



COVERSHEET

Minister	Hon Poto Williams	Portfolio	Building and Construction
Title of Cabinet paper	Construction Contracts (Retention Money) Amendment Bill: Approval for Introduction	Date to be published	6 July 2021

List of documents that have been proactively released		
Date	Title	Author
20 May 2021	Construction Contracts (Retention Money) Amendment Bill: Approval for Introduction	Office of the Minister for Building and Construction
20 May 2021	Construction Contracts (Retention Money) Amendment Bill: Approval for Introduction – Minute of Decision	Cabinet Office

Information redacted

YES

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Some information has been withheld for the reason of Confidential advice to Government.

In Confidence

Office of the Minister for Building and Construction

Chair, Cabinet Legislation Committee

Construction Contracts (Retention Money) Amendment Bill: Approval for Introduction

Proposal

- 1 This paper seeks approval to introduce the Construction Contracts (Retention Money) Amendment Bill to clarify and strengthen existing requirements for the protection of retention money into Parliament and for it to be referred to the Economic Development, Science and Innovation Committee for consideration.

Policy

- 2 Retention money is an amount withheld by a party to a construction contract (party A, a 'payer' who may be a head contractor) from an amount payable to another party to the contract (party B, a 'payee' who may be a subcontractor) as security for the performance of party B's obligations under the contract.
- 3 The Construction Contracts Act 2002 (CCA) regulates the payment provisions in construction contracts including adjudication, and protection of retention money withheld under commercial construction contracts. Holding retention money is voluntary. The amount withheld as retention money is set in the construction contract, and typically ranges between two and ten per cent of the contract value. Retention money is usually paid 12 months after the completion of a contract.
- 4 Government and the construction industry are working together to transform the construction sector through the Construction Sector Accord [DEV-19-MIN-0335 and CAB-19-MIN-0652 refer]. As part of the Construction Sector Accord Transformation Plan, Government and industry have considered improvements to the retention money regime. The protection and transparency of retention money helps maintain steady cash flow for construction businesses, and supports economic recovery efforts underway in the building and construction sector due to COVID-19.
- 5 In 2019, KPMG prepared an independent report for the Ministry of Business, Innovation and Employment (MBIE) to understand the effectiveness of the CCA's retention money regime. The report found that while there was overall compliance with the regime, a number of businesses surveyed were utilising retentions as working capital through the co-mingling of monies, and there were areas of non-compliance. The report also raised concerns regarding the lack of enforceable penalties.
- 6 Stakeholders from the construction sector have also told me of their concerns regarding the current retention money regime, highlighted following the collapse of major construction companies such as Arrow International (NZ), Ebert Construction,

Stanley Group, and Tallwood Holdings. The main issues they identified were that the regime has contradictions, including how the settings of the trust requirement limits its effectiveness to protect retention money, few incentives to comply with the regime, and limited information provided to subcontractors on retention money withheld.

- 7 To address these concerns, Cabinet agreed to a package of changes to the retention money regime in the CCA to clarify and strengthen existing requirements [CAB-20-MIN-0239 refers]. Cabinet also agreed to supplementary changes to support the operability of the regime following an exposure draft process [CAB-21-MIN-0074 refers]. The Bill incorporates these previous policy decisions, which are discussed in more detail below.

Clarifying the existing trust requirement (clause 4)

- 8 Cabinet have agreed to clarify the existing trust requirement by removing the ability to co-mingle retention money with other money and assets held by party A, who may be a head contractor, and remove the use of liquid assets as a way to hold retention money. Retention money held as cash must also be held aside separately in a bank account with prescribed ledger accounts.
- 9 This clarification will ensure greater protection for subcontractors' retention money in the event of insolvency, as the money will be clearly identifiable and separate from other assets held by the head contractor.

Improving the transparency of retention money (clause 9)

- 10 Cabinet have agreed to improve the transparency of retention money withheld by introducing regular reporting requirements and confirmation of retention money held.
- 11 These changes mean subcontractors are notified of the retention money held, and includes requiring head contractors to include more detailed information on the retention money held, including where the retention money is held and the amount.

Introducing offences, penalties and defences (clauses 4 and 9)

- 12 A failure by head contractors to hold retention money aside can create uncertainty and undermine business confidence within the building and construction sector. Cabinet has agreed to introduce offences, penalties, and defences for companies (e.g. head contractors) and their directors for failure to comply with the requirement to hold retention money on trust, including complying instruments.
- 13 The strict liability offence applies where a payer fails to hold retention money on trust in a separate bank account or complying financial instrument, and personal liability for directors will cover instances where a breach is discovered at the point of company insolvency. Offences have also been introduced for providing false information on retention money.

Allowing the receiver or liquidator, appointed in the event of insolvency, to administer the retention money (clause 11)

- 14 Cabinet agreed to allow the receiver or liquidator to be appointed to administer the retention money and charge reasonable fees, in the event the head contractor becomes insolvent.
- 15 This change has the effect of allowing subcontractors access to retention money without a court order, which would only add further costs, time, and complexity.

Avoiding the duplication of existing legislation (clause 4)

- 16 Through changes to the regime, the requirement to establish a separate bank account for retention money under the CCA will be similar to existing requirements under the Public Finance Act 1989 (PFA). Part 7 of the PFA regulates the use of trust money by the core Crown. Cabinet has agreed that where there is duplication of existing legislation (CCA and PFA) with similar outcomes, the core Crown:
 - 16.1 be held to account through the existing mechanisms under the PFA;
 - 16.2 utilise existing interest and investment provisions under the PFA; and
 - 16.3 account for retention money, as trust money in accordance with the PFA.

Additional decisions taken during drafting

- 17 Cabinet authorised the Minister for Building and Construction to approve changes consistent with the policy proposals in the proposed amendments to the Construction Contracts Act 2002 (retention money regime) [CAB-20-MIN-0239 refers].
- 18 During the drafting of the Bill, I authorised several changes consistent with the policy framework. The changes ensure the policy proposals can be effectively implemented, and include the following:
 - 18.1 Clause 4:
 - 18.1.1 Clarifies that the requirement for holding retention money on trust begins at the earliest practical point in time, which is the first payment where retention money is withheld.
 - 18.1.2 Includes a requirement for the head contractor to inform banks that an account holding retention money is a trust account for retention money. This provides further clarity that retention money is held separately from other company assets, which is important in the event the head contractor becomes insolvent.
 - 18.1.3 Clarifies that the offence for failure of holding money aside on trust also applies to failing to hold complying financial instruments appropriately.
 - 18.2 Clause 9 amends the existing section relating to accounting and records, to allow financial statements to be prepared that comply with current accounting

practices, and align with changes to the information on retention money included in the payment schedule.

18.3 Clause 11:

18.3.1 Details the appointment process for liquidators or receivers in the event of insolvency.

18.3.2 Clarifies that the costs and fees recovered by a liquidator and receiver be reasonable.

18.3.3 Allows subcontractors to apply to the Court for a review of the costs incurred by the liquidator or receiver, in the event of insolvency.

Amending the retention money regime

19 Requirements for the retention money regime are prescribed through primary legislation. In order to improve the existing retention money regime, I seek approval to amend the Construction Contracts Act 2002 through the Construction Contracts (Retention Money) Amendment Bill.

Impact Analysis

20 A Regulatory Impact Summary was prepared in accordance with the necessary requirements, and was submitted at the time that Cabinet approval was sought of the policy relating to the Amendment Bill [CAB-20-MIN-0239 refers]. MBIE's Regulatory Impact Analysis Review Panel determined that it met the criteria necessary for Ministers to make informed decisions on the proposals.

Compliance

21 The Bill complies with each of the following:

21.1 the principles of the Treaty of Waitangi;

21.2 disclosure statement requirements (a disclosure statement has been prepared and is attached to the paper);

21.3 the rights and freedoms contained in the New Zealand Bill of Rights Act 1990 or the Human Rights Act 1993;

21.4 the principles and guidelines set out in the Privacy Act 1993;

21.5 relevant international standards and obligations;

21.6 the Legislation Guidelines (2018 edition), which are maintained by the Legislation Design and Advisory Committee.

Consultation

22 The following agencies and Crown entities were consulted on the proposals in this paper: Ministry of Housing and Urban Development, the Treasury, Te Puni Kōkiri,

Kāinga Ora, Department of Internal Affairs, Ministry for the Environment, Ministry of Health, Ministry of Education, Department of Corrections, Ministry of Justice, Waka Kotahi NZ Transport Agency, Inland Revenue Department, Infrastructure Commission, and WorkSafe New Zealand. The Department of the Prime Minister and Cabinet was informed.

- 23 MBIE released a targeted consultation document in January 2020 to key stakeholder groups, including construction industry organisations most likely to be affected. Feedback from targeted consultation directly informed policy development for the Bill.
- 24 MBIE undertook consultation on an exposure draft of the Construction Contracts (Retention Money) Bill in August 2020. The draft Bill has been amended according to feedback received to support the operability of the changes.

Binding on the Crown

- 25 The Construction Contracts Act 2002 binds the Crown. This Bill will also be binding on the Crown.
- 26 This Bill does not seek to create a new agency or department.
- 27 This Bill does not amend the existing coverage of the Ombudsmen Act 1975, the Official Information Act 1982, or the Local Government Official Information and Meetings Act 1987.

Allocation of decision making powers

- 28 This Bill introduces new offences and penalties. This Bill creates a strict liability offence where party A, such as a head contractor, fails to hold retention money on trust in a separate bank account or complying financial instrument. The maximum fine for this offence will be set at \$200,000.
- 29 A penalty will also be imposed on directors of the payer company for failure by the payer to hold retention money on trust in a separate account or complying financial instrument. The penalty will be a maximum fine of \$50,000.
- 30 The Bill also creates additional offences for providing false information on retention money. The penalty for these offences is a maximum fine of \$50,000.

Associated regulations

- 31 There are no new or amended associated regulations for this Bill.

Definition of Minister / department

- 32 This Bill does not contain a definition of Minister or department. Existing definitions within the Construction Contracts Act 2002 will apply. The Minister in the principal Act means the Minister of the Crown who, under the authority of any warrant or with the authority of the Prime Minister, is for the time being responsible for the administration of the Act.

Commencement of legislation

- 33 To manage the impacts on the sector of the additional requirements, the new requirements will come into force six months after Royal Assent. The new requirements will apply to new construction contracts entered into six months after Royal assent.

Parliamentary stages

- 34 I propose a four month select committee process Confidential advice to Government
- 35 I recommend that this Bill be referred to the Economic Development, Science and Innovation Committee for consideration.

Proactive release

- 36 I propose that this paper and the attached minute are proactively released within 30 working days of the final decision being made by Cabinet. The release of the information is subject to redactions consistent with the Official Information Act 1982.

Recommendations

The Minister for Building and Construction recommends that the Committee:

- 1 Confidential advice to Government
- 2 **note** that the Bill will strengthen and clarify the retention money regime in the Construction Contracts Act 2002;
- 3 **approve** the Construction Contracts (Retention Money) Amendment Bill for introduction, subject to the final approval of the government caucus and sufficient support in the House of Representatives;
- 4 **agree** that the Construction Contracts (Retention Money) Amendment Bill be introduced in May 2021; and
- 5 **agree** that the Government propose that the Bill be:
- 5.1 referred to the Economic Development, Science and Innovation for consideration; and
- 5.2 Confidential advice to Government

Authorised for lodgement

Hon Poto Williams

Minister for Building and Construction