

Assessing Outstanding Payment Issues in the Hong Kong Construction Industry

Paul H K Ho¹

Abstract

In Hong Kong, multi-layered sub-contracting is common, with sub-contracts typically providing 'pay-when-paid' arrangements for progress payment. When no payment is made by the employer to the main contractor, all lower-tier sub-contractors and suppliers suffer. To help resolve payment disputes, relevant professional institutions and organisations have suggested the security of payment legislation. Nevertheless, any new legislation requires strong justification to earn legislative councillors' support. Therefore, the main objectives of this study are to (1) assess the durations, amounts and major causes of outstanding payments, (2) identify the common methods adopted to resolve payment disputes, including the assessment of their effectiveness and (3) evaluate whether some common legislative provisions adopted in overseas countries can effectively secure payments in the construction supply chain. This study was conducted by questionnaire with main contractors, sub-contractors and suppliers as the target respondent. Of the 1,000 questionnaires dispatched, 423 were returned, of which 23 cases were subsequently identified as incomplete. Hence, there were 400 successful cases representing an overall response rate of 40%. It was found that while the delay in progress payments was not intolerable, the delay in the settlement of final payments was very long. Many respondents identified variation as the most common source of disputes, generating difficulties in work measurement and valuation along with entitlement to interim payments and final accounts. The amount of the outstanding payment reported by respondents was very serious. With the exception of negotiation, the adopted common dispute resolution methods were considered ineffective for resolving payment problems. The respondents also believed that some of the common legislative measures adopted in overseas countries could promptly resolve the majority of payment disputes in the local construction industry.

Keywords: Outstanding Payment, Dispute Resolution Method, Security of Payment.

1. Introduction

The construction industry has a low capital support and heavy reliance on cash flows to sustain business. Operating under a hierarchical chain of contracts within the construction industry, the financial failure of any one party such as the employer or main contractor can have a domino effect on lower-tier parties in the contractual chain. Extremely tight margins in

¹ Principal Lecturer; Division of Building Science and Technology; City University of Hong Kong; Tat Chee Avenue, Kowloon, Hong Kong SAR, PR China; bshkho@cityu.edu.hk

the industry, restricted cash flows and payment default can force the lower-tier parties to carry bad debts or, if the burden of debt becomes too much, force such parties into insolvency. Nevertheless, some lower-tier parties are reluctant to take the necessary actions available under the contract due to the high cost and time delays involved and concern regarding future work opportunities. Under such circumstances, they may choose to waive their legal rights when faced with promises of future payment (Royal Commission into the Building and Construction Industry, 2002).

Given the seriousness of payment problems, the governments in the United Kingdom, Australia, New Zealand, Singapore and Malaysia have passed specific legislation to help secure payments along the construction supply chain. As the next section reveals, the payment problem in Hong Kong may be more serious than in these countries. Some professional institutions, associations and contracting organisations have recommended that the government pass similar legislation. Nevertheless, any new legislation requires strong justification to earn legislative councillors' support. Therefore, the main objectives of this study are to (1) assess the durations, amounts and major causes of outstanding payments, (2) identify the common dispute resolution methods adopted to resolve payment disputes and assess their effectiveness and (3) evaluate whether some common security of payment legislations adopted in overseas countries would effectively secure payments in the local construction supply chain.

2. Review of Payment Issues in the Hong Kong Construction Industry

Cash flow is the lifeblood of main contractors, subcontractors and suppliers because their businesses' viability tends to depend more on cash flow than profit margin. However, most contracts in the Hong Kong construction industry contain a 'pay-if/when-paid' provision. When the payment is not forthcoming from an employer, all lower-tier subcontractors and suppliers suffer, even though the default is solely due to the main contractor.

In 2001, the Construction Industry Review Committee (CIRC) noted that some overseas countries such as the United Kingdom and Australia had enacted a security of payment legislation to deal with payment-related issues in their construction industry. For instance, the Housing Grants, Construction and Regeneration Act 1996 in the United Kingdom provides the right to progress payments through payment claims for the completed work. Other legislative provisions include prohibiting the conditional payment (i.e. 'pay-if-paid' and 'pay-when-paid' clauses) in a construction contract, providing a right to refer any dispute arising under the contract to adjudication, requiring security for disputed amounts following adjudication, and allowing to suspend performance of obligations for non-payment after adjudication. The CIRC recommended that the need for enacting security of payment legislation be considered, given overseas experiences (CIRC, 2001).

In response to the CIRC's recommendation in 2004, the HKSAR government took the view that security of payment legislation was unnecessary under local circumstances; instead, a voluntary adjudication was introduced in public work contracts to help resolve disputes. Although the objectives of this voluntary adjudication are to achieve a 'simple, speedy and...

effective method of resolving disputes', it cannot improve the payment problem for a few reasons. First, it is limited to government projects and does not apply to projects in the private sector. Second, even in a government project, the voluntary basis means that one party can request adjudication and the other can refuse. Third, it does not apply to subcontractors and suppliers. Finally, it does not affect the unfair 'pay-if-paid' or 'pay-when-paid' contractual provision. In other words, the payment problems in local construction industries have remained unresolved since the CIRC report.

Many of the payment problems that have occurred overseas have also occurred in Hong Kong. However, there are also specific problems in the local construction industry. Many clauses in the standard forms of contract are amended to allocate most risks to main contractors, who have no choice but to accept these inequitable contract provisions in view of the keen competition for any project. When a risk event occurs, some main contractors look for ways to make contractual claims that will allow them to recover their losses, whereas architects and engineers in the same situations are pressed by their employers into a harsh position in which any delay or extra cost is either the main contractor's or their responsibility. Under such circumstances, architects and engineers may not act impartially and fairly when administering the contracts. When a dispute arises, the current adjudication process does not resolve the cash flow problem of lower-tier parties in a speedy and cost-effective manner because it is complex and akin to short form arbitration.

According to a survey of outstanding payments jointly conducted by the Public Opinion Programme and the Construction Industry Council (2010), the top ten most serious problems faced by main contractors, subcontractors and suppliers in the private sector were 'delayed resolution of dispute', 'delayed settlement of final accounts', 'various unreasonable obstacles for payments', 'have to continue works even when arrears are not settled', 'disagreement on substantial completion of works', 'delayed certification of interim payments', 'unreasonable allocation of risk', 'disputable or wrongful contra-charges', 'contracts contain payment terms like "pay-when-paid" or "pay-if-paid"' and 'failure of agreement on variations'. To understand the payment issues in detail, it is necessary to assess the duration of delays in progress and final payments, along with the major causes of outstanding payments and their corresponding amounts.

Moreover, main contractors, subcontractors and suppliers tend to resolve payment disputes through commercial negotiation. While mediation and arbitration are typically specified in contracts as the dispute resolution methods, these are not considered effective enough in securing payments. Common reasons may include concerns about breaking up the business relationship with their clients; imbalance in negotiation positions; mediation's voluntary, non-binding nature; and the fact that arbitration is costly and time-consuming. At present, adjudication is not common in the local construction industry. Before introducing new legislative measures, it is essential to re-examine the effectiveness of the current methods adopted to resolve payment disputes.

A review of the security of payment legislation in the United Kingdom, New South Wales and Singapore indicates that there are some common legislative provisions. These include the provision of default payment periods if the contracts do not contain any payment schedule,

the prohibition of conditional payment terms such as 'pay-if-paid' or 'pay-when-paid', the right to suspend work, the right to adjudication for prompt resolution of construction dispute and recovery of payment and the enforcement of adjudicators' decisions. Before introducing the security of payment legislation, it is important to assess whether these legislative provisions can effectively secure payments in the local construction supply chain.

3. Research Method

3.1 Research Design

This study was conducted using an email questionnaire survey consisting of seven questions. Questions 1-4 collected information on the durations, magnitude and causes of outstanding payments. Questions 5 and 6 collected details on the common methods adopted to resolve payment disputes and their effectiveness. Question 7 elicited information on the effectiveness of some common security of payment legislative provisions for enhancing payment practices, the details of which are as follows.

1. As the timeliness of settling payments is a major concern, question 1 assessed the extent of delays in receiving progress payments from main contractors, subcontractors and suppliers. Respondents were asked to provide information on the interim payment period specified in the contract and the actual period taken to settle the interim payment. As interim payment is a generic term, this study includes a single or one-off payment, a milestone payment and other progress payments.
2. If there are more contractual disputes, the contracting parties take a longer time to agree on the final account. Question 2 assessed the extent of delays for final accounts. The respondents were asked to provide information about the final account period specified in the contract and the actual period taken to settle the same.
3. Question 3 assessed the amount of outstanding payments withheld by upper-tier contracting parties. A snapshot approach was adopted, whereby respondents were asked to provide data on the amount of payments applied and the corresponding amount actually received. The difference between these two payments can be construed as the estimated amount of outstanding payments. In addition, the respondents were asked to provide data on the total amount of annual business receipts. Different grossing-up factors were calculated for different respondents, taking into sampling fractions and response rates. The total amount of outstanding payments could thus be estimated.
4. Question 4 identified the causes of major payment disputes between the contracting parties. Nine major types of payment disputes were identified, including (a) disagreement on workmanship and quality of work done, (b) disagreement on measurement and valuation of variations, (c) disagreement on, and delay in, the settlement of progress payments, (d) disagreement on claims for prolongation of or disruption to the progress of works, (e) disagreement on amount of liquidated damages, contra charges or set-offs, (f) disagreement on issuance of certificate of practical/substantial completion of the works including delay in release of retention money, (g) disagreement on issuance of certificate for making good defects including delay in release of retention money, (h) disagreement on, and delay in, settlement of final account, and (i) disagreement on noncompliance with specified standards. The respondents were asked to provide a breakdown of the

total amount of outstanding payments previously reported based on these nine causes of payment disputes.

5. Question 5 identified common methods adopted for the resolution of payment disputes. The respondents were asked to report the approaches they adopted for the resolution of payment disputes from amongst six methods: (a) dispute resolution adviser, (b) commercial negotiation, (c) mediation, (d) adjudication, (e) arbitration and (f) litigation. Choosing more than one method was allowed because more than one dispute can be encountered in a contract. A distribution analysis of the dispute resolution methods adopted was then prepared to indicate the relative frequency of use.
6. Question 6 evaluated whether the common dispute resolution methods could effectively resolve the payment problems. The respondents were asked to evaluate whether the six identified dispute resolution methods were 'effective' or 'not effective', considering the cost, time, binding/non-binding effect and any other relevant considerations.
7. Question 7 evaluated the potential effectiveness of common legislative provisions, if adopted, to secure payments along the construction supply chain. Five common security of payment legislative provisions used in overseas countries were identified, including the (a) right to progress payments, (b) right to suspend works for non-payment, (c) prohibition of conditional payment provisions, (d) right to rapid adjudication and (f) enforcement of adjudicators' decisions. Because the security of payment legislation is still under consideration, a brief description of these legislative provisions was provided in the questionnaire. The respondents were asked for their opinions on the effectiveness of these legislative provisions, expressed in percentages of the total amount of outstanding payments withheld.

3.2 Data Collection

The target respondents consisted of three groups: main contractors, subcontractors and suppliers. The security of payment legislation in many countries also includes professional consultants, but they are excluded from this study because they do not suffer payment problems to the same extent when compared to the main contractors, subcontractors and suppliers who undertake the physical construction. This study's sampling frame was based on various government registers such as the Registered General Building Contractors and the List of Approved Contractors for Public Works (for main contractors), Registered Specialist Contractors (for subcontractors) and the List of Approved Suppliers of Specialist Contractors (for suppliers). The data were collected between early June and the end of September 2012. Of the 1,000 questionnaires dispatched, 423 were returned, of which 23 cases were subsequently identified as incomplete. Hence, there were 400 successful cases representing an overall response rate of 40%.

4. Findings and Discussion

Table 1 shows the distribution of respondents in respect to the number of questionnaires delivered and successfully returned. The overall response rate was 40% (42.5% for subcontractors, 40% for suppliers and 35% for main contractors). Statistically, the sample sizes for main contractors and subcontractors are acceptable. However, because there are a

relatively small number of returned cases from suppliers, the results derived are subject to a relatively larger sampling error. The key findings of this study are summarised below.

Table 1: Distribution of respondents

Type of respondents	No. of questionnaires delivered	No. of questionnaires completed	Response rate
Subcontractor	600	255	42.5%
Main contractor	300	105	35.0%
Supplier	100	40	40.0%
Overall	1000	400	40.0%

4.1 Delay in Settlement of Interim Payments

The interim payment period specified in the contract and the actual period taken to settle the same are shown in Table 2. The average interim payment periods were 31, 38 and 36 days for main contractors, subcontractors and suppliers, respectively, whereas the average actual periods taken to settle interim payments were 42, 52 and 52 days as reported by main contractors, subcontractors and suppliers, respectively. In other words, there were average payment delays of 11, 14 and 16 days for main contractors, sub-contractors and suppliers, respectively, due to various disputes and delays. This finding indicates that upper-tier parties did not fulfil their contractual obligations to make interim payments within the specified periods. Nevertheless, respondents generally considered such delays to be less serious; rather, they were more concerned with the amount of payments being withheld and how to resolve such withholding.

Table 2: Delay in settlement of interim payments

Durations taken for settlement of interim payment (days)	Main Contractor	Subcontractor	Supplier
Interim payment periods specified in the contract	31	38	36
Actual interim payment periods taken	42	52	52
Difference	11	14	16

4.2 Delay in Settlement of Final Accounts

The final account period specified in the contract and the actual period taken to settle the same are shown in Table 3. The average final account periods were 12, 12 and 6 months for main contractors, subcontractors and suppliers, respectively, whereas the average actual periods taken to settle final payments were 24, 21 and 9 months as reported by main contractors, subcontractors and suppliers, respectively. In other words, the average delays in the settlement of final accounts were 12, 9 and 3 months for main contractors, sub-contractors and suppliers, respectively. This finding also suggests that upper-tier parties could not fulfil their contractual obligations to settle final accounts within the specified

periods. The respondents generally considered these delays to be unreasonably long and reported serious affects to cash flow due to a low profit margin, a high percentage of retention monies and a long period of final measurement and valuation.

Table 3: Delay in settlement of final accounts

Durations taken for settlement of final account (months)	Main Contractor	Subcontractor	Supplier
Final account periods specified in the contract	12	12	6
Actual final account periods taken	24	21	9
Difference	12	9	3

4.3 Estimated Amount of Outstanding Payments

Based on the amount of payments applied and the corresponding amount of payments actually received, the amount of outstanding payments and its corresponding percentage were calculated as shown in Table 4. The percentages of outstanding payments were 8.5%, 11.6% and 4.8% for main contractors, subcontractors and suppliers, respectively. Taking the amount of outstanding payments as a percentage of the total business receipts reported by respondents, the total amount of outstanding payments per annum was estimated to be HK\$11,500 million for main contractors, HK\$11,000 million for subcontractors and HK\$500 million for suppliers. It is noted that the security of payment legislation in the United Kingdom and New Zealand (but not Australia, Singapore or Malaysia) does not cover supply contracts, probably because payment problems in these two countries are not serious. This finding indicates that suppliers also suffer from serious payment problems (4.8%), although the extent is less severe than that experienced by main contractors (8.5%) and subcontractors (11.6%).

Table 4: Estimated amount of outstanding payments

Estimated amount of outstanding payments	Main Contractor	Subcontractor	Supplier
Outstanding payments (HK\$ million)	\$11,500	\$11,000	\$500
Business receipts (HK\$ million)	\$135,000	\$95,000	\$10,500
Outstanding payment as percentage of business receipts	8.5%	11.6%	4.8%

Remark: The amount of outstanding payments to main contractors, subcontractors and suppliers are susceptible to overlapping due to conditional payments in the subcontracting chain. Adding the two figures would result in double counting.

The respondents considered their profit margins in many projects to be far below the percentages of outstanding payments. Operating under this business environment, they had to balance the negative cash flows during the course of the contract and could only realise the profit after the settlement of the final account. Given the substantial amount of outstanding payments, coupled with the considerable delay in settlement of final accounts mentioned above, the security of payment in the local construction industry should be improved by some means.

4.4 Major Causes of Outstanding Payments

Table 5 provides a breakdown of the total amount of outstanding payments (i.e. the difference between payments applied and payments received) into nine identified cause categories. The three most common causes, as reported by main contractors and subcontractors, were 'disagreement on measurement and valuation of variations' (37% for main contractors and 30% for subcontractors), 'disagreement on, and delay in, settlement of final account' (20% for main contractors and 22% for subcontractors) and 'disagreement on, and delay in, settlement of progress payments' (18% for main contractors and 20% for subcontractors).

Table 5: Breakdown of major causes of outstanding payments

Major causes of outstanding payments	Main Contractor	Subcontractor	Supplier
Disagreement on measurement and valuation of variations	37%	30%	-
Disagreement on, and delay in, settlement of final account	20%	22%	25%
Disagreement on, and delay in, settlement of progress payments	18%	20%	40%
Disagreement on claims for the prolongation of and disruption to progress of works	7%	5%	-
Disagreement on issuance of certificate of practical completion of works including a delay in the release of retention money	6%	7%	-
Disagreement on workmanship and quality of work done	5%	7%	-
Disagreement on issuance of certificate of making good defects including delays in the release of retention money	4%	5%	-
Disagreement on amount of liquidated damages, contra charges or set-offs	3%	4%	5%
Disagreement on noncompliance with specified standards	-	-	30%
Total	100%	100%	100%

Due to high land costs, many clients set a tight schedule for both design and construction so that completion can be achieved as soon as possible to generate income. Under the clients' pressure, some projects are inevitably tendered based on incomplete designs and/or specifications. As a result, architects and engineers are required to issue a large number of variations during the construction stage. Disputes often arise in relation to the procedural requirements in respect of the notice of claims, discrepancies among drawings, specifications, bills of quantities and other parts of contract documents, different interpretations between the work specified in original contract documents and the work changed by architects and the measurement and valuation of some variations. All of these disputes lead to underpayments to main contractors and subcontractors. In addition, interim payments, which typically include the estimated values of works done, preliminaries, materials on- and off-site, re-measurements and contractual claims, are generally evaluated

on the conservative/low side. There are various reasons behind. For instance, because so many variations are issued each month, quantity surveyors do not have sufficient time to accurately measure and evaluate all variations. As a result, only approximate values of these variations are included in interim payments. These values are, in many cases, under- rather than over-estimated by quantity surveyors. Furthermore, if there are serious delays in the settlement of variations, contractual claims and other disputes, these will also result in more serious delays in the settlement of final accounts.

The three most common causes of outstanding payments reported by suppliers were 'disagreement on, and delay, in settlement of progress payments' (40%), 'disagreement on noncompliance with specified standards' (30%) and 'disagreement on, and delay in, settlement of final account' (25%). As most supply contracts contain the 'pay when/if paid' clause, this seriously affects the timely settlement of both interim and final payments received by suppliers. In addition, one of the major disputes is whether the materials supplied comply with the specified standards. They cannot normally get payments unless this type of dispute has been resolved.

4.5 Methods for Resolving Payment Disputes

A distribution analysis of the methods adopted to resolve payment disputes is shown in Table 6. The three most common methods, as reported by main contractors, were 'commercial negotiation' (55%), 'mediation' (15%) and 'arbitration' (10%). Indeed, these three dispute resolution methods are commonly specified in most local construction contracts. So it is rational that main contractors would first try to settle disputes through commercial negotiation. If unsuccessful, they would then pursue mediation. If the disputed amount is relatively small, then the dispute can be satisfactorily resolved through mediation. Main contractors still suffer from cash flow problems during the mediation process, which may take few months. However, if the amount in dispute is substantial, it is not likely that the dispute will be resolved by mediation because the losing party may subsequently refer the case to arbitration for a final decision. Nevertheless, arbitration is considered both costly and time-consuming. In many cases, both parties in arbitration have incurred significant legal costs that may not be affordable for small main contractors.

Table 6: Methods adopted to resolve payment disputes

Methods adopted to resolve payment disputes	Main Contractor	Subcontractor	Supplier
Commercial negotiation	55%	65%	70%
Mediation	15%	15%	17%
Arbitration	10%	7%	2%
Litigation	8%	6%	10%
Adjudication	7%	4%	1%
Dispute resolution adviser	5%	3%	-
Total	100%	100%	100%

The three most common methods reported by subcontractors for resolving disputes were 'commercial negotiation' (65%), 'mediation' (15%) and 'arbitration' (7%). Compared with main contractors, subcontractors relied more on commercial negotiation to resolve payment disputes, suggesting that subcontractors rely heavily on cash flows to sustain their businesses. Even if they have strong cases to succeed, they may choose to waive certain legal entitlements for the sake of promptly settling the disputes. Arbitration is considered a last resort for resolving payment disputes.

The three most common methods reported by suppliers for resolving disputes were 'commercial negotiation' (70%), 'mediation' (17%) and 'litigation' (10%). Compared with main contractors and subcontractors, suppliers relied even more on commercial negotiation to settle payment disputes for reasons similar to subcontractors. However, if commercial negotiation and mediation are not successful, suppliers prefer to litigate rather than arbitrate because most supply contract disputes are relatively straightforward and litigation is better than arbitration in terms of the time and cost involved.

4.6 Effectiveness of Payment Dispute Resolution Methods

The effectiveness of the six common payment dispute resolution methods is illustrated in Table 7. The majority of the respondents considered commercial negotiation to be the most effective method, ranging from 80% for main contractors, to 85% for subcontractors and 90% for suppliers. Slightly more than half of respondents considered mediation an effective method, ranging from 55% for main contractors, to 65% for subcontractors and 60% for suppliers. Realising that any formal dispute may break up the business relationship with their clients, main contractors, subcontractors and suppliers prefer to resolve their payment disputes through informal commercial negotiation whenever possible and, if not successful, they would then pursue formal mediation. As lower-tier parties are often in a weak negotiation position, they are sometimes forced to compromise by waiving certain entitlements if the disputes can be settled promptly. Therefore, while commercial negotiation appears to be very effective in dealing with payment disputes, it may not be a fair and equitable solution.

Less than half of the respondents considered adjudication an effective method, ranging from 42% for main contractors, to 45% for subcontractors and 40% for suppliers. First, there are better methods, such as mediation, and second, adjudication is operated in a similar process as the short-form arbitration, which in many cases cannot resolve the disputes in a timely and cost-effective manner. Dispute resolution advisers are only available in government contracts and are not applicable to subcontractors and suppliers, which limits the applications. Other dispute resolution methods, such as arbitration and litigation, were considered ineffective because they were time consuming or expensive. Arbitration or litigation might only be used in cases where the amount in dispute is very substantial. Under such circumstances, no party can afford to lose their cases.

Table 7: Effectiveness of payment dispute resolution methods

Effectiveness of payment dispute resolution methods		Main Contractor	Subcontractor	Supplier
Commercial negotiation	Effective	80%	85%	90%
	Not effective	20%	15%	10%
Mediation	Effective	55%	65%	60%
	Not effective	45%	35%	40%
Adjudication	Effective	42%	45%	40%
	Not effective	58%	55%	60%
Dispute resolution adviser	Effective	32%	-	-
	Not effective	68%	-	-
Arbitration	Effective	20%	17%	12%
	Not effective	80%	83%	88%
Litigation	Effective	8%	6%	15%
	Not effective	92%	94%	85%

4.7 Effectiveness of Security of Payment Legislative Provisions

The effectiveness of each of the security of payment legislative provisions expressed in terms of percentages of the total amount of outstanding payments is shown in Table 8. For main contractors, the three most effective legislative provisions for resolving payment disputes were the 'right to rapid adjudication' (50%), the 'right to suspend works for non-payment' (20%) and 'enforcement of adjudicators' decisions' (12%). For subcontractors and suppliers, the three most effective legislative provisions were the same, i.e. the 'right to rapid adjudication' (40% for subcontractors and 45% for suppliers), 'prohibition of conditional payment provisions' (20% for subcontractors and 18% for suppliers) and the 'right to suspend works for non-payment' (17% for subcontractors and 15% for suppliers). The use of 'others' suggests that these legislative provisions would not resolve all payment problems. If the amount in dispute between parties is substantial, one or both parties may refer the case, at the beginning or after the adjudication, to court or arbitration proceedings for a decision. Nevertheless, past experiences in overseas countries indicate that the security of payment legislation can resolve the majority of payment disputes.

Table 8: Effectiveness of security of payment legislation

Effectiveness of security of payment legislation	Main Contractor	Subcontractor	Supplier
Right to rapid adjudication	50%	40%	44%
Right to suspend works for non-payment	20%	17%	15%
Prohibition of conditional payment provisions	-	20%	18%
Enforcement of adjudicators' decisions	12%	10%	8%
Right to progress payments	10%	7%	5%
Others	8%	6%	10%
Total	100%	100%	100%

For all types of respondents, the right to adjudicate disputes is the most important provision in the security of payment legislation. Based on that legislative provision in overseas countries, adjudicators' decisions are binding unless and until the underlying dispute is resolved in court or arbitration proceedings. The decisions are enforceable even if there are errors of law or fact provided that the adjudicator acted within his jurisdiction and reached his decision in accordance with the principles of natural justice. Following service of the referral, the adjudicator in the United Kingdom must reach a decision within 28 calendar days. This requirement makes it easier for the lower-tier parties to recover their payments without a substantial delay.

The rationale behind the right to suspend is to prevent main contractors and subcontractors from having to continue working without payment, essentially enabling them to legitimately cease the works without fear of breaching the contracts. Suspension also provides an incentive to the upper-tier contracting parties to pay fairly and on time.

Conditional payment terms such as 'pay-if/when-paid' are prevalent in the local construction industry. Arguments in favour of such terms include freedom of contract and allocation of risks. However, the prohibition of conditional payment is based on the principle that a minimum level of clarity and fairness should be maintained in a contract so that the crystallisation of payments due does not depend on factors external to the contract and beyond the power of subcontractors or suppliers to fulfil. This legislative provision would effectively prevent the upper-tier contracting parties from withholding any payments on the grounds that they have not received a payment from a third person, thus protecting the smaller, more vulnerable subcontractors and suppliers in the supply chain.

5. Conclusions

Many of the respondents attributed variations as the most common source of disputes because they generate difficulties in measurement and valuation of the works done as well as agreeing on the entitlement to interim payments. A payment schedule is usually specified in a contract, but there are always delays due to slow certification, conditional payment terms and variation disputes. While respondents could generally get paid from interim payments, they were left in uncertain positions when facing the unduly long time lag in the settlement of final accounts. Under the current settings, the respondents tended to resolve their payment disputes through informal commercial negotiation because the other dispute resolution methods specified in the contract were considered to be ineffective. Under such situations, it was not uncommon that they would have to compromise by accepting a final account less than the amount that they were supposed to be entitled. The total amount of outstanding payments was reported to be substantial which should warrant the introduction of legislative measures to secure payments in the construction supply chain. The respondents also believed that some of the common legislative measures adopted in overseas countries could effectively resolve the majority of payment disputes along the construction supply chain. The way ahead is to consider the exact scope and details of the security of payment legislation appropriate for the local construction industry. This would be a good area for further research.

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