

RETENTION SUM IN
CONSTRUCTION CONTRACTS

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A thesis submitted in partial fulfilment of the
requirements for the award of the degree of
Master of Science in Construction Contract Management

Faculty of Built Environment and Surveying
Universiti Teknologi Malaysia

AUGUST 2022

DEDICATION

Special thanks to my beloved mother, my partner, my supervisor, friends and co-workers for their unconditional and endless support, understanding, helps and guidance.

Deep Appreciations and Thanks.

ACKNOWLEDGEMENT

I would firstly like to express my deepest gratitude to my supervisor Dr. Farrah Azwanee Binti Aminuddin for her willingness of helping and sharing her knowledge with me, Dr. also bestowed her valuable time to scrutiny through my research report as well as giving proper advises, assistances and guidance throughout my Master research journey. The diligent supervision and support from Dr. had aided me in expediting this research report timely and effectively.

Besides, I would also express my sincere appreciation to my company co-workers with legal background for assisting me in searching and attaining relevant case laws for the research, as well as recommended me a proper portal to conduct case laws searching.

Apart from that, I wish to thank my mother who encouraged me and supported me throughout my research journey. Last but not least, I would also like to express my gratitude to partner and classmates who assist me throughout this research.

ABSTRACT

The construction industry in Malaysia is currently going through hurdle being the pandemic hits the country for a discursive period of more than a year. Adding with the repetitious re-enforcement of lockdowns and the current hike in construction material prices. Henceforth, myriad business sectors in country are severely impacted, thereby it seems pessimistic to the construction by which most construction works are suspended thoroughly, cope with the lack of labour due to the standard of operation enforced to contend the pandemic. It is unavoidable that major players from the construction industry suffers both operationally and financially. Apparently, the suspension of works contributes to delay completion thus dilatory revenue of property sales, which finally led to suspension of payments to the main contractors subsequently to the sub-contractors and even the suppliers. In view of that, it is now the undesired reality that many construction companies being the property developers, contractors or supplier are now at greater risk of insolvency due to financial constraint, many industry players are sauntering on the road to liquidation. One of the concern lest any insolvency occurs is the remuneration of the Retention Sum. The Retention Sum is a sum retained by the employer from the contractor's work done amount certified in every claims (usually 10% of total work done certified thus subjected to a limit of 5% of contract sum), the purpose of the Retention Sum is to be substantiated as a security for the performance of the contractor and to secured against the quality of the workmanship. The recent Federal Court decision of *SK M&E Bersekutu S/B v Pembinaan Legenda Unggul S/B & Another Appeal [2019] 4 CLJ 590* had somehow reversed the retrospective court decision of *Qimonda Malaysia Sdn Bhd (in liquidation) v Sediabena Sdn Bhd [2012] 3 MLJ 422*, which the Federal court reserved the principal of Retention Sum that the retention money is no longer be impulsively a trust money, thus induces the Contractors/Sub-Contractors as unsecure creditors lest event that the Employer goes insolvent or liquidation amid the period of new normal of economy downturn. This issue was promulgated by Sr Jaspal Singh in his recent article concerning retention sum titled *New Normal On Retention Sum – A Judicial Paradigm Shift* published on QS Link magazine issue 2020, Sr Jaspal Singh dwelled over the issue concerning the remuneration and release of the retention sum during these trying times as employers and contractors are on the verge of insolvency, Sr Jaspal Singh also brought up the issues imposed by the Federal court on the recent reversed decision and principal on the retention sum, while the retention sum retained is not defined as a genuine 'trust' anymore hence it is merely a contractual debt rather a sum retained designated to the contractor under the contract. Sr Jaspal Singh also highlighted in this article that the most enviable approach is to keep the retention sum into a segregated bank account in the joint name of the employer and contractor so that trust will be established.

ABSTRAK

Industri pembinaan di Malaysia kini sedang melalui halangan kerana wabak penyakit covid selama tempoh setahun. Disamping itu dengan penguatkuasaan Perintah Kawalan Pergerakan (PKP) yang berulang dan juga kenaikan harga bahan binaan. Akibatnya, pelbagai sektor perniagaan di Malaysia telah diparahkan, justeru kebanyakan kerja pembinaan dipaksa berhenti sepenuhnya, kerja disebabkan standard operasi yang dikuatkuasakan untuk menangani wabak ini. Perhentian kerja-kerja pembangunan ini telah menyebabkan kelewatan penyelesaian, yang akhirnya juga menyebabkan penundaan bayaran kepada kontraktor-kontraktor kerja pembinaan. Kesannya, syarikat pembinaan sebagai pemaju bangunan, kontraktor atau pembekal kini menghadapi risiko insolvensi dan muflis, ramai. Namun salah satu risiko menyebabkan insolvensi adalah penundaan bayaran imbuhan jumlah penahanan kerja (“Retention Sum”). Jumlah penahanan ini adalah jumlah penyelesaian kerja yang dikekalkan oleh majikan daripada jumlah kerja yang telah disiapkan oleh kontraktor di dalam setiap tuntutan bayaran kerja (biasanya 10% daripada jumlah kerja yang disiapkan manakala jumlah ini harusnya tertakluk kepada had 5% daripada jumlah kontrak), tujuan jumlah penahanan adalah untuk dikekalkan oleh majikan sebagai langkah keselamatan menjamin kerja-kerja dan prestasi kontraktor. Merujuk kepada kes Mahkamah Persekutuan iaitu *SK M&E Bersekutu S/B v Pembinaan Legenda Unggul S/B & Satu Lagi Rayuan [2019] 4 CLJ 590* yang telah menterbalikkan keputusan mahkamah retrospektif *Qimonda Malaysia Sdn Bhd v Sediabena Sdn Bhd [2012]] 3 MLJ 422*, yang mana mahkamah Persekutuan pertimbangkan prinsipal jumlah penahanan bahawa ia tidak lagi merupakan wang amanah secara impulsif, dengan itu jumlah penahanan yang disebutkan tidak lagi dijamin memiliki kontraktor sekiranya majikan mengalami keadaan muflis. Isu ini telah diisytiharkan oleh Sr Jaspal Singh dalam artikel terbarunya mengenai jumlah pengekalan bertajuk *New Normal On Retention Sum – A Judicial Paradigm Shift* yang diterbitkan dalam majalah QS Link isu 2020, Sr Jaspal Singh mengulas isu berkenaan dengan isu pelepasan jumlah penahanan (“Retention Sum”) dalam masa yang sukar ini kerana majikan dan kontraktor mengalami insolvensi, Sr Jaspal Singh turut mengemukakan isu yang dikenakan oleh Mahkamah Persekutuan mengenai keputusan baru-baru ini dalam *SK M&E Bersekutu S/B v Pembinaan Legenda Unggul S/B & Satu Lagi Rayuan [2019] 4 CLJ 590* dengan prinsip-prinsipnya mengenai isu jumlah penahanan ini, manakala Mahkamah menegaskan bahawa jumlah penahanan sekarang tidak ditakrifkan sebagai 'amanah', ia merupakan hutang berkontrak dan bukannya jumlah penahanan yang ditetapkan kepada kontraktor di bawah kontrak. Sr Jaspal Singh juga mengulang bahawa langkah yang paling berkesan untuk mengelakkan isu ini ialah menyimpan jumlah penahanan ke dalam akaun bank yang diasingkan di atas nama majikan dan kontraktor supaya jumlah penahanan itu akan dilantikkan kepada kontraktor.

TABLE OF CONTENTS

TITLE	PAGE
DECLARATION	i
DEDICATION	ii
ACKNOWLEDGEMENT	iii
ABSTRACT	iv
ABSTRAK	v
TABLE OF CONTENTS	vi
LIST OF TABLES	xiii
LIST OF FIGURES	xiv
LIST OF ABBREVIATIONS	xv
LIST OF APPENDICES	xvi

TABLE OF CONTENTS

	TITLE	PAGE
CHAPTER 1	INTRODUCTION	
1.1	Introduction	1
1.2	Research Background	1
1.3	Problem Statement	2
1.4	Research Questions	3
1.5	Research Objectives	3
1.6	Research Scope	3
1.7	Research Methodology	4
1.8	Significant of Study	5
1.9	Research Outline	5
1.10	Summary of Chapter	7

TABLE OF CONTENTS

	TITLE	PAGE
CHAPTER 2 LITERATURE REVIEW		
2.1	Introduction	8
2.2	What is Retention Sum in Construction Contracts?	9
	2.2.1 The Purpose of Retention Sum	10
	2.2.2 Percentage of Retention Sum Retained	11
	2.2.3 Release of Retention Sum	12
	2.2.4 Expenditure of Retention Sum	12
	2.2.5 Valid Instrument of a Retention Sum	13
	2.2.6 Retention Sum and Trust Account	14
	2.2.7 Ownership of Retention Sum	15
2.3	The Rules of Retention Sum in the Construction Industry.	16
2.4	The Calculation of Retention Sum in the Construction Industry.	18
	2.4.1 Retention Sum based on Value of Work Done	19
	2.4.2 Retention Sum based on Retention Limit	20
	2.4.3 Release of First Moiety of Retention Sum	21
	2.4.4 Release of Remaining (Second Moiety) of Retention Sum	22
2.5	The Recent Issue and Prohibition of Retention Sum	22
2.6	Trust in Retention Sum.	
	2.6.1 Trust on Retention Sum under the Trustee Act 1949 (Act 208) 23,24	24
	2.6.2 Trust on Retention Sum under the Trust Companies Act 1949 (Act 100)	25

TABLE OF CONTENTS

	TITLE	PAGE
CHAPTER 2	LITERATURE REVIEW (CONT'D)	
2.7	The Provisions of Retention Sum in Malaysia's Standard Form of Contracts.	
2.7.1	Agreement and Conditions of PAM Contract 2006	26
2.7.2	Agreement and Conditions of PAM Contract 2018	27
2.7.3	CIDB Standard Form of Contract 2000	28
2.7.4	The AIAC Standard Form of Building Contract 2019	29
2.7.5	FIDIC Red Book Conditions of Contract 2017	30
2.7.6	PWD Form 203A (Rev.1/2010)	30
2.7.7	Comparison of Retention Sum Provisions in SFOC	31
2.7.8	Shortcomings of the SFOC in Pertaining to the Recent Issue of Retention Sum	32
2.8	Potential Strategies to Overcome the Recent Issue of Retention Sum in the Construction Industry	
2.8.1	Potential Amendments to the local SFOC on Retention Sum.	33
2.8.2	Legislative Reformation by Referring to Foreign Act on Retention Sum (e.g. The NSW Building and Construction Industry Security of Payment Regulation 2020).	35
2.9	Summary of Chapter	36

TABLE OF CONTENTS

	TITLE	PAGE
CHAPTER 3 RESEARCH METHODOLOGY		
3.1	Introduction	37
3.2	Framing Questions for Review	38
3.3	Identifying Relevant Work	38
3.4	Assessing the Quality of the Study	39
3.5	Summarization of the Evidence	39
3.6	Interpreting the Finding	40
3.7	Legal Research	40
	3.7.1 Doctrinal Legal Research	41
	3.7.2 Non-Doctrinal Legal Research	42
	3.7.3 Comparison of Doctrinal and Non-Doctrinal Legal Research	43
3.8	Literature Review	44
3.9	Research Methodology	
	3.9.1 Stage 1 – Preliminary Study	45
	3.9.2 Stage 2 – Literature Review	46
	3.9.3 Stage 3 – Data Collection	46
	3.9.4 Stage 4 – Data Analysis	49
	3.9.4.1 Thematic Analysis and Content Analysis	49
	3.9.5 Stage 5 – Conclusion and Recommendation	52
3.10	Summary of Chapter	53

TABLE OF CONTENTS

	TITLE	PAGE
CHAPTER 4 DATA ANALYSIS		
4.1	Introduction	54
4.2	Section A: Doctrinal Legal Research	54
	4.2.1 List of Case Laws Selected for Research	56
4.3	Section B: Case Law Analysis	
	4.3.1 Case Law 1	57
	4.3.2 Case Law 2	59
	4.3.3 Case Law 3	60
	4.3.4 Case Law 4	62
	4.3.5 Case Law 5	63
	4.3.6 Case Law 6	64
	4.3.7 Case Law 7	66
	4.3.8 Case Law 8	67
	4.3.9 Case Law 9	71
	4.3.10 Case Law 10	73
	4.3.11 Case Law 11	74
	4.3.12 Case Law 12	76
	4.3.13 Case Law 13	77
	4.3.14 Case Law 14	78
	4.3.15 Case Law 15	80
	4.3.16 Summary of Case Laws Analysed	81
4.4	Section C: To Identify the Issues of the Standard Form of Construction Contracts	86
	4.4.1 List of Analysed Standard Form of Construction Contracts (SFOC)	87
	4.4.2 Issues Identified on Retention Sum in SFOC	87
	4.4.2.1 Issues of SFOC held by Industry Experts	87
	4.4.2.2 Issues of SFOC from Court Case Issues	90
	4.4.3 Summary of Analysed Issues of the SFOC	92

TABLE OF CONTENTS

	TITLE	PAGE
CHAPTER 4 DATA ANALYSIS		
4.5	Section D: To Identify the Legal Position on the issues of Retention Sum	
4.5.1	Thematic Analysis	96
4.6	Summary of Chapter	100
CHAPTER 5 CONCLUSION AND RECOMMENDATION		
5.1	Introduction	101
5.2	Research Outcome	
5.2.1	The Issues on Retention Sum on the Standard Form of Construction Contracts	101
5.2.2	The Legal Position held by the Court on Retention Sum	102
5.3	Limitation of Research	104
5.4	Recommendation	104
5.4.1	To make adjustment/amendments to the current SFOC adopted in Malaysia	105
5.4.2	To enact new legislation by referring to foreign legislation	105
	REFERENCE	109

LIST OF TABLES

TABLES NO.	TITLE	PAGE
Table 1.1	Research Methodology Sequence	4
Table 2.1	The Rules of Retention Sum in Construction Contracts	16
Table 2.2	Comparison of Retention Sum Provisions (Clauses) in SFOC	31
Table 3.1	Comparison of Doctrinal and Non-Doctrinal Research	43
Table 3.2	Example of Case Law Research	47
Table 3.3	Example of Content Analysis for Research	51
Table 4.1	List of Case Laws Selected for Research	56
Table 4.2	Summary of Case Laws Analysed	81
Table 4.3	Table of Retention Sum SFOC Issues from Literature Reviews	88
Table 4.4	Table of Retention Sum SFOC Issues from Court case	90
Table 4.5	Table of Identified Issues of the SFOC	93
Table 4.6	Data Collection and Sub-Coding	97
Table 4.7	Sub-Coding and Main Coding	98
Table 5.1	Proposed Solutions in relation to Foreign Legislation	107

LIST OF FIGURES

FIGURES NO.	TITLE	PAGE
Figure 2.1	Calculation of Retention Sum 1	19
Figure 2.2	Calculation of Retention Sum 2	20
Figure 2.3	Calculation of Retention Sum 3	21
Figure 2.4	Calculation of Retention Sum 4	22
Figure 3.1	Thematic Analysis	50
Figure 3.2	Example of Thematic Analysis for Research	52
Figure 4.1	Findings from Thematic Analysis	96
Figure 5.1	Valid Instruments of Retention Sum	103

LIST OF ABBREVIATIONS

SFOC	-	Standard Form of Contract (or Contracts)
JKR	-	Jabatan Kerja Raya
PWD	-	Public Works Department
PAM	-	Pertubuhan Arkitek Malaysia
AIAC	-	Asian International Arbitration Centre
CIDB	-	Construction Industry Development Board
FIDIC	-	Fédération Internationale des Ingénieurs - Conseils'
NSW	-	New South Wales

LIST OF APPENDICES

APPENDIX	TITLE	PAGE
Appendix A	SK M&E Bersekutu Sdn Bhd v. Pembinaan Legenda Unggul Sdn Bhd & Another Appeal [2019] 2 MLRA	115
Appendix B	Kumpulan Liziz Sdn Bhd v. Pembinaan Ock Sdn Bhd [2003] 1 MLRH	122
Appendix C	ABB Transmission & Distributions Sdn Bhd v. Sri Antan Sdn Bhd & Anor [2008] 1 MLRH.	124
Appendix D	Syarikat Pembinaan Woh Heng Sdn Bhd v. Meda Property Services Sdn Bhd [2002] 5 MLRH.	127
Appendix E	Jaks Sdn Bhd v. Zeta Letrik Sdn Bhd [2021] MLRHU 1375	130
Appendix F	Dna Bentera Sdn Bhd v. Maju Struktur Sdn Bhd & Ors [2021] MLRHY 1122.	133
Appendix G	Pembinaan Blt Sdn Bhd v. Portneka Sdn Bhd [2019] MLRHU 797.	136
Appendix H	Pembinaan Lagenda Unggul Sdn Bhd v. Geohan Sdn Bhd & Another Appeals [2018] MLRAU 59.	138
Appendix I	Demeter O&G Supplies Sdn Bhd v. Datuk Stephen Duar Tuan Kiat (Encl 5) [2021] MLRHU 2319.	148
Appendix J	Yeong Ah Chee v Lee Chong Hai & Anor and Other Appeals [1994] 2 MLJ614.	151
Appendix K	MacJordan Construction Ltd v Brookmount Erostin Ltd [1994] CLC518.	152
Appendix L	Harrington (P C) Contractors Ltd v Co Partnership Developments Ltd [1998] BLR 44.	156

LIST OF APPENDICES

APPENDIX	TITLE	PAGE
Appendix M	Wates Construction (London) Ltd v Franthom Property Ltd [1991].	158
Appendix N	J F Finnegan Ltd v Ford Sellar Morris Developments Ltd [1991] 27 ConLR 41.	159
Appendix O	Rayack Construction Ltd v Lampeter Meat Co Ltd [1979].	163
Appendix P	Plagiarism Report	168

CHAPTER 1

INTRODUCTION

1.1 Introduction

Chapter 1 will start with a brief elaboration of the research. Most importantly to dwell on the research background. The problem statement of the research will also be outlined, thus the research questions will also be described, and imperatively the research objective of this research, there are two research objectives for this research study in pertaining to retention sum. Moreover, this chapter will also briefly touch on the literature reviews, research methodology chosen as well as the data analysis approach to arrive with findings and recommendations of this research study.

1.2 Research Background

The retention sum in construction is a sum retained through the duration of the construction project, by which is retained by the employer of the contract's certified work done, the retention sum is retained based on the contractor's progressive work done in every interim certificates or interim payments, it is retained by the employer from the contractor's work done amount certified in every claims (10% of total work done certified thus subjected to a limit of 5% of contract sum), the purpose of the retention sum is to be substantiated as a security measure for the due performance of the contractor as well as to be secured against the quality of the contractor's workmanship. While the retention sum is retained by the Employer of a project, there is a necessity of trust to be established, under the general standard form of contract in Malaysia, the employer is generally be a fiduciary as trustee for the contract, whereas such beneficial interest shall be subjected only to the right of the employer to have recourse from time

to time for payment of any amount as the contract administrator may certify, in order to established a valid retention sum, there must be further exigency shall be conducted which will be discussed in the following chapter for literature review.

The recent Federal court decision of *SK M&E Bersekutu S/B v Pembinaan Legenda Unggul S/B & Another Appeal (2019) 4 CLJ 590* had somehow reversed the retrospective court decision of *Qimonda Malaysia Sdn Bhd (in liquidation) v Sediabena Sdn Bhd (2012) 3 MLJ 422*, which the Federal court reserved the principal of retention sum that the retention money are not a trust money, thus induces the Contractors/Sub-Contractors as unsecure creditors in the event that the Employer becomes insolvent or goes into liquidation in this period of new normal of economy downturn. This issue concerning the remuneration and release of the retention sum during these trying times as employers and contractors are on the verge of insolvency (Jaspal Singh, 2020), the issues imposed by the Federal court on the recent reversed decision and principal on the retention sum, while the retention sum retained is not defined as a genuine ‘trust’ anymore hence it is merely a contractual debt rather a sum retained designated to the contractor under the contract. While the most enviable approach is to keep the retention sum into a segregated bank account in the joint name of the employer and contractor.

1.3 Problem Statement

The problem is in the event that the employer becomes insolvent, the retention sum will not be safeguarded and it will usually be included for the distribution of payment of debts to the secure creditor rather than the contractor. To put in other way, the retention sum is categoried under the asset of the employer thus is not desginated to the contractor as the rentention monies is retained in the hand of the employer.

Another problem on retention sum is due to the recent Federal Court's decision of *SK M&E Bersekutu S/B v Pembinaan Legenda Unggul Sdn Bhd [2019]* reversed the previous principal in the case of *Qimonda Malaysia Sdn Bhd (in liquidation) v Sediabena Sdn Bhd [2012]*. Whereby the retention is not trust in nature in the absence of clear stipulation in the condition of contract, as well as an effort to segregate the retention sum into a separate trust account.

1.4 Research Questions:

- i) What are the issues of the Standard Form of Construction Contracts in pertaining to Retention Sum?
- ii) What are the current legal positions in relation to the issue related to Retention Sum?

1.5 Research Objectives

- i) To determine the issues related to Retention Sum in construction contract; and
- ii) To determine the legal position in relation to the issues of Retention Sum in construction contract.

1.6 Research Scope

The legal research for this study shall be mainly targeted to the case laws related to Retention Sum for the construction industry. The studies on the standard form of contracts shall only be subjected to the form of contracts adopted in Malaysia.

Meanwhile the case laws adopted for research will only be based on issues concerning Retention Sum in the event that the paymaster goes into liquidation, as well as case laws which decide the valid mechanism of the Retention Sum in the construction industry, The case laws will be relied on both local case laws and foreign case laws (particularly UK case laws) will be adopted. The main purpose on adopting case laws is the acquire findings on the principles concurred by the court regarding the designation of retention sum issues. Thus the legislative and legal aspect in regards to the formulation of retention sum under the law will not be explored in this reasearch.

1.7 Research Methodology

This research is to adopt the doctrinal legal research by review relevant case laws both local and internationaly. The legal research study is able to to determine the factors that is able to determine the consolidation of the cases. Through the legal research method, the main purpose is to determine the principal of law the valid mechanisms of retention sum in the construction industry, as well as to amalgamate all the law principals of the retention sum, then such study are able to identify enviabale solutions for the research problem. In legal research, methods are adopted of which the aim is to identify and explain what the law is by logic, analogy, and deduction, the sources for such an exercise include legislation and case law. The data collection for the relevant case laws will be based on case laws judgement collection. The Research Methodology Sequence of this research is listed as follows:

Table 1.1 Research Methodology Sequence

Phases	Research Program	Achievements
Phase 1 : Initial Stage (Chapter 1)	- Research proposal.	- Define problems, identify establish research objectives, scope, significant of study and research method.

Phases	Research Program	Achievements
Phase 2 : Literature Review (Chapter 2)	<ul style="list-style-type: none"> - Detailed literature reviews to undertake research statement and research questions. 	<ul style="list-style-type: none"> - Review case laws and articles, books, websites on retention sum. - Review relevant legislation implementations. - Conduct theoretical framework for the study.
Phase 3 : Data Collection (Chapter 3)	<ul style="list-style-type: none"> - Doctrinal legal research was used in view of the type of data to be collected. - 	<ul style="list-style-type: none"> - Prepare protocol to assist of the reliability of the study for legal research - Identify at least 15 case laws with are related to retention sum. - Review the selected case laws and identify the court issues, judgement and principles.
Phase 4 : Data Processing & Analysis (Chapter 4)	<ul style="list-style-type: none"> - Determine how to process and analysis the data collected. - Transforming the data collected through Content Analysis and Thematic Analysis. 	<ul style="list-style-type: none"> - Determine an enviable research analysis method for the legal study. - Make evaluation from the case laws reviewed and arrive with the research finding.
Phase 5 : Research Presentation (Chapter 5)	<ul style="list-style-type: none"> - Involve data presentation, findings and results. - 	<ul style="list-style-type: none"> - Arrive with research finding and draw conclusion based on the findings and make recommendations.

1.8 Significant of Study

This study seeks to determine the issues of the Retention Sum of the contractors and sub-contractors involved in construction projects, firstly the study will seeks to determine the issues of Retention Sum in the standard forms of construction contracts available, then to conduct case study to determine the current legal position of Retention Sum in construction industry, what are the rules of forming a valid Retention Sum.

1.9 Research Outline

Chapter 1 will mention on the introduction of the research topic, which also dwell on the background of the study in pertaining to the problem of the issue. Moreover chapter 1 will elaborate regards the problem statements, research questions, and significance of the study, research scope and research methodology of the study. Subsequently, Chapter 2 will focus on the literature review of the issue on retention sum in Malaysia construction industry. The literature review will firstly base on the secondary resources being published articles, books, organization websites write up and case review. The later part of literature review for potential findings will be basing on foreign legislative enforcement or foreign act to derive with findings for the solution of the problem statement. Then Chapter 3 will emphasizes on the research method of the study. The chapter will also elaborate on the requirement of the case law selected for the study, as well as the chosen method to analysis the case laws reviewed including literature reviewed on retention sum issue. Hence the data analysis will be sorted out in the next chapter. Following with Chapter 4 will definitely be analysing the data and information which were attained by adopting the case law study approach. In order to analyses study, both content analysis data analysis method and thematic analysis study will be adopted. Furthermore **Mendeley** will also be used to sort and organize references and literature studies, as well as to decode the information of the literatures and create citings. While all the data analysis in this study will aim to attain the reaseach objectives. Finally Chapter 5 will concludes the outcome and attained from the analysed

data on qualitative approach. Thus this chapter will also provide recommendations of solutions to the problem statement for this research topic.

1.10 Summary of Chapter

The Chapter serves as a guidelines for the entire research project from background of the study which is the current issues on Retention Sum, the problem statement which the Retention Sum is not designated to the contractor in case the employer becomes insolvent, another problem statement which concern on the recent Federal Court judgement which held that the Retention Sum is not trust money in nature. This chapter also listed the research objectives to determine the issues related to Retention Sum in construction contract and the legal position in relation to the issues of the Retention Sum. Also with the significant of study which aims to determine the issues on Retention Sum and to propose possible solutions in the final chapter of the research. Hence the following chapters which is the literature review will provides further theories of knowledge and studies which are relevant to this research project.

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