consider when it would intervene in an ongoing adjudication in circumstances where natural justice was *potentially* not going to be provided to a party. Justice Coulson held that he did have power to grant declarations even at the stage the adjudication was at, but, because the adjudicator had already indicated he had considered the matter, he would not intervene. He allowed the adjudication to proceed, but said if natural justice was not accorded, then the respondent could resist an adverse decision on that ground.

The case therefore suggests two things. Within the constrictions of the Act, the adjudicator must do all things possible to ensure the parties do have adequate time to properly respond to adjudication applications, and one way of doing that might be to only accept an adjudication application if natural justice is possible. Secondly, there is a real possibility of persuading a court to intervene prior to an adjudication determination being made if it looks like natural justice is not going to be afforded.

Enforcement and Statutory Demands

If we want to talk about what sort of tool adjudication is, we have to talk about whether it can actually get the money at the end of the day.

Once an adjudication determination has been obtained, a claimant has a number of options open to it. The Act provides 3 additional remedies that are not available outside of the Act.

1st- the claimant can give notice in prescribed form and stop work if an adjudicated amount is not paid; notwithstanding provisions in the contract that say otherwise;¹²

¹¹ [2009] EWHC 70 [TCC]

¹² S. 280(1)(b) of the Act

2nd – an unpaid claimant can exercise a lien over any unfixated plant or materials it has supplied; or

3rd – upon converting an adjudication determination to a judgment of a court, the unpaid claimant can garnishee monies which may otherwise be payable by a principal to the respondent under the relevant construction contract.¹³

However, once the work on site has stopped, or is winding down, the claimant's usual course of action has been to register the adjudication determination as a court order and then use conventional enforcement methods against a judgment debtor corporation. That is, a statutory demand is served under s 459 of the *Corporations Act 2001*. A company served with a statutory demand risks being wound up if it does not make payment in response to a statutory demand.

However, s 459 G of the *Corporations Act* provides an entitlement to the company to apply to set aside the statutory demand within 21 days of being served. Section 459 H provides the test that has to be satisfied. There are two bases of challenge – there has to be a genuine dispute about the existence or amount of the debt to which the demand relates, or there can be an offsetting claim. The court will enquire into these questions to decide whether or not to set a statutory demand aside.

Up until recently, Queensland and NSW authorities differed on how to treat a statutory demand served on a judgment based on an adjudication. In Queensland the line of cases started with *J Hutchinson Pty Ltd v Galform Pty Ltd & Ors* in which Justice Chesterman found that a payment claim under the *Building and Construction Industry Payments Act 2004* was a cause of action in contract, despite the special procedures the Act provided, and he thus concluded "There can be no doubt that an adjudication giving rise to an a judgment does give rise to re judicata..."¹⁴

On the back of that decision an application to set aside a statutory demand was considered by the Supreme Court in Queensland in *Peekhrst Pty Ltd v Wallace & Anor*¹⁵. Douglas J had to consider the issue of whether or not the statutory demand should be set aside in circumstances where there was an offsetting claim against an adjudicated amount for defects. He found a statutory demand should not be set aside where judgement had been given on an adjudication certificate even though defects had not been considered in the adjudication.

However, the recent case Queensland case of *Reed Construction (QLD) Pty Ltd v Dellsun Pty Ltd*,¹⁶ has not followed those cases. Rather Queensland has now fallen into line with the NSW cases and it seems, therefore, very likely Victoria will as well. This case was decided by Martin J in a judgment handed down 4 September 2009. The judgment contains a useful review of the NSW cases. The claim history in the case is somewhat complicated, but in essence Dellsun and Reed took part in an adjudication and the adjudicator awarded some of the amounts claimed. No

¹³ See s. 28R, s.32, s.33, s.34 and s.36. In NSW and Queensland this is done by a separate Act.

¹⁴ [2008] QSC 205 at [36]. Vickery J has already expressed the opposite view in *Grocon v Planit Cocciardi* (op. cit) at [111]

¹⁵ [2007]QSC 159

¹⁶ [2009]QSC 263

adjudication certificate was issued, or judgment obtained thereon, but that does not appear material to the decision.

Passing over the extensive legal analysis for a moment, and jumping to the factual conclusions, His Honour found that notwithstanding the adjudicator's determination, there was a real dispute about Reed's claim. Further, there was also an offsetting defects claim. His Honour found there was a genuine dispute about the claim, and he set the statutory demand aside.

What His Honour did in his reasoning was to follow the NSW cases rather than the cases that had been decided in Queensland. The NSW cases had commenced with the decision of Macready As. J in *Max Cooper & Sons (Builders) Pty Ltd v M & E Booth & Sons Pty Ltd*.¹⁷

First he considered the issue of res judicata.¹⁸ His Honour quoted Barrett J in *Shellbridge Pty Ltd v Rider Hunt Sydney Pty Ltd*¹⁹ to find there was no res judicata in an adjudicator's decision. His Honour said:

“..It seems sometimes to be not sufficiently appreciated that, although a judgment debt might result from the adjudication process, there is no curtailing of contractual and other rights arising in relation to the performance of the relevant work.”

What Barrett J was on about was that as an adjudication determination is only an interim decision it makes no sense to talk of a res judicata that shuts off the right to set aside a statutory demand.

Vickery J, in almost a throw away line in *Grocon*, has clearly stated his view that there is no res judicata in an adjudicator's determination.²⁰ This is a clear signpost Victorian courts will go the same way with respect to statutory demands on the back of adjudications.

However, of perhaps greater importance to the NSW line of cases is the Australian Constitution and the fact that, where there is a conflict between Commonwealth and State legislation, effect is given to the Commonwealth law. Barrett J quoted extensively from Young CJ in Eq as he then was in *Brodyn Pty Ltd v Dasein Constructions Pty Ltd*²¹ and his review of s.109 of the Constitution. That section provides:

“When a law of a State is inconsistent with a law of the Commonwealth, the latter shall prevail, and the former shall, to the extent of the inconsistency, be invalid”

¹⁷ [2003] NSW 929

¹⁸ *Reed Construction (QLD) Pty Ltd v Dellsun Pty Ltd* [2009] QSC 263 starting at [37]

¹⁹ [2005] NSW 1152

²⁰ *Grocon v Planit Cocciardi*, *ibid* at [111]

²¹ (2005) 21 BCL 443

He adopted Young CJ's view that the state law could not be used to read down the Commonwealth law²² but rather, the state legislations should be read as consistent with the Commonwealth legislation. Thus the *Corporations Act* has pre-eminence over state-based security of payment legislation.

As an aside, in *Broydn v Dasein*, Young CJ looked at the mischief the Act was directed to and the fact that in that case the subcontractor was in voluntary administration and expressed the view that an insolvent contractor could not use the Act.

So in Queensland and NSW a statutory demand on the basis of a judgment riding on the back of an adjudicator's decision will be set aside if there is a genuine dispute that the claimant was not entitled to the amount awarded by the adjudicator. Costs will be awarded against a party that delivers a statutory demand.

Not only that, in the case of *Ettamogah Pub (Rouse Hill) Pty Ltd v Consolidated Construction Pty Ltd*,²³ White J in the NSW Supreme Court held that this principle applies even when no payment schedule was delivered, and summary judgment from a court is obtained.

These decisions strongly suggest statutory demands should not be issued on the basis of a judgment obtained on the back of an adjudication unless there really is no argument the amount is owing. It is hard to imagine a situation where there not some dispute about a claim that has been referred to adjudication or the existence of an offsetting claim is not arguable.

Where does that leave us? Does this mean, as was submitted to Campbell J (as he then was) in *Demir Pty Ltd v Graf Plumbing Pty Ltd*²⁴ that the Act is toothless. Well Justice Campbell did not think so. He said:

“There are means of enforcement, short of a winding up action, which are open to a judgment creditor. When a judgment has been obtained pursuant to the BACISOP Act, if the judgment creditor does not pay it voluntarily, then the judgment creditor can use the range of remedies open to a judgment creditor.”

The three methods of enforcement the Act itself contains are already referred to above. These are really only useful if the project is ongoing. Beyond that, practitioners have invariably turned to statutory demands. Other more general enforcement methods are available, but of all of them the only useful one appears to be the warrant of seizure and sale.²⁵ Using this procedure, an application to sell real property owned might be made, if the defaulting respondent has any, or perhaps tools of trade can be seized by the sheriff. In my view, the prospect of gaining real traction using such processes in commercial matters looks pretty grim. Amazing though it seems, builders and proprietors seem rarely to actually own anything in their own names nowadays.

²² [84]

²³ [2006] NSWSC 1450

²⁴ [2004] NSWSC 553

²⁵ The others, attachment of earnings and attachment of debt, do not appear to have general application

Section 52 of the Trade Practices Act

Lastly I want to briefly mention s.52 of the Trade Practices Act. Like the application of the *Corporations Act*, it has been held that where an adjudication response was not put in by a respondent because it was misled in some way, the security of payment legislation is secondary to the Commonwealth *Trade Practices Act*, and a court will decline to enter judgment if there is a real argument s.52 has been breached.²⁶ It is likely to be a defence with little scope for general application, but in a landscape where a respondent has so few possibilities, it is one practitioners should always consider.

Conclusion

So, what kind of tool is adjudication?

Clearly it is proving successful in securing payments from recalcitrant principals.

In my experience it also typically leads to the resolution of the entire dispute between parties, notwithstanding its failings in this regard.

It contains some real incentives to the claimant in the time lines it imposes, but a warning bell has now been sounded about pushing that advantage too hard.

But the real looming issue is in enforcement. It would be a brave claimant who serves a statutory demand on the basis of an adjudication in anything but the clearest of cases.

It seems to me to a good analogy might be it is like a crude fishing rod that despite its problems, certainly can catch big fish. The big question at the moment, with the problems around statutory demands, is can it actually land them.

²⁶ *Bitannia Pty Ltd v Parkline Constructions Pty Ltd* [2006] NSWCA 238, followed in the Victorian County Court by Shelton J in *Winslow Constructors Pty Ltd v John Holland Rail Pty Ltd and another* [2008] VCC 1491