

Adjudication in Australia: A Study of Adjudication Activity in New South Wales for 2013/14

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Abstract: *The Building and Construction Industry Security of Payment Act 1999 (NSW) (the NSW Act) is a unique form of statutory regulation for the building and construction industry, which gives virtually all industry participants a statutory right to, and a means of recovering, payments for work done under a construction contract. The research aim is to examine current trends in adjudication applications and determinations under the NSW Act. The data used for this study was the collected by the NSW Office of Finance & Services as part of a regular reporting regime for the period from 1 July 2013 and ending on 30 June 2014. With just over 817 adjudication applications having been made over the 2013/14 period, the data indicates that adjudication is being frequently utilized by stakeholders in the NSW building and construction industry as a means of progress payment recovery. Adjudication is proving to be a popular choice for those making claims of less than AU\$250,000. Claimants were awarded about 36% of the total of claimed amounts and claimants are generally successful at adjudication in terms of the proportion of the claimed amounts determined in their favour. This is particularly so in relation to claims of less than \$100,000, which represents about 70% of the total applications made over the reporting period. The data indicates that adjudication fees are generally modest enough to conclude that adjudication provides claimants across all claim ranges with a relatively inexpensive means of having disputed progress payments determined by an independent adjudicator.*

Keywords: *adjudication, activity, New South Wales, security of payment*

I. INTRODUCTION

The *Building and Construction Industry Security of Payment Act 1999* (NSW) (hereafter referred to as ‘the NSW Act’),¹³ commenced in March 2000 and was introduced as part of the New South Wales Government’s policy to eradicate the practice of developers and contractors arbitrarily delaying payment to subcontractors and suppliers in the NSW building and construction industry. The NSW Act was the first comprehensive legislative scheme to be introduced in Australia to provide, *inter alia*, contractors, subcontractors and building professionals with a statutory right to, and a procedure to recover, progress payments. While it embraces the philosophy of rapid ‘statutory adjudication’ of payment claim disputes introduced in the UK⁴, the NSW Act is substantially different in its structure and operation from its UK counterpart. Similar legislative schemes to that operating in NSW and the UK have since been introduced in all Australian states and territories,⁵ New Zealand,⁶ Sin-

gapore⁷ and the Isle of Man.⁸ On March 8 2011, the Irish Construction Contracts Bill 2010 was passed by the upper house of the Irish Parliament. The Malaysian *Construction Industry Payment and Adjudication Act 2012* was gazetted on 22 June 2012.

‘Statutory adjudication’ is a process defined in the NSW Act of referring a payment claim dispute to an independent third party known as ‘adjudicator’. Whenever a claimant⁹ endorses a payment claim as a claim made under the NSW Act, the claimant may elect to have the payment claim adjudicated upon under the NSW Act if the respondent¹⁰ withholds payment.

This paper will be concerned with the NSW Act only. The aim of the research was to examine adjudication activity under the NSW Act for the period from 1 July 2013 and

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³ New South Wales (abbreviated as ‘NSW’) is one of six states of the Commonwealth of Australia.

⁴ *Housing Grants, Construction and Regeneration Act 1996* (UK) pt. 2

⁵ *Building and Construction Industry Security of Payment Act 2002* (Vic);

Building and Construction Industry Payments Act 2004 (QLD); *Construction Contracts Act 2004* (WA); *Construction Contracts (Security of Payments)*

Act 2004 (NT); *Building and Construction Industry Security of Payment Act 2009* (Tas); *Building and Construction Industry (Security of Payment) Act*

2009 (ACT); *Building and Construction Industry Security of Payment Act 2009* (SA).

⁶ *Construction Contracts Act 2002* (NZ).

⁷ *Building and Construction Security of Payments Act 2004* (Singapore).

⁸ *Construction Contracts Act 2004* (Isle of Man).

⁹ The ‘claimant’ is the person by whom a payment claim is served – see: *Building and Construction Industry Security of Payment Act 1999* (NSW) ss. 4, 13.

¹⁰ The ‘respondent’ is the person on whom a payment claim is served – see: *Building and Construction Industry Security of Payment Act 1999* (NSW) ss. 4, 13.

ending on 30 June 2014. In particular, the trend in the number of adjudication applications and adjudication determinations as well as the success of claimants at adjudication made will be examined. Apart from improving security of payment, the NSW Act also intends to provide a fast and relatively inexpensive mechanism for deciding (on an interim basis) payment claims disputes. Consequently, the researchers attempt to ascertain any trends in the cost of adjudication.

The results of this research may be of interest in other jurisdictions where statutory adjudication for the construction industry has been introduced or where the introduction of statutory adjudication is being contemplated.

II. SECURITY OF PAYMENT DEFINED

The term, ‘security of payment’ is a generic term used to describe [1]: “[The] entitlement of contractors, subcontractors, consultants or suppliers in the contractual chain to receive payment due under the terms of their contract from the party higher in the chain”.

Thus, the security of payment problem refers to [2]: “[The] consistent failure in the building and construction industry to ensure that participants are paid in full and on time for the work they have done, even though they have a contractual right to be paid”.

The security of payment problem has been an ongoing issue for those who carry out construction work, or supply related goods and services under a construction contract [2].

In sum, the security of payment problem is the result of the practice by principals and contractors in the construction industry of unduly delaying and devaluing progress payments owed to subcontractors for work done under construction contracts. The tactic of principals and contractors in delaying payments or unduly reducing the value of payments is largely designed to enhance their positive cash flow at the expense of subcontractors [3].

The security of payment problem has long been a major source of commercial hardship for those operating in the construction industry, particularly for the many small and often undercapitalized firms, which operate at or near the bottom of the contractual chain [4]. It is suggested that, but for the systemically poor payment behaviour of principals and contractors, the problems of commercial hardship and failure amongst small firms in the construction industry would largely be avoided. Furthermore, one must not overlook the potential for the unnecessary generation of societal problems that often accompanies commercial hardship and failure [2].

The next sections of the paper describe the research method adopted for this study, followed by a synthesis and

analysis of the data. Conclusive remarks are then presented.

III. RESEARCH METHOD

The operation of the security of payment legislation in NSW is facilitated by Authorized Nominating Authorities (ANAs). At the time of writing, a total of seven such ANAs were operating in NSW. Their function is to accept adjudication applications, refer adjudication applications to adjudicators and issue, upon request, an adjudication certificate.¹¹ Furthermore, each ANA is required by the NSW Office of Finance & Services (hereafter referred to as the Office) to report regularly on a variety of matters relating to adjudication applications and determinations made in NSW. Reporting is required by the Office with a view of allowing it to “better monitor trends in adjudication” [5].

Data used for this research was the adjudication activity data published by the Office as part of the aforementioned reporting regime. The adjudication activity data used for this research covers the period from 1 July 2013 and ending on 30 June 2014.

IV. ADJUDICATION APPLICATIONS

A. Number and Statuses of Applications

For the period 1 July 2013 and ending on 30 June 2014, the total number of adjudication applications lodged with ANAs was 817 (see Table 1 below). The total value claimed for the period is in the order of AU\$320 million. The highest and lowest claimed amount for the period is AU\$65.2 million and AU\$374 respectively.

TABLE 1: NUMBER AND STATUS OF ADJUDICATION APPLICATIONS

| Status | Number (% of Total) |
|--|---------------------|
| Applications lodged | 817 (100%) |
| Determination released | 556 (68.1%) |
| Determination pending release | 41 (5.0%) |
| Applications completed but not determined [†] | 220 (26.9%) |

[†] ‘Applications completed but not determined’ are application where no determination has been released by the adjudicator and no determination is pending release. In such cases, the adjudication process has come to a premature end between lodgement of the application with the ANA and a determination being made by the adjudicator.

From Table 1 above, it can be seen that, of the total number of adjudication applications lodged with ANAs for the 2013/14 period, a total of 556 determinations were released to the parties. Approximately 5% of the total number of adjudication applications lodged were pending de-

¹¹ ‘Adjudication certificate’ means a certificate provided by an Authorised Nominating Authority under the Building and Construction Industry Security of Payment Act 1999 (NSW), s. 24.

termination or pending release to the parties. About 27% of applications are classified as ‘completed but not determined’.

Whilst the Office does not indicate the reasons for an application being ‘completed but not determined’, previous research shows that it is likely to arise under two following conditions: (1) when the parties settle the dispute and withdraw the application before a determination is made by the adjudicator; and (2) when an adjudicator, after accepting the adjudication application, subsequently decides that the adjudicator lacks the jurisdiction to determine the application and subsequently withdraws their acceptance of the application before making a determination [6,7].

Previous research shows that the first and second condition arises in about 37% and 45% of all cases, respectively [7]. Similar results are reported by in an earlier study [6]. Further study is needed to confirm if the two stated conditions still account for the majority of applications being classified as ‘completed but not determined’.

B. Applications Lodged

Section 14(1) of the Act provides that the respondent may reply to a payment claim by providing a ‘payment schedule’ to the claimant. A payment schedule is, in effect, a notice that must be served on a claimant if the respondent does not intend to pay the whole of the claimed amount by the due date for payment. If the respondent fails to provide a payment schedule within the time allowed under the Act, the respondent becomes liable to pay the claimed amount to the claimant on the due date for payment.

A claimant may lodge an adjudication application under one of the following sections of the Act only - s.17(1)(a)(i); s.17(1)(a)(ii); or s.17(1)(b) as follows:

Firstly, where respondent provides a payment schedule for less than the full amount claimed, and the claimant does not accept the lesser amount, the claimant is entitled to lodge an adjudication application with an ANA under section 17(1)(a)(i) of the Act. Secondly, where respondent provides a payment schedule for the full amount claimed but fails to pay the whole (or any part) of the scheduled amount by the due date for payment, the claimant is entitled to lodge an adjudication application with an ANA under section 17(1)(a)(ii) of the Act. Similarly, where respondent provides a payment schedule for less than the full amount claimed, and the claimant accepts the lesser amount, but the respondent fails to pay that amount by the due date for payment, the claimant is entitled to lodge an adjudication application with an ANA under section 17(1)(a)(ii) of the Act. Finally, where a respondent fails to provide a payment schedule and fails to pay the claimed amount by the due date for payment, the claimant is entitled to lodge an adjudication application with an ANA under section 17(1)(b) of the Act. It should be noted that if an adjudication application is intended to be lodged under

section 17(1)(b) of the Act, and the respondent fails to provide a payment schedule in response to the payment claim, section 17(2) of the Act requires the claimant to give the respondent written notification of the claimant’s intention to apply for adjudication under the Act. This notification, in effect, gives the respondent a second opportunity to provide a payment schedule to the claimant in response to the payment claim.

The distribution of applications lodged (by section of the Act) for the period from 1 July 2013 to 30 June 2014 is shown in Table 2 below.

TABLE 2: APPLICATION LODGED (BY SECTION NUMBER)

| Section number | Number (% of Total) |
|----------------|---------------------|
| s.17(1)(a)(i) | 414 (50.7%) |
| s.17(1)(a)(ii) | 2 (0.2%) |
| s.17(1)(b) | 401 (49.1%) |
| Total Number | 817 (100%) |

Table 2 shows that, for the study period, respondents elected in about half of cases to provide a payment schedule at the first opportunity afforded by the NSW Act (i.e., within 10 business days of receiving the payment claim). However, the data does not reveal how many of the remaining respondents elected to provide a payment schedule in reply to the notification made under s.17(2) of the NSW Act. It may be that those respondents who elected not to provide a payment schedule after receiving notification are ignoring payment claims in order to delay or escape payment. Conversely, it may be that those respondents who elected to provide a payment schedule only after receiving notification are making use of the additional time allowed for under the NSW Act to prepare the payment schedule.

Given the absence of data on this question, no firm conclusions can be drawn as to the reasons why some respondents choose to provide direct-response payment schedules and others delay the provision of a payment schedule until an s.17(2) notice is served.

C. Adjudication Determinations

For the period 1 July 2013 to 30 June 2014 a total of 556 adjudication determinations were released to the parties. The aggregate of adjudicated amounts, for applications where a determination was released, is in the order of AU\$80.6 million. This represents the aggregate amount of progress payments returned to claimants using the statutory adjudication process during 2013/14 period.

Of the total number of 556 determinations released, adjudication applications made in the small to medium value claim bracket (<AU\$500,000) are the most frequently lodged applications by claim range, with claims of less than AU\$250,000 being the most predominate. Furthermore, of the total number of determinations released, applications are most frequently lodged for claimed amounts

of less than AU\$25,000. The data also indicates that 'Contractors' and 'Head contractor' are the most frequent users of adjudication to recover payment.

One indicator of the level of success of claimants at adjudication is the proportion of the claimed amount being determined by adjudicators as payable. The Department's data that shows the proportion of the aggregate claimed amount determined by adjudicators in favour of claimants for the period 1 July 2013 to 30 June 2014.

Of the 556 determinations released, the aggregate of claimed amounts was AU\$221.2 million and the aggregate of adjudicated amounts in the order of AU\$80.6 million. The data indicates that adjudicators, overall, awarded claimants just 36% of the aggregate amount claimed for the reporting period, supporting the view that claimants tend to have a modest level of success at adjudication in terms of the proportion of the claimed amount awarded by adjudicators. When these results are examined by claim-range, it is apparent that the level of success of claimants at adjudication varies noticeably.

For example, The Office's data shows, firstly, that about 70% of the total number of determinations released were made in respect of claims for less than \$100,000. In these cases, adjudicators determined, on average, about 85% of the claimed amount, with 61% of claimants having 100% of their claim determined in their favour. Secondly, about 21% of the total number of determinations released was made in respect of claims in the range \$100,000 to \$500,000. In these cases, adjudicators determined, on average, about 68% of the claimed amount, with 24% of claimants having 100% of the claim determined in their favour. Finally, about 10% of the total number of determinations released was made in respect of claims of \$500,000 or greater. In these cases, adjudicators determined, on average, about 40% of the claimed amount, with less than 10% of claimants having 100% of the claim determined in their favours.

Overall, the Office's data indicate that claimants making claims up to about \$250,000 are notably more successful at adjudication than those making larger claims, both in terms of the average proportion of the claimed amount determined by adjudicators and the frequency of the full amount claimed being determined in favours of the claimant.

It is not clear, however, to what extent (if any) the provision of a payment schedule impacts on the level of success of claimants at adjudication in terms of the average proportion of the claimed amount determined by adjudicators or the frequency of the adjudicator determining the full amount claimed in favour of the claimant. Previous research shows that, generally, claimant success at adjudication declines sharply when respondents provide a payment schedule [6].

D. Cost of Adjudication

One of the most important objectives of the NSW statutory adjudication process is to provide claimants with a rapid and inexpensive mechanism for determining disputed progress payments. This is achieved by the utilization of experienced and independent adjudicators.

The Office's data shows that total adjudication fees (i.e., the fees of the ANA plus the fees and expenses of the adjudicator) for the period 1 July 2013 to 30 June 2014 were in the order of AU\$2.4 million. The average total adjudication fee was AU\$4,235. The largest adjudication fee was AU\$143,190. The smallest adjudication fee was \$nil.

Under the NSW Act, adjudicators have the discretion to determine the proportion of the adjudication fees each party is required to pay. Previous research shows that when adjudicators determine a \$nil adjudicated amount, respondents are generally required to pay 100% of the adjudication fees [6]. In the remainder of cases, the amount of the total adjudication fee that claimants are required to pay will vary.

The distribution of the parties' share of the average total direct fees (by claim range) for all adjudication determinations released for the period 1 July 2013 to 30 June 2014 shows that respondents are, overall, required to pay the greater proportion of the total adjudication fees across the spectrum of claim values.

The Office's data shows that there is an inverse relationship between the amount claimed and the total adjudication fee when expressed as a percentage of the amount claimed. In relation to claimed amounts of less than \$100,000, the total adjudication fee equates, on average, to only about 11% of the total claimed amount. This figure increases to a maximum of about 23% for the claims of less than \$5,000 and decreases to a minimum of about 6% for claims between \$40,000 and \$99,000.

When comparing adjudication with dispute resolution processes, such as arbitration and litigation, which are processes acknowledged as being costly [8], the Office's data indicates that adjudication is providing a financially viable option, particularly for those making claims less than \$100,000, to have progress payment disputes heard and determined, albeit on an interim basis, by an independent third party. This conclusion is consistent with the Office's data which shows that almost 70% all of the adjudication applications made under the NSW Act were made in relation to claims less than \$100,000.

The data shows that the Adjudicators' overall share of the total adjudication fees is about \$1.7 million (or about 73% of the total fees). The ANAs' overall share of the total adjudication fees amounted to about \$632,000 (or about 27% of the total fees).

V. CONCLUSION

With just over 817 adjudication applications having been made from 1 July 2013 to 30 June 2014, the data indicates that adjudication is being frequently utilized by stakeholders in the NSW building and construction industry as a means of progress payment recovery.

The data reveals, overall, that claimants were awarded about 36% of the total of claimed amounts. The data reveals that claimants are generally successful at adjudication in terms of the proportion of the claimed amounts determined in their favour. This is particularly so in relation to claims of less than \$100,000, which represents about 70% of the total applications made over the reporting period.

This result, read in the light of the data showing the proportion of the claimed amounts determined by adjudicators across the individual claim ranges, indicates, on its face, that adjudication is a rigorous process for securing progress payments in the construction industry.

The data indicates that adjudication fees are generally modest enough to conclude that adjudication provides claimants across all claim ranges with a relatively inexpensive means of having disputed progress payments determined by an independent adjudicator. For those making claims of less than \$250,000, adjudication is proving to be a popular choice.

The total of adjudicated amounts was in the order of \$80.6 million. This amount represents the total of progress payments returned to claimants through the adjudication process. It is reasonable to conclude that the NSW Act is making a significant and positive impact on the cash flow of many in the construction industry.

In summary, the empirical evidence suggests that the main aim of the NSW Act to improve security of payment in the building and construction industry is, to a large extent, being achieved.

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