



WHITE PAPER

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Significant Reforms on the Horizon for Security of Payment in Victoria's Construction Industry

Like similar regimes in other States, the *Building and Construction Industry Security of Payment Act 2002 (VIC)* (“Victorian SOPA”) was intended to reduce insolvency in the construction industry and enhance cash flow for subcontractors. Inconsistencies with other States and perceived deficiencies led to a parliamentary inquiry in March 2023, resulting in 28 recommended legislative reforms. On 17 October 2024, all of those recommendations received official support from the Victorian Government (in full, in part or in principle).

The recommendations focus on bringing Victoria's regime into line with other States and simplifying the claims process. For example, the Victorian Government has supported recommendations to repeal the “excluded amounts” and “non-claimable variations” provisions that are unique to Victoria. Other significant recommendations include enabling adjudicators and courts to void notice-based time bars and other construction contract terms deemed to be “unfair”. The proposed changes represent a significant widening of the scope of the Victorian SOPA to become very claimant friendly and, if adopted, will likely result in a significant increase in the use of the regime in Victoria. It is not yet clear when the recommendations will be formally considered for adoption, but reform is on the horizon.

The Victorian SOPA was introduced to address insolvency issues in the construction industry by providing subcontractors with the statutory right to issue “payment claims” for “progress payments” for work done prior to completion of the project to maintain adequate cash flow. The Victorian SOPA allows disputes about payments to be resolved in the first instance via adjudication as opposed to litigation. This introduced a “pay now, argue later” system intended to give subcontractors a “fair go” without the need for lawyers to become involved. However, the Victorian SOPA is not aligned with other Australian jurisdictions and has had several perceived deficiencies that have led the Victorian Legislative Assembly to launch an inquiry into the security of payments in the construction industry (“Parliamentary Inquiry”) in March 2023.

The Parliamentary Inquiry resulted in 28 recommendations for legislative reforms, all of which have received support from the Victorian Government in full, in part or in principle in a report tabled on 17 October 2024. With the Victorian Government having expressed support for reform, significant changes in the construction industry are imminent—namely: (i) the introduction of a mechanism to declare notice-based time bars unfair, a mechanism currently available only in Western Australia; and (ii) the ability for the Victorian Government, via regulations, to expressly prohibit certain contractual clauses as “unfair”.

The Victorian Government has also supported reforms to bring Victoria in line with all other Australian jurisdictions by removing the exclusion of “non-claimable variations” and other defined “excluded amounts” from the Victorian regime, as well as removing the ability to provide “new reasons” in adjudication. There is also support for other practical reforms, such as the abolishment of the concept of “reference dates” that had become highly technical and frequently litigated, as well as the introduction of a “black out period” for filing of adjudications.

The Victorian Government has supported the provision of an entitlement to claim retention money and indicated in-principle support for processes that safeguard progress payments and retention monies from being wrongly withheld or misapplied by those higher in the contracting chain.

Some of the key recommendations supported by the Victorian Government are outlined in more detail below.

REMOVAL OF THE “EXCLUDED AMOUNTS” AND “NON-CLAIMABLE VARIATIONS” REGIME

Currently, the Victorian SOPA prevents “excluded amounts” and “non-claimable variations” from being considered when calculating progress payment entitlements. “Excluded amounts” include payment claims for compensation of costs associated with project delays or prolongation, latent conditions, changes in regulatory requirements and non-contract claims. “Non-claimable variations” are simply disputed variations that are not claimable depending on the value of the contract. Moreover, in *Seabay Properties Pty Ltd v Galvin Constructions Pty Ltd & Ano* [2011] VSC 183, the Victorian Supreme Court determined that the excluded amounts provisions also apply to respondents, thereby barring respondents from referring to an excluded amount to justify their proposal to pay less than the value pursued by the claimant.

The concept of excluded amounts and claimable variations is said to have increased the cost and complexity of disputes and reduced the overall amount of money that can be recovered through the Victorian SOPA adjudication process, inconsistent with regimes in all other Australian jurisdictions.

The Victorian Government has supported the recommendations to:

- Repeal section 10-10B of the Victorian SOPA which prevents “excluded amounts” from being considered when calculating progress payment entitlements;
- Introduce a new provision that enables contractors to claim a progress payment calculated in accordance with a contract or, if the contract does not provide for the matter, calculated on the basis of the value of construction work carried out and accounting for additional costs incurred during the project; and
- In line with the repeal of section 10-10B, remove the adjudication review mechanism in division 2A of the Victorian SOPA, which allows only for the review of determinations that involved excluded amounts.

ABOLISHMENT OF THE “REFERENCE DATE” CONCEPT

Currently, a claim for a progress payment in Victoria can be made within three months of the reference date only. Unless provided for in the contract, if the payment claim is not for a single or one-off payment, or a final payment, then reference dates will arise 20 business days after the work was first carried out and then every 20 business days after the last reference date. In practice, the correct calculation of reference dates can be complex, and it has become a minefield of litigation. Additionally, the Parliamentary Inquiry identified that the reference date provisions facilitate practices in which head contractors strategically invoke termination clauses prior to a reference date to prevent subcontractors issuing payment claims.

The Victorian Government has supported the recommendation to bring Victoria in line with NSW and:

- Remove the concept of reference dates from the Victorian SOPA;
- Enable at least one payment claim to be made per calendar month; and
- Expressly provide for a payment claim to be made on or following the termination of a contract for goods and services provided up to the date of termination.

AMENDMENT OF “BUSINESS DAYS” DEFINITION AND INTRODUCTION OF A “BLACKOUT PERIOD”

The Victorian SOPA includes strict timelines for issuing and responding to payment claims, governed by the definition of “business days”, which excludes Saturdays, Sundays and Victorian public holidays. However, the construction and legal industry shut down for an extended period over Christmas and New Year beyond the public holidays, making it difficult in practice for respondents to address payment claims submitted during this period, and encouraging claimants to exploit respondents by strategically issuing claims in this period.

This issue is currently addressed in all other Australian jurisdictions by a defined “blackout period” during the holiday period that excludes it from the calculation of relevant time frames

for claims. The Victorian Government has supported the recommendation to amend the definition of “business days” to exclude the period between 22 December and 10 January inclusive in addition to weekends and public holidays.

INTRODUCTION OF MECHANISM TO DECLARE NOTICE-BASED TIME BARS UNFAIR

Construction contracts often include notice provisions which require payment claims to be submitted within a specified time frame and bar contractors who fail to meet the time frame from bringing claims. The Parliamentary Inquiry found that “unreasonable” time bars have become common in the industry, making it impossible for claimants to pursue what is otherwise a valid entitlement.

The Victorian Government has supported the insertion of a new provision modelled on the Western Australian legislation which provides that notice-based time bar clauses can be declared “unfair” by an adjudicator, a court, an arbitrator or other expert appointed by the contracting parties to determine a matter under the contract if compliance with the clause is not reasonably possible or would be unreasonably onerous.

This would be a significant amendment given that dispute over such clauses is incredibly common in the industry, and courts have generally been reluctant to modify or not enforce a clearly articulated time bar in a contract between commercial parties. Currently, Western Australia is the only other jurisdiction with this mechanism, introduced only recently in 2021 and remains to be tested in litigation.

PROHIBITION OF UNFAIR CONSTRUCTION CONTRACT TERMS

The Victorian Government has supported the recommendation to amend the Victorian SOPA by inserting a provision that allows the Victorian Government, by amendment to the regulations, to expressly prohibit unfair construction contractual clauses and rendering them void. While it is not yet clear how the threshold of “unfair” will be interpreted, the Victorian Government has indicated that it aims to ensure its regulations can keep pace with evolving contractual practices in the

industry. If this recommendation is legislated, it will be interesting to see how the Victorian Government exercises its ability to effectively alter risk allocation in contracts and whether this increases the instances and costs of adjudication.

EXTENSION OF TIME LIMIT FOR MAKING PAYMENT CLAIMS

The Victorian SOPA currently provides that progress payment claims, including final payment claims, are invalid unless submitted within three months of the relevant reference date, or later if allowed in the contract. This is quite short when compared to New South Wales, which allows for final payment claims to be submitted up to 12 months after construction work is completed. A key issue is that the Victorian SOPA was intended to protect small–medium construction business. Such businesses, however, commonly do not have the expertise or resources to chase up unpaid invoices immediately, especially as non-payment increases the importance of focusing on new projects to maintain cash flow. Moreover, in the event of a payment dispute, three months is not sufficient time to explore a negotiated outcome.

The Victorian Government supported the recommended amendments modelled on the Western Australian regime, which would enable:

- A progress payment to be claimed up to six months after the relevant construction work was completed, or later if provided for in the contract; and
- A final payment to be claimed before whichever of the following is the latest:
 - six months after the completion of works or supply of goods under the construction contract;
 - 28 days after the end of the last defects liability period for the construction contract; or
 - the date provided for in the construction contract.

AMENDING TIME LIMITS FOR PAYMENTS

The Victorian SOPA provides that a payment claim becomes due and payable in accordance with the terms of the contract. It is only where a construction contract is silent on payment

terms that the Victorian SOPA requires payment within 10 business days. In practice, head contractors will impose extensive payment terms (e.g., up to 120 days) on subcontractors with limited negotiating power, thereby exacerbating cash flow issues in the industry.

The Victorian Government supported the recommendation to amend the Victorian SOPA and provide that a payment claim becomes due and payable:

- On the date set by the terms of the contract, subject to the payment term not exceeding 25 business days after the payment claim has been made; or
- If the contract makes no express provision with respect to the matter, on the date occurring 10 business days after a payment claim is made.

PROVISION OF AN ENTITLEMENT TO CLAIM RETENTION MONEY

The Parliamentary Inquiry found that the Victorian SOPA does not adequately support contractors to pursue retention money left outstanding at the completion of a construction project, and contractors withholding retention money without a right to do so has become a “frequent occurrence”.

The Victorian Government supported the recommendation to amend the Victorian SOPA to expressly:

- Provide an entitlement to claim retention money under the Act, either as part of a broader payment claim or as a stand-alone claim; and
- Empower an adjudicator to decide whether retention money is to be returned, the proportion which is owed and the date on which it is to be returned.

Moreover, without deciding on a model, the Victorian Government has indicated in-principle support for processes that safeguard progress payments and retention monies from being wrongly withheld or misapplied by those higher in the contracting chain. The Victorian Government indicated that it would need to engage in further consultation with relevant stakeholders before any specific amendments were made.

This follows a recent clarification by the Victorian Supreme Court that retention money may be claimable under the Victorian SOPA (*Hunters Green Retirement Living Pty Ltd v JG King Project Management Pty Ltd* [2023] VSC 536).

REMOVAL OF THE OPPORTUNITY TO PROVIDE NEW REASONS IN ADJUDICATION

Currently, the Victorian SOPA allows respondents in an adjudication process to provide new reasons for withholding payment which were not previously raised as part of a payment schedule, which is unique to the Victorian jurisdiction. Adjudicators are then tasked with identifying whether an adjudication response includes new reasons for withholding payment, notifying the claimant and providing them with two business days to respond. The Parliamentary Inquiry found that this disadvantages claimants by forcing them to decide whether to adjudicate without all the information as to why payment is being withheld and potentially exposing them to an “ambush” during adjudication of which they have only two days to respond.

The Victorian Government supported the recommendation to bring Victoria in line with other jurisdictions by:

- Prohibiting respondents from including reasons in their response to an adjudicator that were not previously included in the payment schedule; and
- Removing the requirement for adjudicators to identify these reasons and provide claimants with two days to respond to them.

EXTENSION OF ADJUDICATION DETERMINATION DEADLINE

The Parliamentary Inquiry found that the Victorian SOPA provided insufficient time for an adjudicator to determine the dispute. Currently, an adjudicator has 10 business days (or up to 15 business days if the claimant agrees) to make a determination. However, adjudicators will not have all the information they require to make a determination (primarily the adjudication response) until several days into this time frame.

The Victorian Government has accepted the recommendation that the Victorian SOPA be amended to provide that:

- An adjudication determination must be made within 10 business days of:
 - a respondent providing a valid adjudication response;
 - the date an adjudication response became due; or
 - if the respondent is not entitled to provide an adjudication response, the date the adjudicator accepted the adjudication application; and
- The claimant and the respondent may agree to extend the time frame by up to an additional 20 business days.

MODERNIZING SERVICE

The Victorian Government supported practical amendments to the Victorian SOPA that will allow service in relation to payment claims to be made electronically, such as via email.

Although an official draft bill is yet to come, it is important for all contractors in the chain to be aware of the upcoming changes and their impacts on project management and potential payment disputes.

CONCLUSION

If adopted, the proposed changes to the Victorian SOPA will likely result in a significant increase in the use of the regime in Victoria. The Victorian Government is yet to confirm when the recommendations will be formally considered for adoption, but given the issues of insolvency in the construction industry, it is likely the Victorian Government will move quickly.

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