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IMPROVEMENT OF THE PRODUCTIVITY OF THE CONSTRUCTION INDUSTRY
THE BUILDING AND CONSTRUCTION INDUSTRY
SECURITY OF PAYMENT ACT

Prepared by

Ng Cher Cheng

Deputy Director, Business Development Division

BUILDING AND CONSTRUCTION AUTHORITY

SINGAPORE

EXECUTIVE SUMMARY

During the prolonged downturn in the early 2000s, subcontractors and suppliers faced delayed or non-payments for work done or materials supplied and had to take prolonged and expensive legal means to recover payment. The Security of Payment (SOP) Act was introduced to protect the weaker party in the payment chain and facilitate cash-flow by helping to speed up payment in the construction industry so as not to disrupt timely delivery of construction projects.

The SOP regime is characterised by three core pillars: statutory entitlement to payment for parties carrying out work or supplying goods or services for construction projects, low-cost and fast dispute resolution procedure via adjudication for disputed response or non-payment and rights to suspend work if not paid after adjudication. Following the Act's implementation, new standard forms for subcontract have been published, taking cue from the amendments of main contracts both in the public and private sectors. The introduction of the dispute settlement period under the SOP Act serves to promote amicable settlement among the parties, preserving the working relationship.

INTRODUCTION

The productivity of the construction industry in timely delivery projects is in a way influenced by the promptness of payments for work done and services or goods supplied. However, payment problems are not uncommon in the construction industry worldwide. These problems are exacerbated by an industry downturn and highly inequitable and, in some cases, oppressive industry practices. Like its predecessors in the United Kingdom, Australia and New Zealand, Singapore turned to statutory enactments to protect the interests of the industry stakeholders, in particular the subcontractors and suppliers. It has been more than three years since the Building and Construction Industry Security of Payment Act (in short, the SOP Act) came into operation.

Payment Disruption

During the prolonged period of downturn in the early 2000s, many contractors were cash-strapped and some became insolvent. This amounted to “bottom up financing” by the subcontractors and suppliers funding through the entire works. Subcontractors and suppliers who worked and supplied for main contractors experienced delayed or non-payments for work done or materials supplied and had to take prolonged and expensive means such as arbitration or litigation to recover their money. The failure in the smooth and timely payments down the value chain could trigger a collapse of a part or the whole of that chain and more importantly, a severe delay in the progress of the project.

Need for Legislative Intervention

Payment problems, while not unique to the construction industry, are often seen to be worse in this industry than in others. This is because of its multi-tier pyramidal structure of the parties involved, the long construction periods, and the common law position on contractual conditions which lock in those further down the value chain such as payments that often depend on payments further upstream (conditional payment or ‘pay when paid’) and prohibitions on work stoppages or suspensions. The position of subcontractors and suppliers is further weakened by contractual terms which tend to favour those higher up the chain.

A need for legislative intervention is, therefore, necessary to protect the weaker party, in particular the subcontractors and suppliers, and to modify the effects of common law, and codify areas of law as well as to regulate the dispute resolution method by providing a fast and low cost dispute resolution mechanism that is binding in nature. The SOP Act and Regulations came into operation on 1 April 2005.

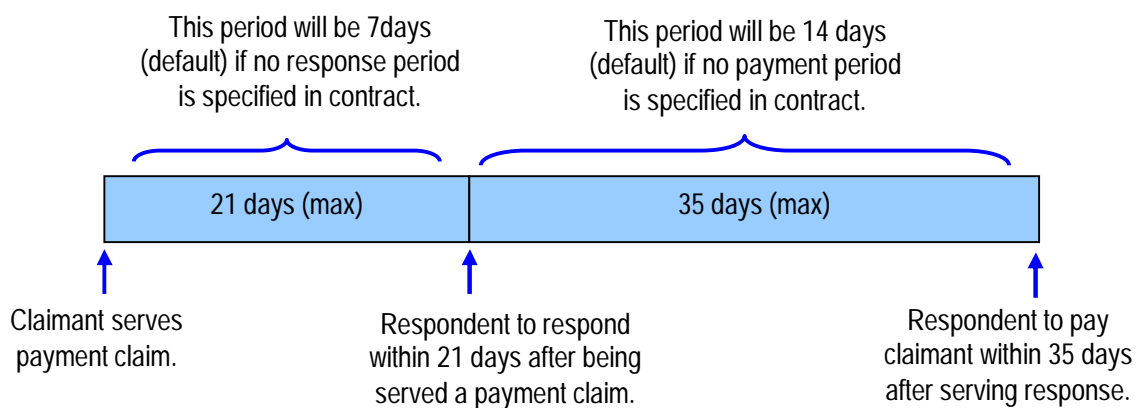
KEY FEATURES OF THE LEGISLATION

The legislation covers two types of contracts: construction contracts (which includes consultancy services) and supply contracts whereby the construction work or related goods and services must be carried out or supplied for a project or site located in Singapore. The Act applies only to written contracts or the written portion of the contract for the construction work or the construction-related services or goods. The SOP regime is characterised by three core pillars: statutory entitlement to payment, low-cost and fast dispute resolution procedure via adjudication and rights to suspend work if not paid.

Statutory Entitlement to Payment

First, it is the statutory entitlement of a party in a written contract who has carried out construction work or supplied related goods or services to progress payments. Contracting parties can agree on terms of payment including when payments are due under the contract. However, the Act will provide for default payment periods if there are no contractual provisions, as well as maximum number of days for payment response and payment due under a contract. In the absence of contractual provision, the default response due date shall be 7 days after a payment claim is served and the payment due date shall be 14 days after a payment response is served. The Act also caps the payment response time to a maximum of 21 days after a payment claim is served and a maximum payment due date to 35 days after the date of payment response is provided.

Figure 1: Payment Timeline for Construction Contracts



Most of the major standard forms of construction contracts do expressly provide for a date on which a progress payment becomes due and payable. However, it was observed that "experiences in other countries have shown that parties with greater bargaining power are likely to impose longer

payment periods on the other parties to circumvent the rights to payment in the SOP Act". To prevent this, the Singapore SOP Act caps the payment period to override unreasonable contractual payment terms and to prevent such exploitation of the freedom of contract which runs contrary to the intent of the legislation. At the same time, this cap is also cleverly introduced to serve a means to keep the overall payment period in check so as to appease the industry's concern over an extended response and payment period.

The Act also seeks to stamp out "pay when paid" contractual provision which makes downstream payments dependent on upstream payments over which they have no control, especially in subcontracts and sub-subcontracts. The Act states that "pay when paid" including various derivatives of such provisions are unenforceable and of no effect in relation to progress payments. If the respondent is withholding any amount from the payment claim, he must provide reasons in his payment response.

This entitlement to payment is further reinforced by the all encompassing statement of policy intent that provisions of the SOP Act cannot be contracted out and, in particular, any provision which purports to exclude, modify, restrict or in any way prejudice (or has such effect on) the operation of the Act or any part thereof is to be rendered void. This includes a provision that may reasonably be construed as an attempt to deter a person from taking action under the Act.

Low-cost and Fast Adjudication

The second core pillar is a low-cost and fast-track dispute resolution proceeding via adjudication with interim binding determination capable of being enforced readily, upholding the statutory entitlement to payment. This process aims to expedite resolution of disputes between parties and hence, a step in the right direction towards enhancing the operating environment of the construction industry by improving cash-flow condition of stakeholders in the construction industry.

Only the claimant has the right to apply for adjudication through the Authorised Nominating Body (ANB) if he does not receive any payment response or full payment or disputes the response amount by the respondent after a seven-day dispute resolution period provided for under the Act. The procedures, including the timelines and the adjudication fees, are prescribed by the legislation.

The ANB shall appoint an adjudicator who must make a determination within 14 days after commencement of the adjudication or any longer time requested by the adjudicator and agreed to by both the claimant and respondent. The determination is binding and the adjudicated amount is payable by the due date unless and until the dispute is determined by a court or tribunal or at any other dispute resolution proceeding, or settled by agreement of the parties. The respondent may apply for the review of the adjudication determination if he is dissatisfied with the determination, provided the disputed amount is above the prescribed amount under the Regulations.

The Act allows for adjudication even if the dispute is the subject of a court proceeding or arbitration, or of any other dispute resolution procedure. Similarly, the Act does not limit any other contractual entitlement the party may have for remedies under any such other dispute resolution procedures. Submission to other dispute resolution procedures, including application to court, also does not end or affect the adjudication. However, an adjudicator must terminate the adjudication proceedings if the dispute is resolved by such other dispute resolution procedure.

Rights to Suspend Work (and Other Resources)

The right to suspend work or supply in order to enforce payment aims to provide a legitimate temporary exit route particularly for subcontractors if not paid in full or not paid at all. Without this, the risk of non-payments would still be there and the subcontractors would still be subject to the imbalance of power. They would be obliged to continue to work albeit at a slower pace and in the process bleed to collapse. If those further down the pyramid are entitled to suspend work for non-payment, it might not prevent the collapse of the main contractor, but it would likely bring down fewer parties and cause considerably less losses to those downstream.

On rights to suspend work or supply, Singapore's cautious approach could be attributed to its small but extremely fast-paced economy whereby any financial impact as a result of suspension of projects would be magnified. Hence, it cannot afford to allow "unnecessary" delay of project which would result in increase in project cost. In addition, several safeguards are also incorporated to prevent abuse of the right to suspend work or supply (for example, the claimant having to serve a prior seven-day notice of such intention to suspend work/supply on the respondent / project owner).

The Act also includes other recourses to the claimant such as the right to exercise lien on goods and enforcement of an adjudication determination as a judgment debt. The principal who is the

respondent's immediate client can also make direct payment to the claimant when the respondent fails to pay the adjudicated amount and recover it from the respondent.

POST-IMPLEMENTATION OBSERVATIONS

Conditions of Contract

Following the implementation of the SOP Act, two of the major standard forms most commonly used in Singapore, the Public Sector Standard Conditions of Contract (PSSCOC) and the Singapore Institute of Architects Standard Form of Building Contract (SIA Contract), have undergone some amendments in an attempt to be in line with the SOP regime.

One of the amendments is the change to payment response provisions. The PSSCOC expressly provides for two types of payment response: the deemed payment response which is effectively a payment certificate issued by the superintending officer and the employer's payment response which will take precedence if it complies with the requirements of the Act or a "merged system". The SIA Contract, however, differs from the approach taken by the PSSCOC. It maintains the independence of the interim certificate to be issued by the architect separate from the payment response to be provided by the employer who is given at least seven days after the issuance of the interim certificate to provide his response. It is also noticed that some subcontracts have also mirrored closely either of the above standard forms on the provisions for payment response.

From the adjudication cases determined so far, it is found that the supposed "payment response" as asserted by the respondents appeared in various forms, in particular the initial cases. In an adjudication case, the respondent's purported payment response by way of letter was served within the prescribed timeline of the Act. However, the letter which was served during the dispute settlement period, in form and substance, must still comply with the requirements of section 11(3) of the Act and Regulation 6 of the Regulations, including the need to state the response amount and reasons for any differences between the claimed amount and response amount. This aims to deter and weed out the unscrupulous practice of delaying or withholding payment without valid reasons.

Similarly, arising from the implementation of the SOP Act, standard forms for domestic subcontract including the supply of goods have been published¹⁰, taking cue from the amendments of the standard forms of main contracts both in the public and private sectors. In order not to be caught by the shorter default provisions for payment response and payment due date under the Act, the subcontracts expressly state such provisions in compliance with the SOP Act. This is one major step forward in the reform of contractual practices and payment behaviour in the industry instilling definitive responsibilities of each party to facilitate cash-flow by expediting payment.

Dispute Resolution

Under section 12(5) of the Act, “dispute settlement period”, in relation to a payment claim, means seven days after the date on which or the period within which the payment response is required to be provided under section 11(1). Section 12(4) of the Act provides that, during the dispute settlement period, either the claimant or the respondent may seek clarification from the other party on any matter relating to the relevant payment claim and that the respondent may provide the claimant with a payment response where he has previously failed to do so or vary the payment response. It is only where the dispute is not settled or the respondent does not provide the payment response at the end of this seven-day period that the claimant may proceed to make an adjudication application.

The provision of such a period, which is in line with a multi-tiered dispute resolution clause in contract, serves to encourage parties to come to an amicable settlement and by avoiding the need for the dispute to be determined in adjudication, any further expenses incurred and time spent could be obviated. In Asian cultures, there is a profound preference for agreed and harmonious solutions rather than one which may damage the parties’ relationship¹¹. As seen in several adjudication cases, the existence of the period itself allows genuine parties to seek clarification or attempt to settle issues and disputes outside adjudication albeit it may not always be successful.

The high level of confidence the courts have on the adjudication machinery under the SOP regime as an interim binding dispute resolution procedure to resolve payment disputes can be seen from a recent case *Lian Teck Construction Pte Ltd v Woh Hup (Pte) Ltd and Others*¹² where Justice

¹⁰ Singapore Contractors Association Ltd (SCAL) Conditions of Sub-Contract for Domestic Sub-Contracts as well as the Conditions of Sub-Contract Supply of Goods.

¹¹ John Burkett, *Disputes without tears: Alternative Methods of Dispute Resolution*, 2000, RIBA Publications, at p37.

¹² [2006] SGHC 118, 4 SLR 1.

Andrew Ang highlighted adjudication under the SOP Act as a faster alternative which the appellant could apply while pending court's hearing on the stay application and summary judgment:

It was argued that to delay the hearing of an application for interim payment until after the stay application had been finally disposed of would cause hardship to a deserving plaintiff. As a partial answer to that, it should be noted that adjudication under s 12(1) of the Building and Construction Industry Security of Payment Act as an alternative means of obtaining interim payment is available *unless* the contract was entered into on or after 1 April 2005. *[With due respect, the learned judge could have meant "if" instead of "unless".]*

Adjudication Statistics (April 2005 to April 2008)

During this period, there were a total of 90 adjudication applications lodged. The main dispute was that most of the respondents did not provide payment response to their claimants. Of these, 58 valid cases were determined, 19 cases were withdrawn by the claimant's own accord and the remaining were either determined invalid or in the progress of adjudication (at the point of reporting). The majority of the adjudicator's fee was within the range of \$2,000 to less than \$6,000 per case.

All the 58 valid cases were determined within the timeline allowed under the SOP Act. The bulk of about 62% were filed by subcontractors against main contractors and another 22% were filed by sub-subcontractors against subcontractors. The rest were cases filed by main contractors or consultants against their clients. 56 determinations were made in favour of the claimants (with close to half of them having obtained adjudicated amount that is more than 90% of their respective claimed amount) and only 2 were determined in favour of the respondents. The maximum and minimum adjudicated amount determined were \$5,632,512.72 and \$11,522.00 respectively.

CONCLUSION

In the Introduction, it is highlighted that the need for a legislative intervention by introducing the SOP legislation in Singapore to protect the weaker party in the payment chain is no different from the other countries who have introduced similar legislation.

While it is recognised that the SOP legislation is not a panacea for all payment issues in the construction industry, it upholds the rights of any party in the industry to seek payment for work done or goods supplied and the speedy and low cost adjudication process will expedite the

resolution of genuine payment disputes so that cash flow will not be disrupted and productivity of the industry will not be adversely affected.

With the core pillars in mind, this Act has been drafted with the understanding on how contractual and dispute settlement are normally handled in the Singapore construction industry, abolishing some undesirable ones yet retaining others which either are in line with or at least does not violate the overall policy intent in providing a more equitable operating environment for all parties of the value-chain in the construction industry as well as reforming the industry payment behaviour.
