

**RIGHTS OF CONTRACTORS ON RECOVERY OF PAYMENT
AFTER TERMINATION OF CONTRACT UNDER CIPAA 2012**

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DEDICATION

“To my beloved mother, father, grandmother, and grandfather”

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ABSTRACT

The Malaysia construction industry has suffered from the reputation as being less efficient and prone to conflict, mainly due to the relationship between main contractors and subcontractors. It has been so-called that main contractors have abused their dominant position in the contractual relationship to withhold monies due to the subcontractors by deploying “pay-when-paid” or “pay-if-paid” clause in their contract with the sole purpose of increasing their own profit margins. The conventional forms of dispute resolution (i.e. arbitration and litigation) indirectly turned-down the contractors from further pursuing their rights to recover the remaining payment after terminated their contracts due to non-payment. This is because of the long period taken and rather expensive and the chance to succeed is rather rare. This research attempts to identify the legal rights of the contractor to recover his remaining payment after the termination of his contract under the Construction Industry Payment and Adjudication Act 2012 (CIPAA 2012). CIPAA was became law on 22 June 2012, has provided another option to the forms of dispute resolution in Malaysia. The Act was intended to address payment issues in the construction industry which involves non-payment and delay in payment. The research methodology utilized primary data and secondary data, i.e. law journals, books, conference articles, etc. including a review of a large section of published literature. The findings obtained basically shows that CIPAA allows contractors to terminate their contracts in the event of employer’s failure to pay and the only last resort to recover the remaining payment is through the arbitration or litigation process if employer continue withhold the payment unreasonably. Legal cases decided under CIPAA and supported by cases from a similar Act from United Kingdom which is the first to implement statutory adjudication. The analysis have been referred to nine legal cases, the five cases from United Kingdom had allowed employers to refuse making payment of outstanding amount due upon termination of contract based on certain conditions such as the service of withholding notice,

issuing pay less notice, contractor's insolvency, Liquidated Ascertained Damages and default by the contractor. Whereas the four Malaysian cases analyzed stated the conditions for contractors to recover his remaining payments due in contract upon termination, such as the existence of a valid contract or collateral contract, the jurisdiction of the adjudicator and the correct implementation of adjudication under CIPAA. It is concluded that, under CIPAA, contractor may recover his remaining payment as long as the requisites stipulated in CIPAA is abided as the employer may argue on the conduct of the CIPAA itself.

ABSTRAK

Industri pembinaan di Malaysia memiliki reputasi sebagai kurang cekap dan berisiko menghadapi konflik, terutamanya disebabkan oleh hubungan antara kontraktor utama dan sub-kontraktor. Ia dikatakan bahawa kontraktor utama telah menyalahgunakan kuasa dominan mereka di dalam kontrak untuk menahan bayaran yang sepatutnya diberi kepada sub-kontraktor dengan mengaplikasikan klausa “pay-when-paid” atau “pay-if-paid” yang terkandung di dalam kontrak dengan hasrat untuk meninggikan margin keuntungan sendiri. Bentuk konvensional dalam penyelesaian pertikaian (arbitrasi dan litigasi) secara tidak langsung menidakkan usaha kontraktor untuk mendapatkan hak mereka dalam mendapatkan semula bayaran mereka yang tertinggal selepas kontrak ditamatkan disebabkan tiada bayaran. Ini disebabkan tempoh masa yang lama dan kos yang tinggi dan peluang yang rendah untuk Berjaya. Kajian ini mencuba untuk mengenalpasti hak-hak kontraktor dalam usaha untuk mendapatkan kembali bayaran yang tertunggak selepas penamatan kontrak merujuk kepada “Construction Industry Payment and Adjudication Act 2012 (CIPAA 2012)”. CIPAA telah menjadi undang-undang pada 22 Jun 2012, dan ia telah memberikan pilihan baru untuk menyelesaikan pertikaian di Malaysia. Akta ini bertujuan untuk menyelesaikan isu bayaran di dalam industry pembinaan ini yang melibatkan masalah tiada bayaran dan penangguhan bayaran. Metodologi kajian ini menggunakan data primer dan data sekunder seperti jurnal undang-undang, buku, artikel konferens, dll. termasuk kajian semula kepada sebahagian besar dari tulisan yang telah diterbitkan. Dapatan kajian ini menunjukkan yang CIPAA membenarkan kontraktor menamatkan kontrak di dalam keadaan majikan gagal membuat bayaran dan di mana pilihan terakhir untuk mendapatkan kembali bayaran tertunggak ialah melalui proses arbitrasi dan litigasi jika majikan tetap menahan bayaran dengan tidak munasabah. Kes undang-undang yang diputuskan di bawah CIPAA dan disokong dengan kes-kes berdasarkan Akta yang

serupa dari United Kingdom yang juga Negara pertama yang mengaplikasikan adjudikasi berkanun. Analisis telah dilaksanakan merujuk kepada sembilan kes undang-undang, lima kes diambil dari United Kingdom telah membenarkan majikan menahan bayaran amaun berbaki selepas penamatan kontrak di atas sebab-sebab tertentu seperti pengeluaran notis penahanan, pengeluaran notis pengurangan bayaran, insolvensi kontraktor, “Liquidated Ascertained Damages” dan kelalaian oleh kontraktor. Sementara itu, empat kes undang-undang dari Malaysia yang telah dikaji menyatakan beberapa kondisi kontraktor boleh mendapatkan kembali bayaran tertunggak di dalam kontrak selepas penamatan kontrak seperti kewujudan kontrak yang sah atau kontrak cagaran, jurisdiksi adjudicator dan pelaksanaan adjudikasi dengan betul di bawah CIPAA. Kesimpulannya, dibawah CIPAA, kontraktor mampu mendapatkan kembali bayaran tertunggak selagi syarat-syarat yang ditetapkan di dalam CIPAA ditepati kerana majikan boleh mengemukakan hujahan berdasarkan pelaksanaan CIPAA itu sendiri.

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LIST OF ABBREVIATIONS

AC	Appeal Cases, House of Lords
All ER	All England Law Reports
AMR	All Malaysia Reports
BCISPA (S'pore)	Building and Construction Industry Security of Payment Act 2004 (Singapore)
BCL	Building and Construction Law Cases
BLR	Building Law Reports
CA	Court of Appeal
CIDB	Construction Industry Development Board
CIPAA	Construction Industry Payment and Adjudication Act 2012
Con LR	Construction Law Reports
ER	Equity Reports
IEM	Institution of Engineers Malaysia
ICR	Industrial Cases Reports
ILR	International Law Reports
JP	Justice of the Peace / Justice of the Peace Reports
KLRC	Kuala Lumpur Regional Centre of Arbitration
LDEDCA	Local Democracy, Economic Development and Construction Act 2009.
MLJ	Malayan Law Journal
NSW	New South Wales
PAM	Pertubuhan Akitek Malaysia
PWD	Public Works Department
SC	Session Cases
SCR	Supreme Court Reporter
SO	Superintending Officer
UK	United Kingdom
UTM	Universiti Teknologi Malaysia
WLR	Weekly Law Report

CHAPTER 1

INTRODUCTION

1.1 Background

Before CIPAA¹ was gazetted in 2012, the legal implementation of claims and cross claims is not likely to be immediately resolved but prone to draw in a lengthy trial. Pending decision of the dispute resolution progression, there is normally no security for the claim, which is risky for contractor's cash flow and profitability.²

In most construction contracts of Malaysia, a punctual payment as contained according to the outline agreed in the contract agreement is deemed insufficient to be stipulated as to be of the essence, thus stoppage of payment shall not be deemed to be a breach of which goes to the root of the contract.³ The law of contract dictates that the decline to compensate within the stated period what is outstanding is not deemed sufficient to constitute breach in supporting the unpaid party to determine his own employment.⁴ Employer's decline to pay promptly what is due on another contract shall also not be sufficient to be constituted a repudiatory breach.⁵ Even though delay in payment is not considered repudiatory, a persistent decline in paying shall turn

¹ Construction Industry Payment and Adjudication Act 2012 (CIPAA) (Act 746)

² Lim, CF (2005). The Malaysian Construction Industry - The Present Dilemmas of Unpaid Contractors. Master Builder Journal. 4th Quarter 2005. p.81.

³ Decro –Wall International v Practitioners in Marketing [1971] 2 All ER 216.

⁴ Mersey Steel & Iron Co v Naylor, Benzon & Co (1884) 9 App.Cas.434.

⁵ Small & Sons Ltd v Middlesex Real Estates Ltd [1921] W.N.245.

into repudiation.⁶ Generally, denial to compensate promptly of what is owed under the agreed contract shall not ordinarily be deemed as an adequate breach to explain the unpaid party to determine his employment. Decline to make payment on time of which is outstanding is even less prone to be a repudiatory breach.

Conversely, the Contract Act 1950 by Section 56 indicated that “*if time is essential to the performance of the contract, the contract may be voidable*”. In *Dawnays v Minter*⁷ the court found that employers have to compensate the contractor with the outstanding amount stipulated on an interim certificate excluding any set-off saves for claims either established or liquidated.

Referring to above, it is understood that under the common law, termination is only allowed after contractor has clearly proved that the employer has declined to carry out his duty, or denied, himself from the conduct and his promise entirely.⁸

On the other hand, PAM 2006 form of contract⁹ stipulates under its clauses 26.1 (a) to (d) the conditions for the contractor to determine his employment under the contract. Besides that, CIDB 2000 standard form of contract also consists of clauses of which permit Contractors to determine his employment under the contract upon default by the Employer.¹⁰

Both of CIDB 2000¹¹ and PAM 2006 permit the determination of employment by the contractor upon the occurrence of employer’s decline to compensate. Both of the forms also allow contractor to be compensated with the value referring to the actual work completed to the determination date. The outstanding claim will be reimbursed to unpaid party subsequent to both parties’ agreement at the final account.¹²

⁶ Siti Suhana [2010]. Contractor’s Right Of Action For Late Or Non-Payment By The Employer. Journal of Surveying, Construction & Property. Vol. 1 Issue 1 2010. p.92

⁷ [1971] 1 WLR 1205.

⁸ Siti Suhana. Supra 6. p92.

⁹ Pertubuhan Akitek Malaysia (PAM) - Standard Form of Building Contract 2006 form.

¹⁰ Clause 45.1 Determination by Contractor with Notice.

¹¹ Construction Industry Development Board - Standard Form of Building Contract 2000 form.

¹² cl. 26.4(b) of PAM 2006 form and cl. 45.3(b) & (c) of CIDB 2000 form.

PWD 203A¹³ form of contract does not have any clause stipulating that the government declining to make payment shall allow contractors in terminating his own employment under the contract. PWD 203A (Rev. 1/2010) under clause 55(a) only stipulated “*if the government without any reasonable cause fails to perform of fulfil any of its obligations which adversely affects the Works*”. The term “*Obligations*” in the provision does not signify non-payment to be allowing the contractor to terminate his own employment. The provision carries the meaning that, once the issue of non-payment by the employer is faced by a Contractor, he can refer his problem into the statutes or the common law.¹⁴

The right to determine a contract due to non-payment is regarded as a settled-law under the provisions on payment in standard form of contract,¹⁵ the right involves that, inter-alia, in common law shall only be applied if the act of non-payment is not stated either in the standard form of contract or the earlier law cases.¹⁶

Nevertheless, in the real construction project, the possibility of recovering an outstanding payment upon determination of employment under a contract is improbable due to the employer’s inclination to disagree at the final account phase by lagging on the agreement of the amount of payment for the contractor. It would be even worse if the employer refuse to pay totally and even making counterclaims from the contractor. Consequently, the disputing parties may only proceed the issue in arbitration or litigation which is the last option in solving disputes. In these circumstances, contractors would be the one who suffered most from the dispute.

Countries under the common law province such as United Kingdom,¹⁷ Australia,¹⁸ Singapore¹⁹ and New Zealand²⁰ have initiated the concept of statutory adjudication

¹³ Public Works Department under Malaysian Ministry of Works - Standard Form of Building Contract 203A form (Rev.1/2010).

¹⁴ Siti Suhana. Supra 6. pp87.

¹⁵ The act of adjusting or determining the dealings or disputes between persons without pursuing the matter through a trial.

¹⁶ Siti Suhana. Supra 6. pp92.

¹⁷ United Kingdom, Housing Grants, Regeneration and Construction Act 1996.

¹⁸ Australia New South Wales State, Building and Construction Industry Security of Payment Act 1999

¹⁹ New Zealand, Construction Contract Act 2002

to the construction industry to address payment disputes and Malaysia is going along with the practice. In Malaysia, another form of statutory security of payment legislation known as Construction Industry Payment and Adjudication Act 2012 (CIPAA) (Act 746) has eventually been gazetted at 22nd June 2012. The main aim of the CIPAA is to focus on the issues of cash flow in the Malaysian construction industry.

It cancels the exercise of conditional payment (pay when paid, pay if paid and back to back) and decreases payment default by designing an inexpensive and faster mechanism of dispute resolution in the structure of adjudication. Adjudication is devised to be an easy and productive process that endorses the pay now, argue later policy.²¹

CIPAA specifies for recovery of payment after the adjudication process has come to a solution²² and it further stipulates the terms of payment default to facilitate situations of the absence of provisions to that effect in the applied construction contract.²³ CIPAA is applicable to every construction contract agreed in writing and relative to construction projects conducted entirely or partially in the country of Malaysia.²⁴ Thus, a statutory right has been generated to help contractors recover their outstanding payment for the works done.

Statutory adjudication is basically an adjudication process stipulated by CIPAA. It is carried out in private and the confidentiality is ensured and it is a compulsory and statutory procedure that does not involve agreement of the parties' to begin the course and predominates over any contractual agreements in contrast between the contracting parties. CIPAA delivers a moderate, cost-saving and quick progression of

²⁰ Singapore, Building and Construction Industry Security of Payment Act 2005.

²¹ Section 35 of CIPAA.

²² Section 28 of CIPAA.

²³ Section 36 of CIPAA.

²⁴ Section 2 of CIPAA.

dispute resolution if compared to arbitration or litigation by the feature of express provisions advocated by the CIPAA.²⁵

CIPAA offers a different and new dispute resolution mechanism via statutory adjudication practice which is faster and inexpensive than arbitration and litigation and it shall be initiated at any time while the contract period is on-going. Thus, for the contractors that have determined their employment under construction contracts and desire to recover their outstanding payment that is being denied by the employers who are ordinarily arguing and vexatiously delaying the final account may elect to pursue the resolution under CIPAA.

1.2 Problem Statement

Sir William Anson as in Ashworth defined a contract as been made when there is a legally binding agreement between two or more parties, by which rights and duties are attained by one or more to acts or forbearances on the part of the other or others.²⁶ Termination of construction contracts commonly occurs in construction industry and usually has serious implications on the project. The employer may terminate the contractor who fails to perform according to the contract; conversely, a contractor may also terminate a construction contract of which has not been remunerated according to what was agreed in the contract.

Termination of contract occurs at a point in time in the progression of a contract period when a legally binding contract is taken to an end before performance due to the acts of one or both parties has been completely discharged.²⁷ The right to terminate a contract rests on the type and the outcome of the other party's breach. In standard form of building contract, they have listed down the procedure to determine a contractor's employment and to terminate a contract. They also have clearly stated

²⁵ Kuala Lumpur Regional Centre of Arbitration (2012). Adjudication [Brochure]. Kuala Lumpur: KLRCA.

²⁶ Allan Ashworth. (2001). Contractual Procedures in the Construction Industry. 4th Edition. Pearson

²⁷ John Wong. (2005). Terminated or be Terminated. The Malaysian Surveyor. 39.1. Page 12

several events of default which may permit an employer or contractor to terminate a contract.

There are a few standard forms of contract available in Malaysia, such as PAM 2006, PWD 203A, IEM, and CIDB 2000. In every standard forms of contract, there are clauses stipulated for the determination of contract. In PAM Contract 2006, Clause 25.2 explained the procedure for employer to determine contractor's employment and Clause 26.2 explained the procedure for contractor to determine his own employment. PWD Form 203A (Rev. 1/2010) on the other hand, has given an idea about the events of default that activates the right of the innocent party to terminate the contract. In PWD Form 203A (Rev. 1/2010) also has provided the clause for termination in the event of general default by contractor such as when the contractor becomes bankrupt and insolvent.

Although the PWD Form 203A (Rev. Rev. 1/2010) does not contain any clause that gives the contractor the right to determine his own employment, this does not mean the contractor has no such right under the law of contract. The contractor can always refer to the Contract Act 1950 and common law principle of repudiation under breach of contract.

Some problems in the construction industry such as insufficient monetary strength, huge time phase, high price of the current dispute resolution systems, and the imbalance in bargaining capacity between construction parties have led to unwanted manipulation. These complications bring detrimental consequences to the construction industry, purchasers and critically the economy. Subcontractors becoming insolvent and vacated projects are just some of the many concerns.²⁸

The establishment of Construction Industry Payment and Adjudication Act 2012 (CIPAA) reflects a substantial improvement in the Malaysian industry of construction. Upon this occasion, the government and stakeholders participating in

²⁸ Raymond Mah, *Construction Adjudication in Malaysia – Faster and Cheaper Dispute Resolution*, Asian Legal Business, 2016.

the construction industry anticipate major advancements to cash flow and payment disputes inside the construction industry which would bring about less delays and abandoned projects, in addition to a better quality of properties and production of more reasonable prices. As stated in CIPAA, its focuses are to facilitate regular and timely payment, to provide a mechanism for speedy dispute resolution through adjudication, to provide remedies for the recovery of payment in the construction industry and to provide for connected and incidental matters.²⁹

The process of arbitration and litigation is time consuming and incurs higher cost compared to adjudication, which is why most unpaid parties chose to recover outstanding payment by adjudication and consider arbitration and litigation as applied only at the last chance.³⁰ Furthermore, adjudicator's determination is binding, which means that the successful party may seek enforcement of the determination by requesting to the High Court for an order of enforcement towards the adjudication decision.³¹

Section 5(1) of CIPAA states "*An unpaid party may serve a payment claim on a non-paying party for payment pursuant to a construction contract*". However, CIPAA 2012 does not contain any section describing the period of payment for those claims were to be made. Moreover, Section 7(2) of CIPAA specifies "*The right to refer a dispute to adjudication shall only be exercised after the expiry of the period to serve a payment response as specified under subsection 6(3)*". The vital sentence extracted from Section 7(2) which is "*shall only be exercised after the expiry of the period to serve a payment response*" states that whichever non-paying party (employer) that fail to serve payment response subsequent to the service of payment claim is considered to be an act of dispute to the payment claim, enabling the unpaid party to begin adjudication process.

The major issue that the author intends to address is that CIPAA does not specify whether the unpaid party is entitled to serve payment claim to the non-paying party

²⁹ Ibid.

³⁰ Yap. E. My Say: Will the CIPA Act Improve Payment Practises? The Edge. Commentary. 2012.

³¹ Section 28(1) of CIPAA.

to recover the remaining payment outstanding or due to him in the occurrence after he has terminated the contract by implementing his rights under their construction contract's self-determination provision. The motive of serving payment claim to the non-paying party is to save his right to start the adjudication in the occurrence of the non-paying failing to serve the payment response.

This issue escalates to a number of significant probes:

1. Whether the unpaid party can serve a payment claim under CIPAA subsequent to termination of contract?
2. Is there any provision under Security of Payment Regimes in other countries that permit the contractor to serve payment claim / refer to adjudication following termination of contract so as to recover his outstanding payment?

Based on the above discussion, this research therefore looks into the legal stance of the unpaid party (contractor) in recovering his outstanding payment that is withheld by his employer after the termination of his contract.

1.3 Objective

To investigate on the legal right(s) of the contractor as an unpaid party/claimant to recover outstanding payment after termination of contract under CIPAA 2012.

1.4 Research Scope

The approach implemented in this study is case law based. The applicable legal cases are restricted to those contained in Malaysia Law Journal (MLJ) and accessible in the databank of Lexis Nexis website. Furthermore, this study has been conducted based on the relevant provisions in Standard Forms of Construction Contract utilised in Malaysia which are PAM 2006, PWD 203A (Rev. 1/2010), CIDB 2000 and other provision under Common Law.

To analyse the statutory payment regime, this research will be examining the Construction Industry Payment and Adjudication Act 2012 of Malaysia. Due to the new development of statutory adjudication in Malaysia, the study examined statutory payment regime in a common law jurisdiction which is the United Kingdom (UK). The selection of the statutory payment regime in UK is that it was the first adjudication Act developed and the Malaysian legal system is in the province of the common law.

United Kingdom's HGCRA 1996³² has been revised by the LDEDCA 2009³³ and the modified act must be obeyed with by all construction contracts entered on or after the 1st October 2011. The alterations to the HGCRA 1996 brought together by the LDEDCA 2009 are not retrospective and the HGCRA 1996 will remain applicable as it was prior to amendment in respect of construction contracts entered into before 1 October 2011. Hence, this study is still concentrating on both HGCRA 1996 and LDEDCA 2009.

The scope of this research will be concentrated on legal position of the parties post-termination of contract as referred to contractual provision and statutory provision.

1.5 Significance of Study

Nowadays, most of the parties in the construction industry such as the main contractor or sub-contractor are generally faced with the problem of termination of construction contract. So, it is strongly believed that this research can bring a lot of benefits to those contractors who face problems in the termination of construction contract.

The goal of this study is to build-up the knowledge of both contractors and employers relative to the issue of termination of contract in the construction industry. The results of this research can also provide an enhanced comprehension for the

³² Housing Grants, Construction and Regeneration Act 1996

³³ Local Democracy, Economic Development and Construction Act 2009.

contractors and employers in regards of their legal positions in the case of construction contract termination.

Moreover, this research is essential as it delivers a basic guideline to those individuals or parties who are involved in the construction industry. This study also helps to raise awareness of contracting parties concerning the legal stance of their rights after a termination. Typical contractors believed that they are entitled to recover their outstanding claims by statutory adjudication which offers faster, inexpensive, and more convenient method of resolution of dispute in contrast with arbitration and litigation and this choice is to preserve a good contractual bond between the parties in the contract.

1.6 Research Methodology

In the effort of accomplishing the objective of the study, an efficient procedure of conducting the study is needed. The designated methodology is allocated into several important steps as shown below.

First of all, an early literature review is imperative to acquire the overview of the conception of this issue. Conversations with course mates, supervisor and lecturers are required so that more knowledge and ideas relative to the issue can be gathered. The issue and statement of problem in this study have been gathered by reviewing journal, cases, articles, books, and magazines. Meanwhile, objective of this study has been produced upon distinguishing the issue and problems.

The following step is data collection. Subsequent to the identification of research issue and objectives, numerous documentation and literature review relative to the research field have been gathered to accomplish the objective.

Normally, primary data can be brought together from Malayan Law Journals and other law journals via UTM Online Databases, e-Journals & e-Books, mainly Lexis-

Nexis Legal Database. The secondary data consist of articles, seminar papers, books and also reports from online database on the construction contract law. These sources are essential in the development of the literature review chapters.

Afterwards, the author have analysed the overall cases gathered, information, judgments, ideas, views and comments. These will comprise of the case law on the relative court cases. The assessment has been carried out by revising and refining all the facts and details of the court case. The last phase of the study procedure majorly contained the writing up and presentation the research outcomes. Researcher would also revise the entire progression of the study with the purpose of ensuring the accomplishment of the objective of the study. Conclusion and recommendations for future research have been prepared based on the results acquired from the analysis.

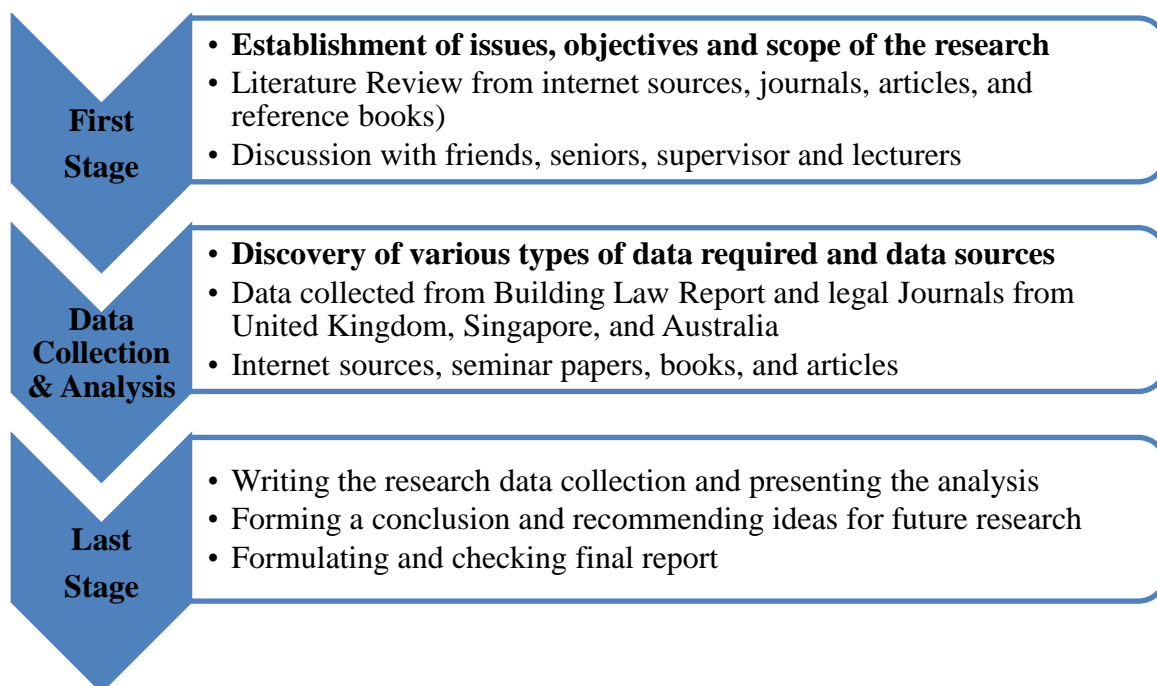


Figure 1 Flow chart of research methodology

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