



Building and Construction Industry Security of Payment Amendment (Retention Money Trust Account) Regulation 2015

April 2015

This latest amendment is designed to secure subcontract retention amounts by requiring head contractors to place subcontract retention money into a trust account, for projects with a value of \$20 million or greater. The Regulation commences on 1st May 2015, and applies to projects where the head contract was entered into after that date.

Projects Included

The Regulation applies to projects with a head contract value of \$20 million or greater. The Regulation does not state that this amount is excluding or including GST, so I have assumed that it is the GST inclusive value. Therefore the Regulation applies to projects with a net head contract value of \$18,181,818 or greater.

However, there may be an alternative interpretation of this, since the Regulation states that '*The value of a construction contract is the amount of consideration that the contract provides is payable for construction work carried out*,' and since GST is not consideration for construction work, then the \$20 million could be taken as the value before GST. It is probably safer to use the first interpretation.

What happens when a contract value is varied?

If a project with an initial value **less** than the threshold, subsequently increases to a value greater than the threshold by reason of approved head contract variation additions, then from that time forward, the Regulation applies to the project, **but only in respect of sub-contacts entered into after the project value reached the threshold**. Thus, a head contractor could have a project where some subcontractors' retentions are not to be included in the trust account, but others are to be included.

Consider a circumstance where we have a project with a value less than the threshold, and we have several sub-contracts in progress, and each subcontractor has received several payments with retentions deducted. The project now has variations and the value increases beyond the threshold. If we make further payments to existing subcontractors, there is apparently no requirement to place the further retentions in trust (**'only in respect of sub-contacts entered into after the project value reached the threshold'**). However, any new sub-contracts would have their respective retentions placed in trust.

Equally, and the Regulation is silent on this point, could we assume that if a project with an initial value **greater** than the threshold, subsequently reduces to a value less than the threshold by reason of approved head contract variation deductions, then from that time forward, the regulation no longer applies to the project.

It would be logical in the case of subcontracts on this project, to withdraw the retentions from the trust account and transfer back to the operating account.

Trust Accounts

The head contractor must establish one or more trust accounts. These may be –

- A separate account for each subcontractor,
- A separate account for each project, or
- One account for all subcontractors and all projects.

Since an account review report and a fee of \$1,500 is payable each year for each account, I believe that most if not all head contractors will opt for the single account.

Trust Account Requirements

- The trust account(s) must be established with an authorised deposit-taking institution (ADI),
- The ADI must be notified in writing that the account is a trust account required by the Regulation,
- The name of the account must include the name of the head contractor and the words "Trust Account",
- The head contractor must notify the Chief Executive (of the Office of Finance and Services) within 14 days of establishing the account, and providing:-
 - The name of the ADI and branch or BSB
 - The number and the name of the account('*head contractor* Trust Account')
 - The opening account balance.

Interest Earned on Trust Accounts

The Regulation states that interest earned '*is to be held on the same trust as the retention money and dealt with accordingly*' unless the subcontract provides otherwise. Presumably, the word '*accordingly*' indicates that the interest accrues to the subcontractor.

It would seem therefore that subcontract documents should now be revised to provide that the subcontractor has no entitlement to any interest – as is the current status.

The calculation of the value of interest attributable to each subcontractor would involve substantial calculation.

What is the Procedure for Managing these Retentions?

The Regulation applies practically at the subcontract level and not the project, as described above. A head contractor will need to identify (and flag) all the subcontracts to which the Regulation applies. As each payment is made and retention deducted, it will be necessary to make periodic transfers of the amounts to the retention trust account.

The accounting system will need to report based on the subcontracts flagged as applicable for the trust account and showing the value of retention by subcontractor, by project. The amount in the trust account may then be 'topped-up' (or reduced) to the required total balance (not including any interest received).

When to Transfer Retention to the Trust Account

The Regulation is silent on all aspects of timing. The wording is simply that a head contractor is to hold the money in trust.

So our question is, what would we interpret as a reasonable time? The reconciliation will not be a simple process and a monthly adjustment and reconciliation would seem to be too onerous.

An annual reconciliation and adjustment prior to year-end, would appear to comply with the Regulation and in my view, this is a serious flaw in the drafting of the Regulation. Perhaps if the reconciliation and any transfers were to be done quarterly, this would be a reasonable compromise.

Withdrawals from the Trust Account

Paragraph 8 of the Regulation provides that withdrawals may be made *'for the purposes of the payment of money in accordance with the terms of the contract.....'* This would appear to cover a withdrawal by the head contractor to reimburse the operating account after a retention release to the subcontractor, and also to reimburse the head contractor when a subcontract retention amount has been used to rectify defects after the failure of the subcontractor to carry out the rectification.

This view is confirmed by paragraph 4, Definitions, which states *'If the head contractor becomes entitled to money held as retention money, the money ceases to be retention money and the requirement under this part that the money be held in trust for the subcontractor in a retention money trust account ceases'*.

Head contractors may also like to consider the case of a subcontractor failing to claim all or part of their retention. In order to comply with the Regulation it would be necessary for the head contractor to establish a right to this money. **That is likely to require a change to the subcontract conditions to provide a time limit for the lodging of the subcontractor's final claim under the subcontract.**

Records

As would be expected, head contractors are required to keep records of the amounts deposited into or withdrawn from the trust account. These records are to be kept for a period of not less than three years

The Chief Executive (of the Office of Finance and Services) may require specific information of a head contractor, sub-contractor or ADI at any time.

Annual Report and Supporting Statement

Head contractors are required to submit an annual report as follows:-

- The report is required by 30th September (3 months after financial year-end),
- The report is an **account review report** prepared by a registered company auditor,
- Pay a fee of **\$1,500** (per report),
- Provide a retention account statement, in the form mandated.

The retention account statement is to show the following,

Head contractor:	Name
ABN:	ABN
Date of account review report:	Date
Trust Account name:	Name
Name of approved ADI:	Name
Date account opened:	Date
Total retention money paid out of account during audit period:	\$ (i)
Total retention money held in account at end of period:	\$ (ii)

Subcontractor	ABN	Full Retention amount retained from subcontractor	Retention amount paid to subcontractor during audit period	Retention amount held at end of period
Subcontractor name	Subcontractor ABN	Presumably this is the value of retention which was deducted during the subcontract, when at its maximum. (iii)	Retentions released during the financial year.	Current retention balance at end of year. (iv)

Notes:

- This will be the total amounts paid to subcontractors, and will exclude any interest received which has been transferred to the head contractor's operating account. This figure will not necessarily match the total bank credits.
- Total retention held could be deemed to exclude any interest received (interest is not retention).
- Full retention amount retained may have been achieved in a prior year.
- The retention balance is not necessarily the account balance (interest added is not retention).

The last column (retention amount held) will not necessarily be the 'full retention amount' less retention amount paid during the period'. Eg. In the prior year, the retention reaches its maximum, and part is released at practical completion. In the current year, the subcontractor has not yet claimed the balance of retention.

Penalties

Penalties for not complying with any requirement are set at 200 penalty units currently equal to \$20,000