



COVERSHEET

Minister	Hon Dr Megan Woods	Portfolio	Building and Construction
Title of Cabinet paper	Construction Contracts (Retention Money) Amendment Bill: Further policy decision	Date to be published	11 November 2022

List of documents that have been proactively released

Date	Title	Author
February 2022	Construction Contracts (Retention Money) Amendment Bill: Further policy decision	Office of the Minister for Building and Construction
9 February 2022	Construction Contracts (Retention Money) Amendment Bill: Further policy decision DEV-22-MIN-0006 Minute	Cabinet Office

Information redacted

YES

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

In Confidence

Office of the Minister for Building and Construction
Chair, Cabinet Economic Development Committee

Construction Contracts (Retention Money) Amendment Bill: Further policy decision

Proposal

- 1 This paper seeks policy approval for changes to be made to the Construction Contracts (Retention Money) Amendment Bill (the Bill) via a Supplementary Order Paper.

Executive Summary

- 2 The Bill makes changes to help ensure that retention money that is payable to subcontractors is available and easily identifiable when that payment is due.
- 3 The Transport and Infrastructure Committee received 42 written submissions on the Bill and heard seven oral submissions. Submitters were largely supportive of the general intention of the Bill to clarify and strengthen the retention money regime. However, submitters wanted more clarity around how the new offences in the retention money regime would be enforced.
- 4 I propose that a Supplementary Order Paper address this by clarifying that the Ministry of Business, Innovation and Employment (MBIE) will enforce the retention money regime.

Background

Summary of the Bill

- 5 The Construction Contracts Act 2002 regulates construction contracts. This includes the payment terms, dispute resolution process and protection of retention money in construction contracts.
- 6 The Construction Contracts (Retention Money) Amendment Bill (the Bill) makes changes to the retention money regime in the Construction Contracts Act to strengthen and clarify the existing requirements.
- 7 Retention money is an amount held back by a party A to a construction contract (a “payer”, for example a head contractor) from an amount payable to a party B to the contract (a “payee”, for example a subcontractor), as security for performance of the subcontractor’s obligations under the contract.
- 8 The holding of retention money is voluntary. If held, retention money is commonly between two and ten per cent of the contract value. It is often paid out after 12 months, following the expiry of the defect repair period.

- 9 The Bill was introduced on 1 June 2021 and reported back to the House on 22 November 2021 and is awaiting its second reading. As reported, the Bill:
- 9.1 clarifies that retention money is held on trust by party A for the benefit of party B, and requires it to be kept separate from other money or assets;
 - 9.2 clarifies that the withheld money becomes retention money as soon as possible;
 - 9.3 requires retention money to be held in a separate bank account in a registered bank in New Zealand or in the form of a complying instrument (such as an insurance policy or a guarantee);
 - 9.4 requires party A to give information about the retention money to party B when the money is first retained and then at least every three months;
 - 9.5 introduces offences and penalties for the company and its directors for not complying with these requirements; and
 - 9.6 clarifies that if party A becomes insolvent, the receiver or liquidator becomes trustee of the retention money for the purpose of collecting and distributing it, and is entitled to be paid reasonable fees and costs for doing so.

Supplementary order paper

- 10 The Transport and Infrastructure Committee received 42 written submissions and heard seven oral submissions on the Bill. Most submitters supported the general intention of the Bill to clarify and strengthen the retention money regime, but recommended changes to improve the effectiveness and workability of the Bill.
- 11 Following submissions, officials identified that further clarification is needed to specify who will investigate and enforce the retention money offences introduced by the Bill.
- 12 To address this, I propose to amend the Bill by Supplementary Order Paper to give the Chief Executive of MBIE the ability to investigate and enforce the retention money offences, if the Chief Executive considers that it is desirable to do so.

Offences and penalties introduced in the Bill

- 13 The Bill introduces offences, penalties and defences for companies and their directors who fail to comply with the retention money requirements. This is in line with Cabinet's previous decision to introduce offences to deter head contractors from not complying with the regime [CAB-21-MIN-0074 refers].

14 The Bill has introduced the following offences:

New section of Bill	Offending Act	Associated penalty if convicted
18DA(1)	Failure to comply with new section 18D, which requires retention money to be: <ul style="list-style-type: none"> • held on trust as cash in a separate bank account and/or a complying financial instrument, and • used only to remedy defects in the performance of the subcontractor's obligations, and with the 10 working days' written notice. 	The head contractor is liable to a fine not exceeding \$200,000 for each instance of breach. If the head contractor is a body corporate, each of its directors commits an offence and is liable to a fine not exceeding \$50,000 for each instance of breach. It is a defence for the head contractor and a director of the head contractor company if all reasonable steps were taken to ensure that they complied with new section 18D.
18FC(7)	Failure to comply with new section 18FC, which requires the head contractor to keep proper accounts and records of retention money held for the subcontractor, including records of: <ul style="list-style-type: none"> • the amount • where it is being held, and • the form it is being held. 	The head contractor is liable for a fine not exceeding \$50,000 for each instance of breach.
18FD(7)	Failure to comply with new section 18FD, which requires the head contractor to provide the subcontractor with information about the : <ul style="list-style-type: none"> • amount • construction contract under which it is retained • date of retention • total amount of retention money held for the subcontractor • details for any bank account or complying instrument where retention money is held for the subcontractor, and • availability of these records for inspection by the subcontractor <p>The head contractor must provide this information when the retention money is first withheld, and at least every three months until the retention money is released.</p>	The head contractor is liable for a fine not exceeding \$50,000 for each instance of breach.

15 The Bill does not specify who will enforce the newly introduced offences. This means that if there is a breach of the strengthened retention money

requirements, subcontractors must pursue adjudication or civil action against the head contractor themselves.

- 16 Submitters on the Bill supported the introduction of offences but also wanted clarity on who will enforce the retention money regime. Eleven of the 19 written submissions received on the offence provisions and all seven oral submissions agreed that for there to be a genuine deterrent effect the government should enforce the offences in the Bill.
- 17 It is difficult for a subcontractor to enforce their rights because there is a power imbalance between subcontractors and head contractors. For example, a subcontractor pursuing adjudication or civil action against the head contractor is both time-consuming and costly, and could also potentially prevent future work from coming to them. Without a clear regulator, this power imbalance would remain unresolved

MBIE is best placed to the offences introduced in the Bill

- 18 To address these issues, I propose that the Chief Executive of MBIE is given the function to investigate and enforce the newly introduced offences in the Bill, if the Chief Executive considers that it is desirable to do so. For example, this may be where, following investigation, there is a compelling public interest in prosecution.
- 19 MBIE is best placed to enforce the offences introduced in the Bill because it is the system steward and central regulator of the building regulatory system.
- 20 I propose that this new function be funded through the building levy. Section 53(1A)(b) of the Building Act 2004 states that the Chief Executive of MBIE may use the building levy for, or in connection with, the performance of the Chief Executive's functions under any other Act that relates to the building sector or any part of the sector. This applies here because the Construction Contracts Act regulates how construction contracts used by the building sector work.
- 21 In addition to the investigation and enforcement functions, I also propose that the building levy be used to fund additional complementary functions for MBIE to:
- 21.1 provide information and education on the retention money regime;
 - 21.2 monitor compliance with the retention money regime; and
 - 21.3 provide advice to the Minister for Building and Construction on the retention money regime.
- 22 These additional functions would support MBIE's investigation and enforcement functions. For example, the monitoring function could alert the Chief Executive of MBIE to possible compliance actions that need to be taken. These additional functions would also support MBIE in its role as steward of the building regulatory system.

- 23 In order to be able to use the building levy for the purposes above, Cabinet must agree to amend the Bill to provide for this function in legislation.

Next steps

- 24 I intend to table a Supplementary Order Paper following Cabinet approvals and drafting by the Parliamentary Counsel Office, Confidential advice to Government

Financial Implications

- 25 There are financial implications for the building levy account as that is where the funding for the proposed functions will come from. Officials advise that it is not yet clear how many cases will be prosecuted annually, but note that the Chief Executive of MBIE must first consider that it is desirable to take an enforcement action. However, the assumption is that there will be one or fewer cases a year.

Legislative Implications

- 26 The proposal in this paper will be implemented through a Supplementary Order Paper to the Bill. I plan to seek approval to table this Supplementary Order Paper through the Cabinet Legislation Committee in March 2022.

Impact Analysis

- 27 Treasury's Regulatory Impact Analysis Team has determined that the proposal to amend the Construction Contracts Act, in order to clarify enforcement of offences introduced in the Construction Contracts (Retention Money) Amendment Bill, is exempt from the requirement to provide a Regulatory Impact Statement on the grounds that it has no or only minor impacts on businesses, individuals, and not-for-profit entities.
- 28 The Climate Implications of Policy Assessment (CIPA) team has been consulted and confirms that the CIPA requirements do not apply to this proposal as the threshold for significance is not met.

Population Implications

- 29 There are not expected to be significant implications on specific population groups as a result of the recommendations in this paper.

Human Rights

- 30 The proposals in this paper are consistent with the New Zealand Bill of Rights Act 1990 and the Human Rights Act 1993.

Consultation

- 31 The following agencies and Crown entities were consulted on the proposals in this paper: Ministry of Housing and Urban Development, the Treasury,

Te Puni Kōkiri, Kāinga Ora, Department of Internal Affairs, Ministry for the Environment, Ministry of Health, Ministry of Education, Department of Corrections, Ministry of Justice, Waka Kotahi NZ Transport Agency, Inland Revenue Department, Infrastructure Commission, and WorkSafe New Zealand. No issues were raised regarding the proposal in this paper.

32 The Department of the Prime Minister and Cabinet has been informed.

Communications

33 No communications are planned for this policy paper. Following the tabling of a supplementary order paper, MBIE will inform affected stakeholders of the policy decisions in this paper as part of communications regarding the passing of the Bill.

Proactive Release

34 This paper will be published on MBIE's website within 30 business days of decisions being confirmed by Cabinet, subject to withholdings as appropriate and consistent with the Official Information Act 1982.

Recommendations

The Minister of for Building and Construction recommends that the Committee:

1 **note** that the Construction Contracts (Retention Money) Amendment Bill, which makes changes to the retention money regime in the Construction Contracts Act 2002 to strengthen and clarify the existing requirements, was reported back to the House on 22 November 2021 and is awaiting its second reading;

Supplementary order paper

2 **agree** that the Chief Executive of the Ministry of Business, Innovation and Employment is given the function to investigate and enforce the newly introduced offences in the Construction Contracts (Retention Money) Amendment Bill, if the Chief Executive considers that it is desirable to do so;

3 **agree** that this retention money regime investigation and enforcement function be funded through the building levy;

4 **agree** that the building levy be used to fund functions that will support the Ministry of Business, Innovation and Employment's retention money regime investigation and enforcement function, namely to:

4.1 provide information and education on the retention money regime;

4.2 monitor compliance with the retention money regime; and

4.3 provide advice to the Minister for Building and Construction on the retention money regime;

Legislative implications

- 5 **authorise** the Minister for Building and Construction to issue drafting instructions to the Parliamentary Counsel Office to give effect to the above recommendations;
- 6 **authorise** the Minister for Building and Construction to make additional policy decisions and minor or technical changes, consistent with the policy intent of this paper, on issues that arise during the drafting of the Supplementary Order Paper and regulations.

Authorised for lodgement

Hon Poto Williams
Minister for Building and Construction