

By post and by fax at 3167 2630

18 September 2015

Development Bureau  
Works Policies 1 Section  
15/F, West Wing, Central Government Offices  
2 Tim Mei Avenue  
Tamar, Hong Kong

[Attn: Ir VY Ek Chin]

Dear Ir VY

**Public Consultation on Proposed "Security of Payment" Legislation for the Construction Industry**

Thank you for the letter of 29 May 2015 inviting the Institution to put forth our views on the captioned subject.

In response to the subject, the Hong Kong Institution of Engineers is pleased to provide herewith our views and suggestions for your consideration.

Thank you for your kind attention.

Yours sincerely



Ir CHAN Chi Chiu  
President  
The Hong Kong Institution of Engineers

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## Enclosure

### **Views from the Hong Kong Institution of Engineers on Proposed Security of Payment Legislation for the Construction Industry**

#### **Introduction**

The Hong Kong Institution of Engineers (HKIE) supports in general the Proposed Security of Payment Legislation (SOPL) for the construction industry which aims at regulating certain aspects of payment practice in the construction industry and also providing for rapid interim dispute resolution through adjudication.

2. The HKIE notes the following rationales in the Consultation Document of SOPL:

- (i) SOPL for the construction industry is to help main contractors, sub-contractors, consultants and suppliers receive payments on time for work done and services provided. It also provides a means to rapidly resolve disputes. There have been many voices in the Hong Kong construction industry advocating the introduction of SOPL to improve payment practices and dispute resolution.
- (ii) Significant payment problems are being experienced by main contractors, sub-contractors, consultants and suppliers. Particular problems include the use of 'pay when paid' clauses and payments being delayed by disputes. Payment problems are more severe in the private sector. Administrative and contractual arrangements on public works contracts alone cannot help resolve the problems of the wider industry.

3. The HKIE notes in the Consultation Document that the two broad considerations of the legislation are providing rights to those who provide work, services, materials or plant who are most in need of protection, and who are often smaller contractors and sub-contractors working in the lower tiers of contract chains; and ensuring that less sophisticated and less knowledgeable procurers of work, services, materials or plant are not over burdened with the requirements of the legislation or put at risk of claims and adjudications which they are ill equipped to deal with.

4. The HKIE observes that the coverage of SOPL will be different in the public and private sectors, and that SOPL is proposed to apply to written and oral contracts.

5. The HKIE welcomes the enactment of SOPL for Hong Kong and believes that this enactment will encourage fair payment as well as rapid dispute resolution and increase cash flow in the construction industry.

## Further Views

6. In the following sections, we would like to provide our comments in details on the respective questions as laid down in Appendix B of the Consultation Document for consideration:

*Q1(1)* The HKIE agrees that SOPL should apply to all public sector contracts but should not override the power and duties of the *Contract Administrator* as provided in the contract. Taking General Conditions of Contract (GCC) for Civil Engineering Works 1999 Edition, Cl 86(1) as an example, “statutory Payment Claims” should only be served after the “Settlement of Dispute” procedures under the contract has been exhausted, i.e. either that the Engineer fails to give such decision for a period of 28 days after being requested to do so or that the Employer/ the Contractor be dissatisfied with any such decision of the Engineer.

*Q1(2)* The HKIE notes the first consideration of the legislation as mentioned in paragraph 2 above. As private Alteration & Addition contracts and renovation/ maintenance contracts involve many small local contractors and sub-contractors who are in need of protection of SOPL, the HKIE suggests that all private contracts should also be included in the proposed legislation but which may be implemented at a later stage, say, after reviewing the experience and condition of implementation of SOPL on public sector contracts.

*Q2* As one of the broad considerations is to provide rights to those who provide work, services, materials or plant, and who are most in need of protection and that these are often smaller contractors and sub-contractors working in the lower tiers of contract chains, the HKIE does not object that all private sub-contracts (irrespective of whether the main contract is subject to SOPL or not) may also be included in the proposed legislation.

*Q3* The HKIE agrees that the SOPL should apply to contracts relating to construction activities carried out in Hong Kong even if one or both parties are foreign parties and even if the law of the contract is not Hong Kong law since it is anticipated that the works will mainly be carried out by local contractors and sub-contractors.

*Q4* The HKIE agrees that SOPL should apply to oral and partly oral contracts as well as written contracts since the smaller contractors and sub-contractors who are in need of protection of SOPL are the parties most likely to be working on the basis of oral or partly oral agreements.

*Q5* The HKIE agrees that professional services contracts which relate directly to planned or actual construction activities in Hong Kong should be covered by SOPL.

- Q6* The HKIE agrees that contracts for the supply of materials or plant (even if they do not include for any installation or operation on site) should be covered by SOPL.
- Q7* The HKIE agrees that contracts of employment, insurance, guarantee and loan should be excluded from the scope of SOPL.
- Q8* The HKIE agrees that parties to the contract should be free to agree the number of Progress Payments, when they can be claimed and the basis for calculating amounts due, as the practice of Design and Build contracts with milestone payment schedules.
- Q9* The HKIE agrees that the maximum Payment Period which can be agreed for payments should be 60 calendar days for interim Progress Payments and 120 calendar days for final Progress Payments.
- Q10(A)* The HKIE agrees that parties who are entitled to payments under the terms of a contract covered by Hong Kong's SOPL should be entitled (but not obliged) to claim their payments by way of statutory Payment Claims, but "statutory Payment Claims" could only be served after the "Settlement of Dispute" procedures under the contract has been exhausted, like the scenario of the example mentioned above in *Q1(I)* GCC for Civil Engineering Works 1999 Edition, Cl 86(1).
- Q10(B)* The HKIE agrees that paying parties should be entitled to serve Payment Responses no later than 30 calendar days after receipt of Payment Claims.
- Q11(A)* The HKIE agrees that in the absence of express agreement, parties undertaking work or providing services, materials or plant should be entitled to make Payment Claims at calendar month Payment Intervals.
- Q11(B)* The HKIE agrees that in the absence of express agreement, payments due should be calculated based on the value of work, services, materials or plant provided and with valuations based on any relevant contract price or pricing or in the absence of the same on market rates prevailing at the time the contract was entered into. However, the HKIE notices that determining the quality issues can be often quite subjective, and in the absence of express agreement, calculating the value of work done for Design and Build contracts with milestone payment schedules would be difficult.
- Q11(C)* The HKIE agrees that in the absence of express agreement, paying parties should be entitled to serve a Payment Response within 30 calendar days of receiving the Payment Claim for interim payment claims. However, it may take much longer time to respond to final or near-final payment claims.

- Q11(D)* The HKIE does not object that in the absence of express agreement, the Payment Period for any amount due should be 60 calendar days (interim Progress Payments) or 120 calendar days (final Progress Payments) after receipt of a Payment Claim.
- Q12(A)* The HKIE agrees that paying parties who fail to serve Payment Responses within 30 calendar days (or any earlier period agreed in the contract) of receipt of Payment Claims should not be automatically liable to pay the full amount of the Payment Claim, as it may take much longer time to respond to final or near-final payment claims.
- Q12(B)* The HKIE agrees that paying parties who fail to serve Payment Responses within 30 calendar days (or any earlier period agreed in the contract) of receipt of a Payment Claim should not be able to raise any set off against amounts properly due against the Payment Claim.
- Q13(A)* The HKIE agrees that ‘pay when paid’ clauses should be rendered ineffective.
- Q13(B)* The HKIE agrees that ‘pay when paid’ clauses should be ineffective even where the reason for non-payment is insolvency higher in the supply chain. The HKIE notes that the issue of injustice to the paying party, who is also adversely affected but unlikely to obtain any remedy without going through lengthy legal process, should be addressed.
- Q14(A)* The HKIE agrees in principle that clauses which make payment under a contract conditional on certification or performance of obligations under another contract should be rendered ineffective, but opines that consideration may be given if other contract is also made between the same contracting parties and under the same project.
- Q14(B)* The HKIE agrees that no exception should be made for nominated sub-contractors.
- Q15* The HKIE agrees that Hong Kong’s SOPL should introduce a right for parties to suspend all or part of their works or reduce the rate of progress in the event of non-payment.
- Q16* The HKIE agrees that the right to suspend or reduce the rate of progress should only arise after non-payment of an adjudicator’s decision.
- Q17(A)* The HKIE agrees that parties which suspend or slow work for non-payment should have rights to additional time to complete their obligations and to reasonable costs and expenses in respect of delay and disruption arising from the suspension.

*Q17(B)* The HKIE agrees that the right to suspend or slow work should go hand in hand with the obligation to resume work within a set period of time after payment is made, and the set period for resumption of work after payment is suggested to be 10 working days.

*Q18(A)* The HKIE agrees that unpaid parties should be obliged to give written notice of their intention to suspend to the non-paying party and (if known) to any party which pays the non-paying party (the “principal”) and to the site owner to allow the site owner to make preparations before serving the intention to suspend work.

*Q18(B)* The HKIE opines that there should be different notice periods for non-payment of amounts admitted as due in a Payment Response and non-payment of adjudicators’ decisions. Our suggested appropriate notice period would be:

(a) 10 working days after non-payment of amount admitted as due in a Payment Response; and

(b) 5 working days after non-payment of adjudicator’s decisions.

*Q19(A)* The HKIE agrees that both parties to a contract should be entitled to refer disputes to adjudication, but we opine that “Statutory Payment Claims” could only be served after the “Settlement of Dispute” procedures under the contract, if any, has been exhausted.

*Q19(B)* The HKIE agrees that the right to adjudicate should be limited to disputes relating to

(a) the valuation of work, services, materials and plant supplied and claimed in a Payment Claim;

(b) other money claims made in accordance with any provision of the contract and claimed in a Payment Claim; and

(c) set offs and deductions against amounts due under Payment Claims.

While it is noted that assessment/ response to claim for entitlement to extension of the time for performance would take much time and effort, it is however a common item of dispute and would lead to great impact on cost. It is suggested that a threshold may be considered to set out, such that for contracts which have large EOT disputes (say, 30% of contract period or cost exceeding a 10% of contract sum), adjudication may be used to determine entitlements.

*Q20* The HKIE agrees that there should be a time limit for commencement of adjudication of 28 calendar days from either

- (a) non-payment of an amount admitted as due in a Payment Response; or
- (b) service of a Payment Response disputing all or part of a Payment Claim and/or identifying amounts to be set off against or deducted from amounts otherwise due in respect of the Payment Claim; or
- (c) the failure of the paying party to serve a Payment Response in relation to the Payment Claim within the required time.

But the HKIE opines that disputes as to the entitlement to extension of the time for performance of work would take much time and effort to assess, and may not be suitable for adjudication.

*Q21(A)* Regarding the adjudication procedure features, the HKIE opines that

- (a) “Statutory Payment Claims” could only be served after the “Settlement of Dispute” procedures under the contract, if any, has been exhausted;
- (b) the adjudicator should be appointed by nomination from an agreed nominating body or (if none) from the default nominating body within 5 working days of commencement, and that the default nominating body should be led by the construction industry comprising relevant professionals and other stakeholders for nomination of adjudicators who are conversant in contract administration and dispute resolution in order to swiftly resolve disputes in particular those relating to non-payment;
- (c) the claiming party must serve their submissions together with all supporting evidence they rely on (which may include documents, photographs, witness statements and expert reports) on the responding party on or before the date of appointment of the adjudicator and on the adjudicator on the day of their appointment or the next working day;
- (d) the responding party has 20 working days from receipt of the claiming party’s submissions to respond with their own submissions and all supporting evidence they rely on, but notes that it would take much longer time to respond to final or near-final payment claims, and Extension of Time (EOT) claims;
- (e) the adjudicator shall reach and publish their decision, with reasons,

within 20 working days of receipt of the responding party's submissions extendable by the adjudicator up to 55 working days and to in excess of 55 working days if both parties agree, but notes that it would take much longer time to respond to final or near-final payment claims, and EOT claims;

- (f) the adjudicator should not be allowed to seek response or further submissions and evidence unless they are essential information which the parties should have submitted in the first round of notice of adjudication and response, but instead the adjudicator should be required to inform the disputing parties within 10 working days whether in his opinion the dispute is suitable for adjudication after considering the scope, scale and complexity of the dispute;
- (g) the adjudicator shall be entitled to disregard any further submissions and evidence unless they are essential information requested by the adjudicator himself;
- (h) the adjudicator shall be entitled to resign if they consider that it is not possible to decide the dispute fairly in the time available (being the maximum time available including any extended periods agreed by the parties). The HKIE suggests that the adjudicator should inform the disputing parties whether in his opinion the dispute would need more time to decide, or that the dispute is not suitable for adjudication after reviewing and considering the scope, scale and complexity of the dispute;
- (i) each party will bear its own costs of the adjudication but the adjudicator may decide which party pays the adjudicator's fees and expenses or the proportions in which they are to be jointly paid by the parties. The HKIE opines that the word 'legal' before 'costs' should be deleted in order not to encourage legal input from either party. The HKIE also suggests that the adjudicator should be required to inform the disputing parties his estimate of the total fee for the adjudication prior to commencement of the process.

*Q21(B)* The HKIE opines that the adjudicator should not allow a claiming party to introduce new material in an adjudication unless they are essential information requested by the adjudicator which the parties should have submitted in the first round of notice of adjudication and response.

*Q22(A)* The HKIE agrees that parties should be free to agree adjudicator nominating bodies (ANBs) in their contract. For Government contracts, it is suggested that contracting parties may follow the procedures in appointment of

Disputes Resolution Advisors (DRAs). This leads to the need for establishment of a list of approved (or accredited) ANBs and for clarifying whether fee proposals should be invited and how fee proposals could be assessed.

*Q22(B)* The HKIE opines that the agreed ANB should be responsible for nominating a suitable adjudicator for all disputes since it would be difficult if not impossible for the parties to agree an adjudicator for a specific dispute even after the dispute and right to adjudicate have arisen.

*Q22(C)* The HKIE opines that it is necessary to have a default nominating body, and that the default nominating body should be led by the construction industry comprising relevant professionals and other stakeholders such as the Hong Kong Institution of Engineers, the Hong Kong Institute of Architects, the Hong Kong International Arbitration Centre, the Hong Kong Institute of Surveyors etc. for nomination of adjudicators who are conversant in contract administration and dispute resolution in order to swiftly resolve disputes in particular those relating to non-payment.

*Q23* The HKIE agrees that Hong Kong's SOPL should include provision allowing adjudicator's decisions to be enforced in the same way as judgments of the court and without set off or deduction and allowing responding parties only a short period within which to lodge any challenge to validity.

## **Conclusion**

7. The HKIE would like the Administration to provide further concrete details in regard to the proposed legislation at a later date, so that the opinions of all stakeholders could be obtained and suitably incorporated in the proposed legislation for the overall interest of the whole construction industry.