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## Security of Payment Legislation and Set-Off Under Commonwealth Insolvency Laws

*Australia Energy, Infrastructure and Resources Alert*

*By Jenny Mee, Sandra Steele, Jason Opperman and Jemimah Roberts*

A recent Victorian Supreme Court case has clarified the impact of Commonwealth insolvency set-off provisions on State-based security of payments legislation.

The case demonstrates that although a principal is generally precluded from relying on a set-off or counterclaim in certain contexts under the *Building and Construction Industry Security of Payment Act 2002 (Vic)* (BCISP Act), due to the operation of section 553C of the *Corporations Act 2001 (Cth)* (Corporations Act), this does not apply if the claimant is in liquidation.

The case also provides useful commentary on what is considered a 'payment schedule' for the purposes of the BCISP Act.

### Background

*Façade Treatment Engineering Limited v Brookfield Multiplex Construction Pty Ltd*<sup>1</sup> involved a dispute between an insolvent plaintiff subcontractor (Façade) and a respondent contractor (Multiplex). The parties entered into a subcontract on 7 September 2011 for the design, supply and installation of façade and curtain wall works. Façade submitted two payment claims to Multiplex (Payment Claim No 18 and Payment Claim No 19) in compliance with the requirements of a valid payment claim under section 14 of the BCISP Act.<sup>2</sup> Multiplex did not pay any of Payment Claim No 19, and only paid part of Payment Claim No 18. On 6 February 2013, Façade was ordered to be wound up in insolvency and placed into liquidation.

An issue arose regarding the parties' entitlements in respect of amounts owed in these circumstances:

- Façade argued that it was entitled to seek judgment in respect of the unpaid amounts pursuant to section 16 of the BCISP Act. Under section 16(2)(a)(i), where a payment claim has been validly submitted and no payment is made or payment schedule served in response, the claimant may recover the unpaid portion of the claimed amount as a debt. Façade alleged that Multiplex had not provided any payment schedules in response to either Payment Claim No 18 or Payment Claim No 19.
- Multiplex argued that it had significant counterclaims against the insolvent subcontractor and was entitled to set these off against the contractor's entitlements pursuant to section 553 of the Corporations Act. This section provides for a statutory set-off scheme between insolvent companies and their creditors.

<sup>1</sup> [2015] VSC 41.

<sup>2</sup> Under section 14(2), a payment claim must (a) be in the relevant prescribed form (if any); (b) contain the prescribed information (if any); (c) identify the construction work or related goods and services to which the progress payment relates; (d) indicate the amount of the progress payment that the claimant claims to be due; and (e) state that it is made under the BCISP Act.

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This raised a number of issues for the court to consider.

### Conflict Between Corporations Act and BCISP Act?

A key issue in this case was the interaction between the Victorian BCISP Act and the Commonwealth Corporations Act.

- Section 16(4)(b) of the BCISP Act expressly prohibits a defendant in section 16(2)(a)(i) proceedings from bringing any cross-claim or raising any defence in relation to matters under the parties' subcontract in the proceedings.
- By contrast, section 553C of the Corporations Act provides for a statutory set-off of opposing claims where there are "mutual credits, mutual debts or other mutual dealings" between an insolvent company being wound up and a creditor.

Justice Vickery considered that there was a conflict between these two sections, as allowing a company in liquidation to recover entitlements under the BCISP Act regardless of the existence of set-off or counterclaim would "fly directly in the face of the scheme established by section 553C of the Corporations Act".<sup>3</sup>

In such circumstances, it was held that section 109 of the Commonwealth Constitution operated to resolve the tension between the Commonwealth and State Acts. Under this section, where a law of a State is inconsistent with a law of the Commonwealth, the latter (in this case, the Corporations Act) shall prevail to the extent of the inconsistency.

This meant that Multiplex was able to rely on the statutory set-off scheme contained in section 553C of the Corporations Act, despite the fact that this was not permitted under the Victorian security of payments scheme. As such, Façade (ie an insolvent company to which section 553C of the Corporations Act applied) was precluded from:

- entering judgment pursuant to section 16(2)(a)(i) of the BCISP Act
- relying on section 16(4)(b) as a bar to Multiplex bringing a cross-claim or raising a defence by way of set-off.<sup>4</sup>

### Notice of Insolvency: Section 553C(2) of the BCISP Act

Notwithstanding the above, Façade argued that even if this was the case, Multiplex was precluded from claiming the benefit of set-off under section 553C because of its knowledge of Façade's insolvency.

Under section 553C(2) of the Corporations Act, a person may not claim the benefit of a set-off if that person had 'notice' of the fact that the company was insolvent at the

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<sup>3</sup> See para [80].

<sup>4</sup> See para [85]. Note, however, that the Court stated (at para [84]) that this position may be different where a defendant evinces an intention not to proceed with its foreshadowed counterclaims (either expressly, or by letting further and inordinate time pass without taking steps to prosecute these claims). In this event, Vickery J considered that it would be open to a plaintiff to seek appropriate declaratory relief before proceeding to enter judgment under section 16 of the BCISP Act.

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time of "giving credit to the company, or at the time of receiving credit from the company".

In considering this question, the court had to determine the appropriate time at which notice of insolvency for the purposes of section 553C(2) should be assessed.

- The subcontractor submitted that the relevant date for the operation of section 553C(2) was the time when the contractor (Multiplex) was liable under the BCISP Act to pay the payment claims.
- By contrast, Multiplex submitted that notice should be assessed as at the date of entry into the subcontract.

After reviewing the relevant authorities, Vickery J agreed with the latter approach, holding that any notice of knowledge of Façade's insolvency on the part of Multiplex should be considered as at the date the subcontract was executed.<sup>5</sup> As there was no suggestion that Façade manifested any signs of insolvency at this date, or that any such signs came to the attention of Multiplex, section 553C(2) did not operate to preclude the set-off proposed to be advanced by Multiplex.

### Payment Schedules

The case also provides useful guidance on what constitutes a valid payment schedule for the purposes of section 15 of the BCISP Act. It was common ground that Multiplex did not serve a valid payment schedule in respect of Payment Claim No 18. However, on 5 October 2012, Multiplex sent Façade an email responding to Payment Claim No 19, advising that it considered Payment Claim No 19 to be invalid. Multiplex argued that this document satisfied the requirements of a payment schedule under section 15 of the BCISP Act.

Façade argued that the email could not constitute a payment schedule for the purposes of section 15, as:

- on its face, it did not purport to operate as a payment schedule
- the email did not indicate the amount of the claim, if any, it proposed to make (contrary to what it argued was prescribed by section 15(2)(b) of the BCISP Act). Section 15(2)(b) relevantly provides that "[a] payment schedule ... must indicate the amount of the payment (if any) that the respondent proposes to make (the *scheduled amount*)".

However, Vickery J rejected this approach stating that it was clear from the email that Multiplex did not propose to pay anything in respect of Payment Claim No 19. His Honour considered that a proposal to pay 'nothing' or 'nil' or 'zero' in a response to a payment claim is 'an amount' for the purposes of section 15(2)(b), as it was clear that they were proposing to pay less than the claimed amount. In reaching this conclusion, Vickery J noted that the courts have long recognised that the requirements of the security of payments legislation, including section 15 of the BCISP Act, should "not be approached in an overly technical manner".<sup>6</sup>

<sup>5</sup> See para [98].

<sup>6</sup> See paras [29] onwards.

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### *Prescribed Forms?*

In considering the above, Vickery J noted that the Victorian Building Authority has not taken the step of prescribing any forms for use in providing payment schedules (as contemplated by section 15 of the BCISP Act). His Honour observed that if there had been such a prescribed payment schedule form in existence, "no doubt the present issue in the proceedings would not have arisen and the parties would have been saved the costs of litigating the matter".<sup>7</sup>

His Honour referred to initiatives of other bodies in developing payment claim forms for use under the security of payments legislation, noting that a "similar initiative could also readily be taken in Victoria to develop forms for payment schedules under s 15 of the BCISP Act".<sup>8</sup>

### Implications

Accordingly, parties to construction contracts should be aware that Commonwealth insolvency provisions, triggered in the event that one party to a construction contract goes into liquidation, may have the effect of overriding the regime that would otherwise apply under the relevant State's security of payments legislation.

Specifically, in circumstances where a BCISP Act claimant is in liquidation, a respondent will be able to rely upon the benefit of set-off contained in section 553C of the Corporations Act (subject to limitations regarding notice contained in section 553C(2)).

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<sup>7</sup> See para [26].

<sup>8</sup> See pars [26] and [27].

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