

Insights

KEY DEVELOPMENTS AND CHANGES IN COMPARISON WITH THE EXISTING CONTRACTUAL SECURITY OF PAYMENT REGIME

CONSTRUCTION INDUSTRY SECURITY OF PAYMENT BILL 2024

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SUMMARY

In May 2024, the Hong Kong Government introduced the Construction Industry Security of Payment Bill (**Bill**) to the Legislative Council for first reading. If the Bill is passed into law, the Bill will introduce a statutory security of payment regime for both public sector and private sector construction contracts in Hong Kong.

Currently, a contractual security of payment regime is in place for public sector construction contracts only. In this article, we will compare the clauses in the Bill against the public works contracts pilot programme security of payment provisions (**Pilot Provisions**) promulgated by the Development Bureau (**DevB**) for the contractual regime, and consider the key development, changes and differences.

This is the first article in a series of two articles. In the next article, [we will take a deeper look at the change of two features in the payment process and the adjudication process](#) relating to variation claims and time-related disputes.

THE PILOT PROGRAMME AND THE BILL

In 2021, Hong Kong took its first significant step towards the introduction of a security of payment regime. On 5 October 2021, the DevB published the Technical Circular (Works) No.6/2021 (**Circular**) which promulgated a contractual regime to implement “the spirit of the Security of Payment Legislation” into public works construction contracts and sub-contracts. The contractual regime came into effect in two stages, and applied to public works contracts that were tendered after 31 December 2021 (first stage) and 1 April 2022 (second stage).

We have covered the draft and final versions of the Circular in the following articles:

- [Security of Payment in Hong Kong – pilot programme for public works contracts](#)
- [SOP in Hong Kong – Public Works Contracts](#)
- [Security of payment circular issued by the Development Bureau of Hong Kong – to take effect from 31 December 2021](#)
- [The new security of payment regime in Hong Kong – key issues to consider before its implementation](#)

With the introduction of the Bill to the Legislative Council, it is important for the construction industry in Hong Kong to prepare itself for the impact of the Bill. We have looked at the structure and key provisions of the Bill in our earlier article “[Hong Kong Security of Payment Bill gazetted](#)”.

In this article, we will consider some of the more notable developments, changes, and differences by comparing clauses in the Bill to clauses in the Pilot Provisions (which are set out in Annex C to the Circular).

COMPARISON WITH THE PILOT PROGRAM

The Government’s Bill includes developments, changes and clarifications to the Pilot Provisions. Some of the more notable changes or differences are:

CHANGES AND CLARIFICATIONS REGARDING THE CLAIM HANDLING PROCEDURE

(Clause 9 of the Pilot Provisions; Clause 23 of the Bill)

It is a feature of both the Pilot Provisions and the Bill that a payment dispute does not arise in respect of a claim for additional payment, unless the parties first go through the claim handling procedure stipulated in the contract. Clause 23(5) of the Bill now provides further clarification of the scope of this feature by defining additional payment, in brief terms, as payments provided for in a construction contract for expenditure or loss incurred (a) because of delay or disruption, or (b) because of variations. This brings greater certainty.

Where an additional payment is claimed in respect of a specified compensable event, under clause 9(3) of the Pilot Provisions, a payment dispute does not arise unless and until the contract administrator has notified his rejection or assessment of that claim, or has failed to do so within the applicable timescale or, if no timescale is specified, a reasonable time. Although the clauses appear similar at first sight, by contrast, clause 23(4) of the Bill requires such events to have occurred **before** the Payment Claim is served. We will be taking a deeper look at the potential effects of this in the next article.

CHANGES REGARDING THE ADJUDICATOR’S POWER TO DECIDE ON EXTENSION OF TIME AND TIME-RELATED CLAIMS

(Clause 17 of the Pilot Provisions; Clauses 33, 42 and 56 of the Bill)

Whether the adjudicator should be given the power to decide on extension of time and time-related claims has been a matter of much debate.

Under the Circular, an adjudicator has the jurisdiction to make binding determinations on time-related costs forming part of a payment dispute and, in the process of doing so, decide on a party's entitlement to an extension of time as a consequential or ancillary matter.

The position has shifted in the Bill, which makes it clear that the adjudicator has the power to decide on extension of time and time-related claims. The adjudication of time-related disputes will apply initially to the public works contracts and sub-contracts, with a possibility of being extended in future to apply to private sector construction contracts and sub-contracts.

We will be taking a deeper look at the details of this development in the next article.

INTRODUCTION OF A PROCEDURE AND REQUIREMENT FOR THE ADJUDICATOR TO DISREGARD LATE SUBMISSIONS, RESPONSE, DOCUMENT OR EVIDENCE

(Clauses 31, 32 and 37 of the Bill)

Clause 37(1) of the Bill require the adjudicator to disregard any submission, response or reply that is served late.

Clauses 37(2) and (3) further require (by the use of the word "*must*") the adjudicator to disregard submissions, responses, documents or evidence (a) of which the objecting party is unaware on the date on which the adjudication notice is served, (b) should reasonably have been served on the objecting party before the date on which the adjudication notice is served, and (c) that cannot be fairly considered or responded to by the objecting party (**new material**). This is a new feature introduced by the Bill.

The test is whether **the adjudicator is satisfied** that the alleged new material falls within the three requirements above, hence is under the discretion of the adjudicator. This introduces some uncertainty to the process. According to [the Legislative Council Brief on the Bill](#), (1) this mechanism is also a feature of Singapore and Western Australia, but not a feature of the United Kingdom, New Zealand, or Malaysia; and (2) implementation of the Bill will include the "*making of adjudication rules, practice notes and code of conduct by [Adjudicator Nominating Bodies]*", which hopefully will bring more clarity regarding this mandate.

A paying party may raise in its Adjudication Response an objection to the inclusion by the claiming party of new material (Under clause 31(3)(b)). The claiming party may raise such an objection, two working days after the service of the Adjudication Response, in the form of a Reply to Adjudication Response (Under clause 32). The Reply to Adjudication Response is a new "round" of submission

introduced by the Bill solely for the purpose of giving the claiming party an opportunity to raise objections to the inclusion of new material.

This mechanism appears to reinforce the idea that it is the Payment Claims and Payment Responses rather than the submissions that set the scope for the adjudication. It creates a strong incentive on the parties to present all key arguments and evidence before adjudication is commenced, and is designed to prevent ambush tactics whereby a party deliberately holds back information with a view to gain a tactical advantage in the adjudication.

INTRODUCTION OF A STATUTORY MECHANISM FOR SETTING ASIDE AND ENFORCING OF DETERMINATIONS BY THE COURTS

(Part 3 Division 6 of the Bill)

Under the Bill, parties may apply to court to set aside an adjudicator's determination or to enforce the determination as a judgment.

The Bill provides very limited grounds for setting aside a determination. The only grounds are (a) fraud or bribery, (b) material denial of natural justice, (c) issues regarding independence or impartiality of the adjudicator, and (d) the adjudicator acted in excess of his jurisdiction. A party has 14 days to make the setting aside application.

A party may apply to enforce a determination as a judgment, if the adjudicated amount remains unpaid after the payment deadline, and no setting-aside application is pending. The Bill further provides that the court must grant leave for enforcement within seven days, unless (a) a setting-aside application is pending, (b) the determination no longer is binding on the parties, or (c) the adjudicated amount has been paid in full. This is a pro-enforcement feature.

DIRECT PAYMENT MECHANISM NOT PROVIDED FOR IN THE BILL

(Clause 43 of the Pilot Provisions)

Under the contractual regime, there is a direct payment mechanism whereby a sub-contractor of any tier may request the Government as the employer to make direct payment of any unpaid adjudicated amount to the requesting sub-contractor. Unsurprisingly, such a mechanism is not provided for in the Bill.

It remains to be seen whether the Government (and other private sector employers) will adopt direct payment mechanisms as an additional contractual avenue for enforcing adjudication determinations.

CHANGES AND DEVELOPMENTS REGARDING THE UNPAID PARTY'S RIGHT TO DELAY WORK

(Clause 37 of the Pilot Provisions; Part 4 of the Bill)

Under the Pilot Provisions, an unpaid party may suspend or slow down work in relation to non-payment of an admitted amount, deemed admitted amount or adjudicated amount, upon giving notice to the (non)paying party and the employer. The suspending party will have five days to resume work after receiving payment. This feature is now known in the Bill as the right to delay work.

The Bill extends and clarifies the protections available to the suspending party. The suspending party not only is not liable for breach of the construction contract or losses and damages suffered by the (non)paying party, but also expressly is entitled to reasonable extension of time and loss and expenses reasonably incurred as a result of exercising the right to delay work. According to the Legislative Council Brief on the Bill, (1) the proposal of allowing a choice between suspension and slowing down work has received majority support from Hong Kong stakeholders; and (2) a similar approach has been adopted in Malaysia and the United Kingdom.

CHANGES TO SET-OFF AND WITHHOLDING

(Clause 6 of the Pilot Provisions; Clause 19 of the Bill)

Under clause 6 of the Pilot Provisions, a paying party must state in its Payment Response any amounts of set-off or withholding, as well as the grounds and basis of calculation. This express requirement has been removed from the equivalent provision of the Bill (clause 19).

Instead, clause 21 of the Bill now only provides that a paying party who has failed to serve a Payment Response is not allowed to raise any set-off in the adjudication proceedings.

The above leaves open the questions whether a paying party otherwise may raise and rely - and whether the adjudicator has jurisdiction to decide - on a set-off or withholding in an adjudication. There also is the question of whether a set-off or withholding can be relied upon to deny the unpaid party's right to delay works. Further complications may arise where the paying party attempts to rely as set-off a sum that arises under a different contract (not being the contract to which the adjudication relates or for which the right of delay works is exercised).

NEXT STEPS AND WAY FORWARD

As of the date of writing, the Bill was referred to the House Committee on 31 May 2024 for the formation of a Bills Committee. The Bill will be further considered by the Bills Committee and no date has yet been set for resumption of the second reading and for third reading. If the Bill is passed into legislation, according to Section 1 of the Bill, there will be a transition period of eight months from the date on which the legislation is gazetted before the legislation will come into effect.

It is important for the industry to get ready for the implementation of the statutory security of payment regime. Employers, main contractors and subcontractors alike should review their contracts and internal processes to ensure compliance and compatibility with the regime. There also will be a need for personnel from different levels to be familiar with the payment and adjudication processes introduced under the security of payment regime, including their features, requirements, and areas of flexibility, and to understand their wider implications.

BCLP has extensive experience in security of payment regimes both in Hong Kong and in various overseas security of payment jurisdictions, and from the perspectives of both employers and contractors. We are happy to discuss with you and to guide you in preparing for the coming into effect of the statutory security of payment regime in Hong Kong.

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MEET THE TEAM



Glenn Haley

Hong Kong SAR

glenn.haley@bclplaw.com

+852 3143 8450



Barry Wong

Hong Kong SAR

barry.wong@bclplaw.com

+852 3143 8419



Horace Pang

Hong Kong SAR

horace.pang@bclplaw.com

+852 3143 8411

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