Project and Statutory Trusts

Position paper

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Project and Retention Trust Accounts

Security of payment laws in Australia vary between the States and Territories. This paper is a high-level overview of mandatory project bank / trust accounts and statutory retention trusts.

Trust accounts on construction projects aim to improve security of payment for subcontractors and protect payments from insolvencies that may occur higher in the contracting chain.

However, there is little evidence this will be achieved and the root causes of poor payment practices do not appear to be addressed by project bank/trust accounts. Further, the costs of project bank / trust accounts outweigh any benefits.

Government contracts and project bank accounts

Western Australia is an example of project bank accounts mandated by government procurement processes. The UK government also introduced project bank accounts on government projects, however it appears project bank accounts are not implemented as widely on UK government projects as may have been expected after publication of the UK Playbook[1]

Contractual project bank accounts are mandated through government policy and contractual provisions, typically required on government projects over a certain value. Project bank accounts require a deed of trust to be entered into, and one party, typically the head contractor, establishes an account where payments are held in trust for certain subcontractors and suppliers. If set up correctly and all necessary steps taken, the funds in the project bank account may be protected from other creditors in the event of a principal's insolvency (unlikely to occur on government projects).

The project bank account regime in WA applies so that the head contractor and chain of subcontractors to be paid simultaneously – therefore achieving a much faster cashflow for the subcontracting network. Under the WA scheme, subcontracts with a value over $20,000 will be part of the scheme and others can opt in.

Under the WA scheme issues can arise where the contractor views a claim as valid and the client has not signed it off as a valid claim, meaning the contractor must "top up" or pay the over cost outside of the Project Bank Account.

Government contracts set the contractual terms for project bank accounts and provide template documents. The head contractor is required to provide a payment instruction to

[1] https://www.theconstructionindex.co.uk/news/view/project-bank-account-usage-not-being-monitored-by-government

the principal’s contract administrator each month (payment cycle) setting out how much each participating subcontractor and supplier is to be paid.

This approach aims to achieve faster payments for the subcontracting network and protects subcontractors from a head contractor insolvency in that payments determined as owing will be paid simultaneously with the head contractor receiving payment.

However, it does not address poor payment practices such as lengthy payment timeframes by the client (where permitted), or a failure to assess variations and other claims in a timely manner by the client or head contractor.

Further, as a government policy approach, project bank accounts will apply to government projects only, where typically subcontractors are paid in a timely manner.

Statutory project trust accounts

Queensland is the first jurisdiction to legislate project trust accounts (called project bank accounts in 2018 and applying to government projects, before legislative amendment to the current project trust account scheme), although it has been considered by other jurisdictions.

The statutory regime operates in a phased approach from the initial government projects to ultimately applying to all private and public sector building projects over $1 million from 2023.

Under the Queensland scheme, head contractors will be required to set up a project trust account for each project that meets the threshold requirements, as well as a retention trust account for cash retentions. The head contractor must pay eligible subcontractors – and only “eligible” subcontractors, as beneficiaries – from the trust account. If there are insufficient funds to pay everyone who is owed a payment, the head contractor must deposit funds into the trust account to make the payments. The head contractor cannot pay itself if there is an amount owing to a subcontractor.

The aim of the statutory regime is to protect the money in the account in the event of head contractor or client insolvency. However, as with project bank accounts, this scheme does not address contractual payment terms, delays in assessing variations and other claims in a timely manner by the client or head contractor, or non-compliant payment claims. The root causes of poor payment practices and insolvencies, including the adversarial nature of lump sum contracts passing all risk to the contractor, along with a ‘lowest cost at the tender box’ approach, both of which drive a culture of claims, are not addressed.

Statutory retention trust accounts

Legislated retention trust structures exist in a number of jurisdictions including NSW, WA and Qld.

These require cash retentions to be paid into a separate trust account and held on trust for the applicable subcontractor. The intent is for those higher in the contractual chain to not use retention money as working capital, on the basis that money does not ‘belong’ to the higher party unless a contractual right exists (for example rectification of defective work).

Some regimes will roll out ‘cascading’ retention trust accounts so that all eligible parties in the contractual chain holding cash retentions will hold those on trust.

The notion of a statutory trust for retention money has merit. However, they can lead to a push for non-cash security (such as bank guarantees) to avoid the requirement to open a trust account, which are not always available for smaller subcontractors. It is also an additional administrative burden and cost for larger contractors who may need to keep trust account records across a number of entities and projects, with little evidence those contractors fail to return retention pursuant to the contract.

ACA Position

Project trust accounts / project bank accounts are a blunt instrument for a complex problem. The cause of the problem has received insufficient analysis for the cost and complexity imposed on head contractors. Due to this cost and complexity, it can be cost-prohibitive for smaller head contractor entities to establish and comply with the requirements and adds pressure to the already tight margins experienced in the industry.

It is submitted that project and retention trust accounts do not accurately target the problem they aim to resolve, and do not address the underlying causes of poor payment practices or industry insolvencies.

The ACA believes security of payment concerns are best addressed by treating the underlying causes and incentivising the right behaviours.

Changing the culture of the industry is an essential step to changing payment practices. Intertwined with this, risk allocations and contractual frameworks must be re-assessed to drive the desired behaviours, and project teams must have the knowledge and skills to effectively work collaboratively. Consistent adoption of technological advances will increase cashflow and industry-wide productivity.

Improving cashflow on projects would result in micro and macroeconomic benefits to the industry. Poor cashflow is largely fuelled by the 'industry norm' of paying contractors progressively (often with lengthy timeframes) following completion of certain work or milestones, an issue that is not improved by mandatory project bank / trust accounts and statutory retention trusts.

This reinforces the three pillars of a sustainable industry for which the ACA advocates: namely, positive industry culture, equitable and aligned commercial frameworks and sufficient capability, capacity and skills.

As a means of achieving the needed industry reforms, ACA encourages the adoption of collaborative contracting frameworks, appropriate allocation of risks, adoption of the Culture Standard[2], developing skilled leaders at all levels of the industry and a reconsideration of 'value for money' beyond the lowest up-front price. These measures will go a long way to address concerns as to poor payment practices without the need for imposing costly and complex regulatory and administrative burdens on head contractors.

[2] www.cultureinconstruction.com.au