



**THE LAW REFORM COMMISSION
OF WESTERN AUSTRALIA**

Project No 54

Contractors' Liens

WORKING PAPER

AUGUST 1974

INTRODUCTION

The Law Reform Commission has been asked to advise on the practical effects of enacting liens and charges legislation, (with particular reference to the South Australian and Queensland legislation), to protect the interests of persons involved in the building and construction industries.

The Commission having completed its first consideration of the matter now issues this working paper. The paper does not necessarily represent the final views of the Commission.

The Commission has been asked to submit a report by the middle of September 1974 and requests that comments be sent to it on or before 5 September next.

Copies of the paper have been sent to the

Association of Architects, Engineers, Surveyors and Draughtsmen of Australia (W.A. Division)
Associated Banks in Western Australia
Association of Consulting Engineers
Association of Painting Contractors
Australian Department of Labour & Immigration
Australian Federation of Construction Contractors
Australian Finance Conference Ltd.
Builders Registration Board
Building Industry Subcontractors Organisation
Building Owners and Managers Association
Chief Justice and Judges of the Supreme Court
Citizens Advice Bureau of W.A. (Inc.)
Clay Brick Manufacturers Association of W.A.
Commissioner of Titles
Employers Federation Inc. (W.A.)
Fremantle City Council
Housing Industry Association
Judges of the District Court
Law School of the University of W.A.
Law Society of W.A.
Local Government Association of W.A.
Local Government Department
Magistrates Institute
Main Roads Department
Master Builders Association
Master Painters Decorators & Sign-writers Association
Master Plasterers Association
Master Plumbers Association

Metropolitan Water Supply, Sewerage & Drainage Board
Painters Registration Board
Perth Chamber of Commerce
Perth City Council
Public Works Department
Real Estate Institute of Western Australia (Inc.)
Royal Australian Institute of Architects (W.A. Chapter)
Solicitor General
State Electricity Commission of Western Australia
State Department of Labour
State Housing Commission
State Minister for Works
Stirling City Council
Subcontractors and Suppliers Association
Supervised Home Builders Association
Trades' Labour Council of W.A.
Under Secretary for Law
W.A. Permanent Building Societies
West Australian Chamber of Manufacturers
Law Reform Commissions and Committees with whom this Commission is in
correspondence.

A notice has been placed in *The West Australian* inviting anyone interested to obtain a copy of the paper and to submit comments.

The research material on which the paper is based is at the offices of the Commission and will be made available on request.

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TERMS OF REFERENCE

1. The Minister for Justice, on 17th of June 1974, asked the Commission to advise on the practical effects of enacting liens and charges legislation, (with particular reference to the South Australian and Queensland legislation), to protect the interests of persons involved in the building and construction industries.
2. On 10 July 1974 the Minister for Justice indicated that he wished the Commission to deal with the project as a matter of urgency, and that he desired an interim report by 24 July. An interim report was submitted on that date setting out the tentative views arrived at by the Commission, based on the limited research it had done in the time available.
3. In its interim report the Commission recommended that it be permitted to follow its normal practice of issuing a working paper for public comment on the questions raised, before submitting a final report. The Minister for Justice accepted this proposal and asked that a report be submitted to him by the middle of September 1974.

THE LAW IN WESTERN AUSTRALIA

4. The law in this State does not place a head-contractor or a subcontractor in a privileged position to enforce payment for the work done or the materials supplied in respect of building work.

Such a person cannot, in the absence of a contractual provision, claim a lien over the land on which he works or over materials supplied or installed by him on that land. Nor can a subcontractor claim a charge on money due to the head-contractor in respect of work or materials supplied by him under his subcontract. He ranks as an unsecured creditor of the head-contractor in the event of the latter's insolvency (*Pritchett & Gold & Electrical Power Storage Co. Ltd. v. Currie* [1916] 2 Ch. 515).

5. At common law all materials and fittings once incorporated in or affixed to a building or land pass to the owner of the land. Moreover, some contracts provide that as soon as plant or materials are brought on to the building site they become the property of the owner, either absolutely, or until the work is completed. Such a provision has the effect of preventing the

plant and materials passing to the receiver or trustee in the event of insolvency of the head-contractor or his subcontractors (see generally *Hudson's Building & Engineering Contracts* (8th ed.) 362). When the property in plant or materials has passed to the owner of the land, a head-contractor or subcontractor has no lien on them or on any work constructed, unless he has expressly contracted to that effect (*Wallis v. Smith* (1882) 21 Ch. D. 243).

6. A subcontractor usually cannot by-pass the head-contractor and have recourse against the owner because there is no contract between them (*A. Vigers Sons & Co. Ltd. v. Swindell* [1939] 3 All E.R. 590, *quaere Property Law Act 1969* (W.A.) s.11). Furthermore, the owner cannot pay to the subcontractor money due to the head-contractor, unless the agreement between the head-contractor and the owner so provides (In *Re Holt, ex parte Gray* (1888) 58 L.J.Q.B. 5). Any provision authorising payment direct to a subcontractor by the owner is now rare (see *Report of the Inquiry into the Building Industry of Western Australia 1973-74* (hereinafter called "the Smith Report"), paragraphs 7.15 and 7.16), and will be strictly construed (*J.A. Milestone & Sons Ltd. v. Yates Castle Brewery Ltd.* [1938] 2 All E.R. 439, 444).

7. A head-contract can be so framed as to create a trust in favour of a subcontractor in respect of money paid by the owner to the head-contractor. This will bind the head-contractor's trustee or liquidator in the event of insolvency (see *Re Tout & Finch Ltd.* [1954] 1 All E.R. 127). In this way the owner can to some extent avoid disturbance to the contract programme. However, the Commission understands that this practice is extremely rare.

8. The *Workmen's Wages Act 1898* (W.A.) gives a workman a first charge for unpaid wages upon the money due by the owner to the head-contractor in respect of the contract, work or undertaking (s.4(1)). The Act, which limits a claim to \$20 (s.4(2)), appears to be in disuse.

LAW IN OTHER JURISDICTIONS

South Australia

9. The *Workmen's Liens Act 1893* (S.A.) enables workmen, head-contractors and subcontractors to register a lien over the land of an owner who has consented to work being

done on his land or to the supply of materials thereon. They may also register a lien over the interest in land of an occupier who has consented to work being done on that land. (A lien over land is registered at the General Registry Office when the occupier's interest is not recorded on the certificate of title to that land) (ss.4 & 5). In addition, workmen and subcontractors may claim a charge over the money payable to the head-contractor or subcontractor by whom they are employed or with whom they have contracted (s.7). A lien over the land, but not a charge over money, may be claimed in respect of the supply of materials even though not furnished in connection with work on the land of the owner (s.9b and see *Ready Mixed Concrete (S.A.) Pty. Ltd. v. Constructions (Broken Hill) Pty. Ltd.* [1963] S.A.S.R. 340). Both a lien over land and a charge over money are limited to the amount of the contract price unpaid at the time the lien over the land or charge over the money is created (ss.6 & 7(5)). A workman's lien is limited to four weeks wages and a maximum of \$200 (s.4 (3)).

10. The holder of a lien over land or a charge over money is treated as a secured creditor of the head-contractor under the bankruptcy laws (see *In Re Hollywood Homes Pty. Ltd.* [1964] S.A.S.R. 116; *Stapleton v. F.T.S. O'Donnell, Griffin & Co. (Q'land)* (1961) 108 C.L.R. 106). However a lien is subject to prior registered encumbrances on the title of the owner or occupier, but has precedence over unregistered encumbrance even those created prior to the Lien (see ss. 9, 9a and *Farrier-Waimak Ltd. v. Bank of New Zealand* [1965] N.Z.L.R. 426). On the other hand a charge is subject to any prior equities attaching to the money charged, although any assignment by the head-contractor of money payable to him under the contract is subordinated to the charge even though made prior to the notice of the charge. Thus a charge take priority over a debenture given by a head-contractor to a bank (*Albert Del Fabbro Pty. Ltd. v. Wilckens and Burnside Pty. Ltd.* [1970] S.A.S.R. 277).

11. A lien over land lapses unless it is registered within twenty eight day of the money becoming due and unless action is commenced to enforce it within fourteen days after registration (ss.10(1) and 15). Money becomes due for this purpose seven days after demand for payment to the person liable to pay the money or on that person committing an act of bankruptcy or suffering his goods to be taken in execution (s.10(2)). A charge lapses unless steps are taken to enforce it within twenty eight days after the money in respect of which the charge has arisen becomes due (s.7(3)).

12. A lien may be discharged by depositing with the Registrar-General of Deeds the amount claimed thereunder either in discharge of the lien or to abide the result of an action to enforce the lien (s.16). Liability under a charge or lien will cease upon payment into court of the amount claimed (s.26).

13. Section 8 of the Act provides for the following order of priorities as between competing liens and charges under the Act -

- (i) liens and charges of workmen (see paragraph 9 above),
- (ii) liens and charges of subcontractors;
- (iii) liens of contractors.

As between the same classes, claimants participate rateably.

14. The Crown is not bound by the Act (see s.48 and *Ready Mixed Concrete (S.A.) Pty. Ltd. v. Constructions (Broken Hill) Pty. Ltd.* [1963] S.A.S.R. 340).

Queensland

15. The *Contractors' and Workmen's Lien Act of 1906*, which was repealed in 1964, provided for liens and charges and for a statutory retention fund. It was similar in most respects to the existing New Zealand legislation. Reasons given for the repeal of the Queensland legislation were: there was no justification for giving subcontractors in the building industry any special protection over other creditors; the owner of land was "caused additional expense and embarrassed and inconvenienced in respect of a default by a person over whom he has no control" and the Act had been criticized by judges, in particular by Philp J. in *Terrazzo Tile Co. v. Willis & Sons Ltd.* [1960] Qd. R. 475 (Parl. Deb. (Q) (1963) p. 1787). Mr. Justice Philp said that the criticism of the New Zealand legislation that it was "a difficult, obscure and technical piece of legislation and one which presents serious problems in its practical application", also applied to the Queensland Act. He suggested that it be repealed, "and if a substituted Act be passed that it be made intelligible to the lawyer and the layman" (p.479).

16. The *Subcontractors' Charges Act 1974*, which came into force on 1 July 1974, to some extent replaces the repealed Queensland legislation on this subject. It does not deal with liens over land; it permits a subcontractor to claim a charge over money payable to the head-contractor and to superior subcontractors (s.5). (For the purposes of this working paper a superior subcontractor is any subcontractor who has subcontracted part or parts of his work.) It does not provide for any statutory retentions (see paragraph 28 below) or for security in respect of workmen's wages.

17. The Act provides that a subcontractor is required to give notice of his claim to a charge to the person by whom the money is payable, to the person who would, but for the claim, be entitled to receive the money payable and to a magistrate's court within thirty five kilometres of the place where the work was done (s.10). A notice can be given at any time after the subcontractor commences work, but must in any event be given within thirty days after the completion (s.10(2)).

18. A person who receives notice of a charge over money must retain sufficient money to satisfy it. Liability under the sum total of all the charges cannot exceed the contract price less any portion thereof paid prior to the notice of the charge, and in good faith and not for the purpose of defeating a charge (s.5(3) and 6). Any assignment of money payable under the contract or subcontract is void against a subcontractor's charge over that money (s.7).

19. If the head-contractor or superior subcontractor, as the case may be, does not give notice disputing the charge within seven days, he is deemed to have admitted its validity (s.11(8)). Liability under the charge may be discharged by paying the amount charged into court but it cannot be paid out of court except by order (s.11(7)). Proceedings must be commenced to enforce the charge within twenty one days after the notice of it is given, except in the case of retention money when proceedings must be commenced within two months of that money becoming payable (s.15).

New South Wales

20. The *Contractors' Debts Act 1897* provides that once a court of competent jurisdiction finds money to be due to a subcontractor for "work and labour", "material", or "material work and labour", it can issue a certificate to that effect (s.3). The certificate entitles the holder to

payment by the owner out of the money as it becomes due and payable by the owner to the head-contractor (s.9). Notice of the certificate acts as an assignment of the money, subject to any prior assignments under the Act (s.8). Once a subcontractor has served a notice that he has commenced an action against the head-contractor, the notice acts as an interim injunction and the owner must retain the money until judgment is obtained (s.14). The statutory assignment provided by the Act is good against the receiver in bankruptcy (*Re Stewart* (1943) 13 A.B.C. 229).

21. The Commission understands that the provisions of the New South Wales legislation are not often relied upon because they are considered ineffectual.

Other Australian jurisdictions

22. None of the other States or Territories of the Commonwealth has legislation giving either liens or charges to those involved in the building industry.

23. There appears to be an administrative arrangement by which head-contractors employed by the Public Works Department of Tasmania are required to make satisfactory arrangements for the payment of subcontractors as the work proceeds (see the Smith Report, paragraph 6.14). The Commission understands that the Commonwealth Department of Housing and Works seeks to protect subcontractors by using the system of nominated subcontractors and insisting that head-contractors produce receipts verifying payment to subcontractors before it pays instalments to the head-contractor.

New Zealand

24. The *Wages Protection and Contractors' Liens Act 1939* enables head-contractors, subcontractors and workmen who perform work upon or in respect of any land to claim a lien over the estate or interest of the owner in the land (s.21). Workmen and subcontractors are also entitled to a charge over money payable under any superior contract for the work (s.21). The supply of material used or brought on the premises to be used in connection with the work is sufficient to constitute "work" within the meaning of the Act (s.20), (cf. *Winstone Ltd. v. Wellington City and F.E. Seagar Ltd.* [1972] N.Z.L.R. 399).

25. A person intending to claim a lien or charge must give notice to the owner of the land and to every person who, to the knowledge of the claimant, would otherwise be entitled to receive the money (ss.28 & 29) .The notice can be given although the work is not completed (s.30(2)). The recipient of any such notice of a lien or charge is obliged to retain a sufficient sum, from the money payable or to become payable, to satisfy the claim: if he does not, he is personally liable for the amount claimed (s.31). Liability under the sum total of all liens and charges cannot exceed the contract price, less any portion thereof paid prior to receipt of notice of the lien or charge in good faith and without intention of defeating a charge or lien and without breach of the provision as to statutory retentions (see paragraph 28 below). It is an offence for a contractor who enters into a subcontract to fail to give particulars of it to the owner and all superior contractors (s.33).

26. Action to enforce a lien or a charge must be commenced within sixty days after the completion or abandonment of the work specified in the head-contract, otherwise it is extinguished (s.34(4)).

A lien has no effect until it is registered (s.41). If judgment is obtained on a claim for a lien, the court may order the sale of the land affected (s.43) .A lien may be discharged by payment of the amount claimed into court (s.40).

27. Under s.26, priority is given to competing liens and charges as follows -

- (a) liens and charges for wages not exceeding 3 months wages and up to a maximum of \$100 per worker;
- (b) liens and charges for workers' wages in so far as they are not included in (a), and the liens and charges of subcontractors;
- (c) liens of head-contractors or superior subcontractors.

Where a notice of a lien or charge is not given within 30 days of the completion of the work in respect of which it is claimed, the lien or charge drops one step in the priority order (s.26(2)).

28. Section 32 of the Act also requires the owner, and any superior contractor, to retain for thirty one days after the date of completion or abandonment of the work specified in the

contract or subcontract, the following percentages of the money that has become payable (including progress payment) since the making of the contract -

- (a) 10% of the first \$200,000 or part thereof;
- (b) 5% of the first \$800,000 or part thereof;
- (c) 2½% of the next \$1,000,000 or part thereof;
- (d) 1% of the next \$2,000,000 or part thereof; and
- (e) ¼%, of any amount in excess of \$4,000,000.

It has been held that this retention is not a special fund in favour of the claimant. For example, it is available to the owner for the purposes of satisfying a set-off or counter claim against the head-contractor (see *J.J. Craig Ltd. v. Gillman Packaging Ltd.* [1962] N.Z.L.R. 201).

Canada

29. In Canada, legislation designed to give security to persons who contribute value to land in the form of building material or work, has been in force for more than one hundred years.

30. Each of the Provinces has its own legislation which, generally speaking, is of similar import to that in New Zealand. An example of such legislation is The *Mechanics' Liens Act* of Manitoba (R.S.M. 1970, M.80). That Act provides for the registration of a lien on the land of the owner upon which (inter alia) building work is carried out. The lien may be registered in favour of any person who performs "work or service" upon or in respect of, or supplies materials to be used in, (inter alia) the construction of any building or erection on that land (ss. 4(1) and 14). Unlike the legislation in New Zealand it is possible to contract out of the Act (ss.3 and 4(1)). A lien upon registration "arises and takes effect" from the date of the commencement of work or service or upon delivery of materials (s.4(2)). Where a lien is claimed by a person other than the head-contractor the maximum amount thereof is limited to the debt owing to the head-contractor or superior subcontractor for whom the work has been done or materials supplied (s.8). Every lien ceases to exist after two years unless every effort is made to enforce it (s.22). Wages for "mechanics or labourers" are given priority over liens to the extent of thirty days wages (s.12(1)).

The Act also requires the person "primarily liable" upon a contract under which a lien may arise to deduct from payments made pursuant to the contract, 20% of the "value of work done", and to retain the same for thirty days after the work is completed (s.9(1)). Liens created by the Act operate as a charge on the amount retained (s.9(5)).

31. Additional protection is given in Manitoba by The *Builders and Workmen Act* (R.S.M. 1970, B.90), to subcontractors and workmen who have done work in or about any building, and to any person who has supplied material in connection therewith. The Act provides that all money received by the head-contractor or superior contractor on account of the contract price shall constitute a trust fund out of which such workmen, subcontractors and suppliers are to be paid for work done or material supplied before the head-contractor or superior subcontractor can appropriate any part of the fund to his own use. (ss.2, 3(1) and 3(2)). Although the Act provides no penalties for breach of the trust, the Canadian Criminal Code provides penalties for criminal breach of trust (s.282). The intention in establishing the trust fund is that if the head-contractor becomes insolvent, his workmen or subcontractors will be in a preferred position to his other creditors. Where there is a written contract between the owner and the head-contractor or subcontractor the latter may be entitled to a lien over the owner's land for the amount of the contract price (s.11).

REVIEW OF LEGISLATION IN OTHER JURISDICTIONS

32. With the exception of the recently enacted Queensland *Subcontractors' Charges Act 1974*, the legislation existing in other jurisdictions designed to give special protection to head-contractors and subcontractors in the building industry was enacted many years ago. At that time the present day complex chain of subcontractors, specialists and consultants did not exist. Possibly as a consequence legislation of this type has over the years been the subject of criticism and review.

33. In 1965 a committee under the chairmanship of Mr. D.F. Dugdale recommended that the existing New Zealand legislation be replaced with something more workable. However, the report of that committee has itself been the subject of much review and no steps have been taken to repeal the legislation or to enact any other. In 1967 a commission of inquiry into the *Mechanics' Lien Act* of Alberta recommended its repeal. The Law Reform Commission of British Columbia and Ontario, although not recommending repeal of similar legislation in

those Provinces, reported that many submissions to the respective Commissions advocated repeal (see Law Reform Commission of British Columbia, working paper No.5, Sept. 1971; Ontario Law Reform Commission, Report on *Mechanics Liens Act*, Feb. 1966).

34. In South Australia, because of misgivings as to the operation of the legislation in that State, the Law Reform Committee has been asked to undertake a review of it. In 1962 the Statute Law Revision Committee of Victoria recommended against the enactment of legislation providing for liens and charges, but is currently considering the need for legislation in this area.

DISCUSSION

(a) General

35. In his report, Mr. C.H. Smith Q.C. recommended (inter alia) that -

"legislation based upon the *Workmen's Liens Act 1893-1964* (S.A.) be enacted. Such legislation should bind the Crown and the financial protection which it affords should extend to all subcontractors and workmen, but not to persons who supply material and not services" (the Smith Report, paragraph 10.3.B(iii) p.74).

36. Legislation of the type recommended by Mr. Smith seeks to resolve the conflicting interests of the owner on the one hand, in limiting his responsibility to payment of debts he himself has incurred, and those of the sub-contractor on the other, in being paid for the work he has done.

37. The Question arises whether the law should be amended to provide a privileged position for certain persons in the building industry, when it leaves other creditors unprotected. Mr. Smith has suggested that special privileges should be given to subcontractors because his enquiries indicated that very few head-contractors actually performed much building work. He found that subcontractors carry out between 80% - 90% of the actual construction work in the house building sector and approximately 60% - 70% in larger projects (the Smith Report paragraph 2.15). Further, his Report indicates that there has been an unduly high incidence of insolvency in the building industry, particularly of building companies with small paid up capital, and this has occasioned substantial loss to building subcontractors (the Smith Report ch. 7).

38. The underlying arguments in support of the need for legislation providing for liens or charges seems to be -

- (a) that the subcontractor has by his work improved the value of the owner's land, and
- (b) that the owner should take some responsibility for the payment of subcontractors by reason of his having initiated the project.

However, even if it is assumed that legislation placing subcontractors in the building industry in a privileged position is desirable in principle, it is necessary to consider whether legislation can be devised which work satisfactorily, which does not affect unduly the rights and interests of others, and which in fact assists those for whose protection it is devised. Paragraphs 40-76 discuss major problems associated with legislation providing for liens or chares, based on experience in other jurisdictions.

39. In addition to studying the report referred to in paragraphs 33 and 34 above, a research officer of the Commission went to South Australia and discussed the operation of the legislation in that State with a cross section of persons concerned with it, including the chairman of the South Australian Law Reform Committee, Mr. Justice Zelling; the solicitor for the Master Builders' Association; two solicitors with wide experience in the area of contractors' liens; the Director of the Public Buildings Department; a representative of the Building Industry Sub-Contractors Association; a debt collecting agency and certain Government departments.

The Commission has also discussed the matter generally with Mr. C.H. Smith Q.C., who conducted the inquiry into the building industry of Western Australia in late 1973 and early 1974.

(b) Some problems common to both liens and charges

(i) Finance for head-contractors and subcontractors

40. The existence of legislation providing for liens or charges may make it harder for a head-contractor or even a subcontractor to obtain the money necessary to finance the building

project in its early stages. Usually no money becomes payable to the head-contractor until a significant part of the building work has been done. He or his subcontractor must therefore rely on their own resources in the initial stages of the project.

41. The Commission is informed that the most usual security taken by lending institutions for advancing money to builders is a floating charge or bill of sale over their assets. However, the claim of both a lien holder and a charge holder take precedence over such a security, even though the security may have been created prior to the registration of the lien over the owner's land or the creation of a charge over money payable to the builder (see *Dales Freightways Ltd. v. N.Z.F.P. Ltd.* [1970] N.Z.L.R. 150; *Albert Del Fabbro Pty. Ltd. v. Wilkins and Burnside Pty. Ltd.* [1970] S.A.S.R. 277; see also paragraph 10 above). The result is that banks, in particular, are reluctant to advance money to any builders but those of considerable substance, unless they can obtain a satisfactory security such as a first mortgage over the land of the builder.

42. A similar problem operates for the supply of materials to contractors, particularly subcontractors. Sometimes contractors assign the benefit of a building contract to the supplier in consideration of supply of materials on credit to the contractor. However, because the legislation under review renders such an assignment void or ineffective as against any subcontractor (or sub-subcontractor), such a security may well be worthless (see *Ashby Bergh & Co. Ltd. v. R. Powley & Co. Ltd.* [1970] N.Z.L.R. 906; *Albert Del Fabbro Pty. Ltd. v. Wilkins and Burnside Pty. Ltd.* (supra)). This could make it more expensive or difficult for contractors to obtain goods on credit, unless suppliers themselves were given the protection of the legislation (see paragraph 66 below).

43. If the legislation is to be effective, the commission is unable at present to see any satisfactory answer to the problems created by the subordinate position in which finance institutions, and others who provide credit to contractors in the building industry, are placed in as a result of the creation of a lien or a charge.

(ii) *Creation of liens and charges*

44. There has been a considerable amount of litigation in New Zealand and South Australia on the question of the point of time at which a lien or charge can arise. In New

Zealand a lien over land can be created as soon as the contract is entered into (see paragraph 25 above). In South Australia however, since the money must be due under a contract, it appears the work must be completed or a progress payment due (see paragraph 11 above). The ascertainment of the time of completion also raises difficult questions. The greatest difficulties seem to have arisen in relation to charges. There is some doubt as to whether a charge can arise before work under the subcontract is completed, and if so, whether it relates back to when the contract was made or when the work commenced, or whether it relates back at all (see *Miller's Lime Ltd. v. Royal Agricultural and Horticultural Society of South Australia* [1936] S.A.S.R. 306; *W. Curl & Sons v. Buck Industries Pty. Ltd. and Dillingham Constructions Pty. Ltd.* (1972) 2 S.A.S.R. 335; *Stucoid Pty. Ltd. v. Stadiums Pty. Ltd.* (1960) 107 C.L.R. 521 and *Pitt Ltd. v. The Corporation of the Town of Glenelg* [1927] S.A.S.R. 501). These questions are relevant in determining priorities between competing liens or charges and with other securities.

45. Some of these difficulties could probably be overcome by drafting. For example the legislation could provide that a lien or a charge arises at the time the total money or a progress payment is due, whether under the head-contract or subcontract. Alternatively, it could arise when the work commences or when it is completed. Difficulties in practice may arise whichever alternative is chosen. For example, the parties may be able to avoid the legislation by not providing for progress payments in a subcontract. If the relevant time is when work is completed under the head-contract, this could penalise a subcontractor who completed his work in the early stages. If the relevant time is immediately work commences, this may tend to reduce cash flow to the head-contractor with consequent disruption.

(iii) *Amount payable*

46. Where a contract provides that the entire work is to be completed before payment is due, it follows that no money becomes payable if the work is abandoned before completion (see *Sumpter v. Hedges* [1898] 1 Q.B.673). Where the contract price is payable by instalments, money due at the time of abandonment is payable subject to any deduction for damages (*Hanak v. Green* [1958] 2 Q.B.9). If the head-contractor abandons the work before money becomes due to him the charge or lien has no effect, irrespective of whether or not the subcontractor has finished his work.

47. The question arises whether the legislation should provide (as it does in South Australia, Queensland and New Zealand) that the owner cannot be liable, in respect of a charge or lien, to pay more than he is liable to pay the head-contractor. The Commission tentatively favours the approach adopted in these other jurisdictions.

48. The completion date of work is not always easy to ascertain. Work may be substantially completed, yet defects remain to be corrected. The original completion date may be altered because the head-contractor has done additional work. Also renegotiated contracts can lead to difficulties in this context. In one case, the consequence of a renegotiated contract was that even though a new contract had been made the owner was held to be liable to pay money to a subcontractor when he was under no contractual obligation to pay anything to his head-contractor (see *Bank of New Zealand v. Cemas Modular Industries Ltd.* [1972] N.Z.L.R. 661). Possibly these problems could be overcome by providing that work is deemed to be completed upon possession being given and taken or then the architect certifies completion, as the New Zealand Dugdale Committee recommended (Dugdale Report paragraph 21). But there could be difficulty if possession is taken of only part of the building or is taken before the date specified for completion in the contract.

49. The Commission's enquiries reveal that subcontractors seem reluctant to resort to charges or liens as a matter of course, for fear of antagonising contractors and reducing their chances of obtaining further contracts. They do not usually seek to register a lien or create a charge for money due to them until they suspect the contractor or superior subcontractor will have difficulty in paying them. By this time the owner may well have paid over a substantial proportion of the contract price and, even if at the time the charge or lien is created money is due to the head-contractor, it is often insufficient to satisfy the debt to the subcontractor. Enquiries in South Australia suggest that on average little more than 5% of lien holders or charge holders are paid in full.

50. The experience in South Australia is that where one charge or lien is created this encourages others to seek security for the debts due to them. This prevents the owner advancing any further money to the head-contractor until the charges or liens are satisfied, which often removes the latter's incentive to continue the job. In such an event usually no money becomes payable to him by the owner and so no money becomes payable under the charges or liens. Possibly if the job had continued to completion or to the next stage, there

may have been sufficient funds to meet at least part of the charges and liens. This appears to be a problem of business confidence, rather than a legal problem and therefore almost impossible to overcome by statute.

51. As previously mentioned, under the statutory schemes studied it has been held that an owner is entitled to deduct damages from money which is payable to the head-contractor (see paragraph 47 above and *J.J. Craig Ltd. v. Gillman Packaging Ltd.* [1962] N.Z.L.R. 201: *Metropolitan Brick Co. v. Hayward* [1938] S.A.S.R. 462). Thus any delay caused by the creation of a charge or a lien may defeat the subcontractors, since compensation for the delay to the owner will be taken from the amount otherwise available to satisfy the charge or lien.

52. The right of an owner to deduct damages from money held by him pursuant to the liens legislation was criticised by the Dugdale Committee which considered that this power should be abolished in order that the object of the statute be fulfilled (the Dugdale Report paragraph 17). But for the statutory requirement to withhold money to satisfy the charge or lien, the owner may well have paid the money to the head-contractor. Damages for any defect in the works which subsequently arose could not of course have been deducted from this money.

(iv) *Settlement or compromise of claims*

53. If more than one subcontractor has a charge or a lien and one refuses to remove his lien or charge, the liquidator of an insolvent head-contractor may be prevented from entering into a scheme of arrangement to enable the works to be finished and the subcontractors paid at least in part. It should also be noted that even though a subcontractor may have registered a lien over the owner's land or created a charge over money due from him to the head-contractor, he may not be able to enforce them where the owner is a company in liquidation, without leave of the court (see *Companies Act (W.A.)* ss. 181, 230 (3) and 263 (2); see also *In Re Hollywood Homes Pty. Ltd.* [1964] S.A.S.R. 116 and R.D. Elliott *The Artificer's Lien* pp. 101-102).

(v) *Frivolous or vexatious liens and charges*

54. Because a lien or a charge can embarrass the owner it would be necessary to consider to what extent, if any, provision should be made requiring a claimant to justify his lien or charge before it becomes effective. Neither the South Australian, New Zealand or Queensland legislation requires a claimant to do so. Legislation in the last two mentioned jurisdictions renders the vexatious claimant liable to damages, but this may not be satisfactory unless he is a person of means (see the *Wages Protection and Contractors' Liens Act* (N.Z.) s.45 and the *Subcontractors' Charges Act* (Qld.) s.22). The South Australian legislation imposes a penalty of \$100 or imprisonment for six months for lodging a vexatious lien or charge (The *Workmen's Liens Act* (S.A.) s.33). The Commission is informed that subcontractors in South Australia register liens even though there is a good reason why they have not been paid by the head-contractor (e.g. faulty work). Although this device is often effective in extracting payment from the head-contractor, the Commission was informed that the practice is giving rise to concern because of the increasing tendency of subcontractors to adopt it.

55. It is often essential for the subcontractor to register his lien over the land of the owner quickly. A possible abuse of the scheme arising out of this need is where subcontractors register liens over all such pieces of the owner's land that could conceivably be relevant without making proper inquiry as to the exactly relevant piece. This practice is also giving rise to concern in South Australia.

56. In many cases a number of liens are registered or charges created in respect of money claimed in liens or charges registered or created by another person. Thus some of the money claimed by a head-contractor will be to pay the subcontractor who may also have registered a lien or created a charge securing the debt due to him by that head-contractor. Consideration might therefore be given to confining a subcontractor to charging the money due to his immediately superior contractor (cf. *Workmen's Liens Act* (S.A.)s.7).

(c) **Problems with respect to liens only**

57. Unlike a charge over money, a lien operates as an encumbrance against the owner's land and so restricts his right to deal with it. The registration of a lien over land can lead to financial loss to the owner, whether or not the lien is justified. Experience in South Australia

is that persons who are relying on building mortgages to construct a dwelling house, for example, find that the financier will not advance further money under the mortgage until the lien is removed, because the security over which the money is advanced is no longer unencumbered. This of course can cause hardship, particularly since the registration of one lien tends to bring in others (see paragraph 50 above). Similar problems to those referred to in paragraph 60 below may also arise.

58. Where a lease is registered against the land of the owner, that owner runs the risk of having a lien registered over his land to the extent of the interest created by the lease because of work done for the lessee. The registration of such a lien may act to the detriment of not only the lessee but also the owner. There are also problems where an owner sells under a term contract a house which is partly constructed. The new owner may find that subsequently his land becomes encumbered by a lien for work performed for the original owner.

59. It is difficult to see why in most circumstances a charge alone rather than a lien over land should not meet the needs of a subcontractor. However, where the head-contractor is also the owner of land (as with many speculative builders), the registration of a lien over his land could prove an effective means of securing a debt due by that owner to the subcontractor. In such cases many of the objections applicable to innocent owners are not relevant. The Queensland *Subcontractors' Charges Act 1974* in contrast to the legislation repealed in that State in 1964, does not give a subcontractor the right to a lien over land.

(d) Problems relating to charges only

60. As with a lien the existence, or possibility of the existence, of a charge can considerably delay work. The courts in South Australia have suggested that no formal notice of a charge is necessary, verbal notice being sufficient (see *Millar's Lime Ltd. v. Royal Agricultural and Horticultural Society of South Australia* [1936] S.A.S.R. 306). The practice in that State is for most architects to refuse to issue a certificate for payment where they suspect a charge over money may arise. This is done to protect the owner by ensuring that he will not be rendered liable to pay both the head-contractor and the subcontractor. A refusal to issue a certificate would result in a delay of payment to the head-contractor with resultant embarrassment to the subcontractors.

61. In practice in South Australia holders of money subject to a charge have sometimes considered it prudent not to payout the money without first obtaining directions from the court. The costs occasioned are usually ordered to be paid from the money charged thereby reducing the amount available to subcontractors. The Commission consider that it would be proper for a similar course to be adopted in this State if legislation of the type now under review was enacted.

(e) **Other matters**

(i) *Delays*

62. One of the difficulties with liens and charges is the delay in enforcing them. This may adversely affect not only the claimants but also the owner of land. In South Australia it takes between six and nine months for the court to hear a claim in respect of a disputed lien or charge. The Registrar-General in that State informed the Commission that there were a number of liens which had been registered against the title for five years.

63. The Commission understands that in Queensland it was considered that delays were less in the Magistrates' Court than in the Supreme Court and that it was for this reason that the Queensland legislation gives the Magistrates' Court exclusive jurisdiction to determine disputes over charges. In New Zealand the Magistrates' Court has concurrent jurisdiction with the Supreme Court to enforce charges and liens. In South Australia, both the Local Court and the Supreme Court have jurisdiction within their normal limits.

The Commission favours the South Australian approach in this respect.

64. Experience in South Australia is that a claimant issues process to comply with the statutory requirement to enforce the charge or the lien within the time limit and then, in most cases, leaves the owner to pursue the matter or negotiate a compromise of the claim. There may thus be point in limiting the time for which a lien or charge remains effective, with power for the court to extend that time (see the Dugdale Report, paragraph 9).

65. In an endeavour to avoid unnecessary argument and delay the Queensland *Subcontractors' Charges Act 1974* provides that unless a head-contractor or superior

subcontractor on whom notice of claim of charge is served, denies within seven days his liability to pay the amount claimed, he is deemed to have admitted it (s.11(8)). This appears to be undesirable.

(ii) *Supply of materials*

66. In South Australia a supplier of materials cannot claim a charge over money unless he also does "work" in connection with his contract. This restriction does not apply in the case of a lien over the owner's land (see paragraph 9 above). In New Zealand a supplier of material only can claim both a lien and a charge, provided that the materials were supplied for or in connection with the work in question (see paragraph 24 above). A similar situation appears to exist under the Queensland legislation, as far as charges are concerned. The Commission is tentatively of the opinion that suppliers should be excluded from the operation of any legislation since they are generally in a better position than subcontractors to protect themselves from bad debts. Mr. Smith recommends that suppliers of material who do not also provide services be excluded from any proposed legislation (see the Smith Report, paragraph 10.3.B(iii)).

(iii) *Statutory retention*

67. The New Zealand legislation (as did the former Queensland legislation) requires the owner to retain a fixed percentage of money payable under the head-contract in addition to the money required to meet a particular lien or charge (see paragraph 28 above). No such retention is required under the South Australian or existing Queensland legislation.

The operation of the New Zealand scheme has caused considerable complexities and met with criticism, some of which is referred to in paragraphs 68 to 71 below.

68. The requirement for statutory retention has been criticized because it reduces the amount of money available to head-contractors and to subcontractors. This may place a sub-subcontractor at a disadvantage because each superior subcontractor as well as the head-contractor and owner is required to retain the appropriate statutory percentage of his contract price. Thus more than the statutory percentage of the head-contract is ultimately retained. The

cash flow becomes even more restricted where money in addition to the statutory retention is held back to satisfy a charge or a lien and to comply with retention provisions of the contract.

69. The existence of a statutory requirement to retain part of the contract price may lead to abuse. A head-contractor or superior subcontractor might hold back more than the statutory requirement to protect himself against liens or charges over money retained, which would otherwise be paid to him. Any such additional retention would be in breach of contract.

70. Another problem arises in connection with the requirement for the owner to hold back the money under the head-contract for a period after the works are completed. This can penalise a subcontractor, the nature of whose work is such that it is done at the early stages of the job. An accumulation of money withheld from a subcontractor in such circumstances could create hardship for him.

71. As the courts have decided that an owner is entitled to deduct damages due from the head-contractor to him the retention fund can in some circumstances be of little or no use to the subcontractor (*J.J. Craig v. Gillman Packaging Ltd.* [1962] N.Z.L.R. 201; and see paragraphs 51 and 52 above). The difficulties in ascertaining the date of completion of work referred to in paragraph 48 are also applicable (see *Bank of New Zealand v. Cemas Modular Industries Limited and Others* [1972] N.Z.L.R. 661).

(iv) *Statutory trust in favour of subcontractors*

72. The Commission has only briefly examined the trust scheme which operates in Manitoba (see paragraph 31 above). Such material as has been available to the Commission suggests that the larger and financially stable head-contractors have no trouble operating a separate trust account for each job. However, it appears that smaller head-contractors rarely abide by the trust provisions in the absence of strict audit requirements. Unless there was a fidelity bond scheme to protect those who suffer as a consequence of the breach of trust the scheme would be of little benefit to subcontractors, except in the case of bankruptcy where money was due and unpaid to the bankrupt (see paragraph 7 above). Legislation to enforce trust provision by creation of a separate offence would probably be largely ineffective, and it would appear to be difficult to prove any such breach.

(v) *Interstate contractors*

73. The Commission understands that a number of building contractors whose operations are based in other States are now carrying on business in this State. The question of whether a contractor based in another State would be bound, if any legislation similar to that in South Australia or Queensland were enacted, needs consideration (see *w. Curl & Sons v. Buck Industries Pty. Ltd. and Dillingham Constructions Pty. Ltd.* (1972) 2 S.A.S.R. 335). Parties to a head or subcontract may provide that it is to be interpreted in accordance with the law of another State. There may also be some difficulties in enforcing a lien or charge against a company or person resident interstate because of the geographical limits on the jurisdiction of the courts in this State.

(vi) *Workman's wages*

74. With the exception of Queensland, most of the legislation examined by the Commission enables workmen to claim some protection for unpaid wages. In South Australia, a charge or lien in respect of unpaid wages is limited to four weeks wages and a maximum of \$200, but has first priority (see paragraph 13 above). The Commission was informed that such claims under the South Australian legislation are rare. In New Zealand, unpaid wages for a period up to three months and a maximum of \$100 per worker is given first priority, while any remainder ranks equally with those of subcontractors (see paragraph 27 above). Criticism has been made of the New Zealand provision in setting the amount of the priority (\$100) at an unrealistic level.

75. The Commission at this stage expresses no view as to whether liens or charges legislation should extend to workmen. This question would need to be examined having regard to existing industrial legislation and other forms of protection available to workmen. If it is to be so extended it would be necessary to consider the maximum amounts (if any) in respect of which a lien or charge should apply and the period for which it should relate. It would also be necessary to consider the priority which should attach to wages: some limit may be necessary if the sum total of workmen's liens or charges is not to operate to defeat claims of subcontractors.

(vii) *The Crown*

76. In South Australia the Crown is not bound by either liens over its land or charges over money payable by it (s.48 and see *Ready Mixed Concrete (S.A.) Pty. Ltd. v. Constructions (Broken Hill) Pty. Ltd.* [1963] S.A.S.R. 340). The New Zealand legislation protects "any land vested in the Crown or in any local authority or public body" from the operation of the Act (s.50). However, in the Queensland legislation the Crown is bound (*Subcontractors' Charges Act 1974* s.4). As a substantial proportion of building operations in this State are carried out by or on behalf of the Crown, it would seem desirable that it be bound by any provisions relating to charges.

COMMISSION'S TENTATIVE VIEWS

77. The Commission's tentative views are -

- (a) that it would be undesirable at the present time to introduce legislation designed to protect head or subcontractors by liens against the owner's land:
- (b) that a scheme could be devised: to protect subcontractors by legislation creating a charge in their favour. The Commission tentatively suggests that such a scheme should be confined to money not yet paid by the owner to the head-contractor at the time notice of charge is given. There are however difficulties, some of which are referred to in this working paper, which require to be resolved in order to make such a system operate satisfactorily.

78. An alternative approach to the problems created by insolvencies of head and subcontractors may be to give consideration to the implementation of the licensing and insurance provision mentioned in paragraph 10.3.A of the Smith Report.

79. The Commission would welcome comment on any of these views or on any other matter arising out of this paper.

The Commission emphasises that it has been asked to report by the middle of September next. Comment should therefore be sent to the Commission by 5 September.