

Contractor's Right Of Action For Late Or Non-Payment By The Employer

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Abstract

Late or non-payment of interim payment to Contractors has been a major issue in the Malaysian Construction Industry. It has affected the performance of Contractors and has caused several of them not being able to complete the work on time thus causing delay in the completion of the project. In the worse scenario, they are forced to abandon their projects for lack of fund and some were on the brink of bankruptcy. This should not be the case because it is clearly stated in the various standard form construction contract used in Malaysia i.e. the PWD203A (Rev 1/83), PAM 1998/2006 and CIDB 2000, that the Contractors must be paid within 30 days, 14 days and 21 days after his receipt of the Interim Certificate respectively. Apart from arbitration, what other remedies available to the Contractor when he is not paid on time or have not been paid at all by the Employer. This paper is written based on a master thesis entitled "The Contractor's Right of Action for Late or Non-Payment by the Employer". The objective of the research is to determine the various actions that a Contractor can take in the event of late or non-payment by the Employer. The research focuses only on the issue of late or non-payment of Interim Certificate. It is based on the study of the PWD 203A (Rev 83), PAM 98/2006 and CIDB 2000, common law principles and case laws. This research carried out by adopting from combination of document analysis, case law and review of act and statute. This study involve in legal matter, which can only be carried out based on court decision which reported in MLJ, MLJA, MLJu etc and this study is more Qualitative research. The study suggested that a when faced with the problem of late or non-payment by the Employer the Contractor may either suspend the work, claim for interest, apply for summary judgment, apply for the winding up of the Employer's company or he may determine the contract with the Employer. But consideration must be given to the actual construction of the contract and details of each case.

Keywords: *Interim payment, Contractors, Late payment, Non Payment, Construction Contract*

1. Introduction

Over many decades there has been a multitude of industry appellation about the relationship between the construction industry and payment.⁴ Payment is considered as the lifeblood of the construction industry because constructions often involve very large capital outlay and take a considerable time to complete.⁵ It is beyond the means or capacity of most Contractors to complete the whole of the construction work before they get paid. This is especially so among the medium and small size Contractors or when the works involve millions of ringgit. They need some form of regular or periodic financial injection to maintain their cash-flow to continue with their work in a diligent manner. It is a common arrangement under most contracts for Contractors to be paid progressively at regular intervals.

Any hitch to such an arrangement could spell a disaster, not only for the Contractor but also to the owner and the project itself. A failure of the Contractor getting regular and timely payment could result in project delay, reduced profitability and in the extreme case, the company may go into liquidation.⁶ It will also have a knocking effect on the whole of construction business chain because the Contractor will not be able to pay his banks, his sub-Contractors, suppliers, hirers and workers on time thus causing everyone to suffer.

Payment problems are old age issues that permeate the Malaysian construction industry over the years. Every so often we hear of Contractors complaining of either not getting paid or the payments have been unduly delayed by the Employer. In fact a study which was carried out recently showed that most construction disputes which have been brought to court were mainly concerning payments – either late payment or non-payment by the Employers to the Contractors.⁷

Consequently, there have been cases of Contractors taking their own course of actions when they are not paid or when the payments are unduly delayed. These include

⁴ A report of A Questionnaire Survey on Late and Non Payment Issues in the Malaysian Construction Industry

⁵ Ameer Ali (2005) A “Construction Industry Payment and Adjudication Act” – Reducing Payment – Default and Increasing Dispute Resolution Efficiency

⁶ Ibid no 1

⁷ Asniah Abidin (2007) – The Profile of Construction Disputes – M.Sc Construction Contract Management Dissertation, UTM

stop working, suspending the work and slowing down their work. In the worst scenario the Contractor may simply leave the site and abandon the project. There was a case of a Contractor demolishing the work that he has completed because he didn't see his payment was coming at all. This scenario gave rise to a number of pertinent questions - can a Contractor take any of these actions when they are not paid or when payment is unduly delayed? Were they not in breach of their contract with the Employers? Is there any provision in the PWD 203A (Rev 83), PAM 98/2006 and CIDB 2000 forms contract that allow the Contractor to resort to such actions? Is there any common law provision that gave the Contractors all these options? Is there any other remedy available to the Contractor to address the problems? This paper looks into some of these questions and considers the various other actions that the Contractors can take when faced with the problems of late or non-payment by the Employers.

2. The Aim Of The Paper

This paper is based on a research for a Master Thesis entitled "*The Contractor's Right of Action for Late or Non-Payment by the Employer*". The objective of the research is to determine the various actions available to the Contractors when they are faced with the problems of late or non-payment by the Employer. The study analyses and synthesises the provisions on remedies for late or non-payment found in the three major standard forms of construction contract namely PWD 203A Standard Form of Contract (Rev 83), PAM Standard Form of Contract 1998/2006 and CIDB Standard Form of Contract 2000 which after this, will be referred to as PWD203A, PAM 1998/2006 and CIDB 2000 respectively. It also examines the remedies available under the law of contract and the common law. This paper also examines the related case laws found in the Lexis Nexis.

3. Payment In Construction

But before we go deeper into the subject of remedies for late or non-payment, it is appropriate for us to have some understanding about payments in construction environment. Literally, payment means the money given or to be given to a person/s in return for the goods sold or services rendered. In construction, payment is defined as "a

monetary consideration for the Contractor's performance⁸ or work done". In *Royden (M) Sdn Bhd v Syarikat Pembinaan Yeoh Tiong Lay Sdn Bhd*,⁹ payment was defined as "the value of any work, materials or goods comprised in the contract". In other words, payment is the consideration, in term of money, for the work that a Contractor has carried out in accordance with the contract plus the materials delivered to site. Contractually, the said money must be paid promptly and fully unless there are specific reasons for delaying or withholding it.

In construction contract, there are two types of payments - one is the **Interim Payment** and the other is the **Final Payment**¹⁰ which is disbursed upon certification by the Architect, Superintending Officer, Engineer or Contract Administrator. This paper dwells only on the remedies for late and non-payment of Interim Payment. It does not consider issues or problems associated with late or non-payment of Final Payments.

4. Interim Payment

The word "**interim**" means temporary, provisional or short term. For that, it can be said that "Interim Payments" are provisional or short-term payments made progressively to a Contractor at weekly, bi-weekly or monthly intervals based on periodical estimated value of work that the Contractor has carried out. Interim payment is also known as progress payment or stage payment¹¹.

Osborn's Concise Law Dictionary defined Interim payment as:

*"A payment on account of any damages, debt or other sum (excluding cost) which the Employer may be held liable to pay to or for the benefit of the Contractor. It required financing the Contractor's operations because most construction work involves considerable sums of money and spanning a considerable length of time."*¹²

It is the payment arrangement found in almost all the contracts for large construction projects with construction time more than one year. The old JCT 69, stated that:

⁸ Ibid no 1

⁹ [1992]1 MLJ 33

¹⁰ Jamaluddin Yaakob (2007), Lecture note on Certificate and Payment

¹¹ Clause 30.3 PAM Form of Contract 1998

¹² A Guide on The Administration of Public Works Contracts (1988), Jabatan Kerja Raya Malaysia

“The obligation of the Employer to pay for the work does not arise in the case of entire contracts until the whole of the work is entirely performed, subject to mitigating effect of doctrine of substantial performance, whereas in the rare instances of contracts of general employment payment becomes due pari passu with the execution of the work. An obligation to pay by installments or on account at specified stages or intervals will usually only arise from the express terms of the contract, but such arrangements are common in the building contract”.

The major standard forms of construction contracts used in Malaysia namely the PWD 203A (2007), PAM (1998/2006) and CIDB (2000), contain provisions for payments to be made against Interim Certificates issued periodically¹³ by the Architects, Superintending Officer (S.O.) or Client’s Representative or Contract Administrator as the case may be. The provisions give the Contractor the right to be paid upon the issuance of the interim certificate and compel the Employer to pay the Contractor the certified amount¹⁴. In other words, the employer must pay the contractor at the right time in the right amount.

The purpose of interim payment is to ensure that the Contractor is regularly paid throughout the progress of the works. It is to maintain the Contractor’s cash-flow and thus minimizing any deficit which may affect the smooth running of the project. It is an important aspect of construction because the whole process involves many different participants i.e. the suppliers, sub-contractors, workers etc. and large sums of money have been paid in advanced to them.¹⁵ “Cash flow” has been considered as “the very life-blood of the enterprise”.¹⁶ In *J.M.Hill & Sons Ltd v. London Borough of Camden*,¹⁷ the judge held that:

“The very essence of the provisions of contract about payment on the Architect’s certificate was to maintain the Contractor’s cashflow”

The interim certificate is considered as virtually cash. Therefore it must be

¹³ Payment term in standard form of contract “Parties to construction contract often agree to arrange payment on a periodic basis although in general there is no common law right to payment by instalment

¹⁴ Harban Singh (2003), *Engineering and Construction Contract Management – Post Commencement Practice*. Singapore: Lexis Nexis

¹⁵ The Aqua Group, *Contract Administration for the Building Team*, 7th ed., Oxford: BSP Professional Books, p. 65

¹⁶ Lord Denning MR in *Gilbert-Ash (Northern) Ltd v Modern Engineering (Bristol) Ltd*, (1973) 71 LGR 162, 167.

¹⁷ (1980) BLR 31 (CA)

honoured by the Employer and thus ensuring that the Contractor will have adequate funds to successfully construct and complete the project on time. As pointed out by the judge in the case of *Dawnays Ltd v F G Winter*¹⁸

“Interim certificate was taken to be almost equivalent to cash like a bill of exchange and must be honoured”.

As pointed out earlier, the Contractor is entitled to receive payment upon certification by the Architect, S.O or Contract Administrator as the case may be. But when does the Contractor’s entitlement to payment arise and how much is he entitled? As stated by Lord Goddard CJ in the case of *“Dunlop & Ranken Ltd v Hendall Steel Structures Ltd*¹⁹:

“A Contractor who has all the expense of the materials and labour wants money from time to time, and it is perfectly clear that, until the Architect has given a certificate, the Contractor has no right to receive any sum of money from his Employer.....until the Contractor can produce to the building owner a certificate from the Architect, the Contractor cannot get anything.”

The case pointed out that the Contractor’s right to receive payment only arise when he had received the interim certificate and able to produce it to the Employer. But when should the interim certificates be issued by the Contract Administrator and when is the Contractor entitled to receive the certified amount? Table 1.0 below shows the certification intervals, the time frame for issuance of the Interim Certificates and also the time frame for the Employer to honour the certificates as provided for by the various contracts.

¹⁸ (1971) 1 WLR 1205

¹⁹ [1957] 3 All ER 344

Table 1.0 – The Period of Interim Payment and Time for Honouring the Certificate

	PWD203A	PAM 1998	CIDB2000
<i>Period of Interim Certificate</i>	One month [Clause 47(a)]	One Month [Clause 30.2)	One Month [Clause 42.9(a)]
<i>Issue of Interim Certificate after Site Valuation</i>	14 days after site valuation [Clause 47 (b)]	Upon the receipt of Contractors details and particulars [Clause 30.2]	21 days after receiving Statement of Work Done [Clause 42.9(b)]
<i>Period of honouring the Certificate</i>	30 days from the date of the issuance of the Interim Certificate [Clause 47(d)	14 days from the date of the issuance of Interim Certificate [Clause 30.2]	21 days from the date of the issuance of Interim Certificate [Clause 42.9]
<i>Issuing Person</i>	Superintending Officer (S.O)	Architect	Client's Representative
<i>Amount to be Paid</i>	Value of Work Done + 90% Material On Site	Value of Work Done + 90% Material On Site	

The table establishes that a Contractor is entitled to be paid at least once a month. It is also the time when the Architect or the S.O is obliged to issue the Contractor with the Interim Certificate. The Employer in return must honour the certificate by paying the Contractor within the time stated in the contract which is 14 days under PAM 98, 30 days under PWD 203A and 21 days under CIDB 2000 respectively.

5. Late And Non-Payment

But what happen if the Employer failed to pay the Contractor within the stipulated time, and continue not doing so 2 or 3 weeks or 3 months after the latter was issued the

Interim Certificate? Can it be considered as late payment or in the latter case as non payment? Can we assume it to be the case of late payment or non-payment if the Architect or S.O issue the Interim Certificate much later than the time frame stipulated by the Contract?

Ameer (2005) defined late payment as the failure by the Employer to pay the Contractor within the time stated in the Contract. He also defined that non-payment occurs when the Contractor is not being paid at all for his work. In the practical world, the issue of late or non-payment is not as straight forward defined by Ameer. In the PWD203A Form of Contract (2007), it is stipulated that the period for honouring the certificate is **30 days** from the date of the issuance of the certificate. Clause 30.1 of the PAM Form of Contract (2006) stated that the period of honouring certificate is within **21 days** after the issuance of the certificate. Any payment made later than the stipulated time frame can be considered as late or delayed payment.

However, such a delay cannot be construed to mean that the Employer has delayed or failed to pay the Contractor. Based on Clause 30.7 and Period of Delay stated in the Appendix, it can be deduced that an Employer will only be considered to have neglected or failed to pay the Contractor if the latter does not receive his payment for a period of 2 – 3 months after the period of honouring certificate. There has also been a suggestion that non-payment of contractor occurs when he is not paid three months after the end of the period of honoring certificate. In the opinion of the construction professionals, the Employer is considered to have delayed or failed to pay the Contractor when the latter does not receive his payment after 3 to 5 consecutive periods of interim certificate (3-5 months).

What are the remedies available to the Contractor if he finds that his Employer has delayed or failed to pay him 3-5 months after the period of honouring certificate? In other words, what kind of actions can the Contractor take if he is paid very late or not paid at all by the Employer?

6. Actions That The Contractor Can Take In The Event Of Late Or Non-Payment By The Employer

After reviewing the various standard forms of contract (PWD 203A (Rev 83), PAM 1998 and CIDB 2000 form contract), law cases, journals, books and the related

monographs, it appears that the Contractor may have several options if the Employer has neglected or failed to pay him on time or has not pay him at all. They include the following:

- (a) the suspension of work,
- (b) slowing down the work,
- (c) claiming for interest,
- (d) apply for summary judgement,
- (e) apply for the winding up of Employer's company or
- (f) determining the contract with the Employer.

a) Suspension Of Works

It is universally known that there is no right of suspension of work due to non payment under the common law. The general principle is that the Contractor has no legal right to suspend work, and on the part of the Employer, he has also no legal right to order any suspension of work. Once the construction work started, the Contractor is contractually obligated to carry out the work "*regularly and diligently*" until the project is completed.

Suspension is a temporary halting by one party of the performance of their obligations under the contract on the grounds that the other party is in breach contract for failing to make payment in accordance with the terms agreed between them. Suspension is temporary in nature because where there is a right to suspend, the procedure does not bring the contract to an end; but putting on hold the obligation of the suspending party until the breach has been properly remedied.

According to Murdoch and Hughes (1996), "*it is not uncommon to find that a Contractor or Sub-Contractor, who has not been paid what is due, threatens to suspend the work under the contract until payment is made*". It must be noted that without a clear contractual right to suspend the works, the Contractor is not entitled to do so even though the Employer has failed to pay him within the time stipulated in the contract. In this respect, if the Contractor suspends the works the court may find him guilty of repudiating the contract.

i) Provisions Contain in the Forms of Construction Contract

Theoretically, a Contractor is only entitled to suspend the works on site

following any late or non payment if such a term is expressly stated in the contract. But what do the various construction contract forms say about this matter? Let us look into the different standard forms of building contract and learn what each of them says about the issue.

PAM Form of Contract 1998

There is no express provision that permits the Contractor to suspend his work when he is not paid or his payment was not forthcoming in due time after receiving the Interim Certificate. Clause 25(1) (ii) and Clause 23.4 state that the Contractor is to proceed regularly and diligently and he is to use his best endeavours to prevent delay. The clauses clearly demand the Contractor to show a good performance and continue with the work to prevent disruption to the progress of the project.

But the new PAM 2006 contains provision that give the Contractor to suspend the progress of work if the Contractor is faced with problem of delayed or non payment by the Employer. It is clearly stated in clause 30.7. But it requires the Contractor to give a written a notice to Employer with reason to suspend the works until the Employer has paid the amount due to the Contractor.

PWD 203A Standard Form of Contract (Ed.1983)

This form of contract contain no expressed provision that allows the Contractor to suspend the works if his payment was unduly delayed or he is not getting his payment at all.

CIDB 2000 Standard Form of Contract

Clause 42.10 of the CIDB 2000 allows the Contractor to suspend wholly or partly or to reduce the rate of the works until the Employer makes full payment plus the interest due. The Contractor is also entitled to any extension of time or loss and expense arising from such suspension.

ii) Analysis of Case Laws

It appears that CIDB 2000 and PAM Form of Contract 2006 contain the provision which allow the Contractor to suspend the work in the event of non-payment by the Employer. Now let us look into the many case laws and minutely consider the judgment that has been made in connection with the

issue of late or non-payment.

In *Kah Seng Construction Sdn.Bhd. v Selsin Development Sdn.Bhd.*²⁰ it was stated that a Contractor's response to actual or alleged breaches of contract by the owners by suspending or deliberately going slow are extremely perilous. In this case, the plaintiff contended that it was entitled to suspend works because of non payment of one certificate and partial non payment of another. The defendant argued that even if the Defendant was not entitled to set off sums of monies for delay and defective works against sums due to the Plaintiff in the interim certificates, there was no provision in the rudimentary contract between the parties for non payment of certified sums and that the Plaintiff's admitted suspension was wrongful. The judge held that:

'There is no intermediate right in a building contract to suspend works. If the Contractor insists on the continued performance of the contract, i.e. he affirms the contract, he must himself continue to perform his primary obligations under the contract i.e. continue performing the contract works. That is why suspension of the works by the contract, i.e. not continuing with his primary obligations, becomes itself a repudiatory breach by the Contractor'

In *Ban Hong Joo Mines Ltd v Yap Ltd*,²¹ there is no intermediate right in a building contract to suspend works even if the plaintiff can establish that the Defendant is in repudiatory breach of contract. The Plaintiff would have no right to suspend work, but instead would have had to elect to either terminate the contract or insist on due performance. By suspending works without valid legal cause, the Plaintiff has in fact repudiated its contractual obligations.

In case of *Jia Min Building Construction Pte Ltd v Ann Lee Pte Ltd*,²² the High Court held that a Contractor had no general right at common law to suspend work unless this was expressly agreed upon. An absolute refusal to carry out the work or an abandonment of the work before it was substantially completed, without lawful excuse, was a repudiation which would entitle the other party to terminate the contract. The court simply stated its view that it

²⁰ [1997]1 CLJ Supp 448

²¹ (1969) MLJ 83

²² [2004] 3 SLR 288

was “...Quite satisfied that there was no legal basis on which the suspension of work could be”. Its mean this case was affirmed the position of Contractor’s right of suspension.

In case *Canterbury Pipe Lines v Christchurch Drainage*,²³ A decision of the New Zealand Court of Appeal which held that a Contractor has no implied right of temporary suspension following non payment on the part of the Employer.

In *Mersey Steel & Iron Co. v Naylor Benzon & Co.* ²⁴, decision goes far to explain the apparent absence in English building contract law of any recognition of a common law right to suspend work for wrongful withholding of a progress certificate or payment, as distinct from a right to rescind for a breach going to the root of the contract.

Apart from suing for interim payments or requiring arbitration where that is provided for, the remedy and apparently the only remedy which the Contractor is recognized as having at common law is rescission of a sufficiently serious breach has occurred. If he chooses not to rescind, his own obligations continue. He is bound to go on with the work.

It can be deduced from these cases that a Contractor has no implied right to temporarily suspend the works in case of late or non payment from the Employer. In most cases, the judge held that the suspension of work by the Contractor will constitute a repudiatory breach of contract unless there is an expressed provision in the contract that allows the contractor to do so.

iii) Provisions under the Common Law

Now let us look at what the Common Law has provided with regard to the issue of late and non-payment. Under the general principle of the Common law the Contractor has no legal right to suspend work, and the Employer has no legal right to order its suspension. Once the contract work has commenced, it is the Contractor’s obligation to carry out the work in a regular and diligently until it is completed. As a result, unjustified suspension by either party will amount to a breach of contract for which damages may be claimed. The right

²³ [1986] 33 BLR 76

²⁴ (1884) 9 App.Cas.434

to suspend work is not conferred in common law.

There is no general common law right of suspension of work for late or non payment.²⁵ But, a Contractor has a right in common law to suspend work so long as the damage is not sufficiently serious to become a fundamental breach. In the United Kingdom, Section 112 of the Housing Grant Construction Regeneration Act (HGCRA) provides that when the sum is not paid on the final day of payment and no withholding notice has been issued by the Employer, then the Contractor is entitled to suspend his performance until the full payment is paid.

But, mere/simple breach of a payment obligation does not constitute common law repudiation and it is not the ground to suspend work. The principle is to consider whether the non payment show an intention not to be bound. A clear indication of refusal or inability to pay future installments will be repudiation as well as a repeated failure to pay on time in response to warnings. The remedy for non payment if it constitutes repudiation is to terminate the contract pursuant to express termination provisions in the contract or rescission at common law for a breach going to the root of the contract or suing for interim payment or requiring arbitration where that is provided. If the Contractor chooses not to rescind or terminate the contract, his own obligation continues and he is bound to go on with the work.

If the Employer continuously refuses to make payment when payment is due, then it may show the defaulting party's intention so as not to be bound by the contract. As such, the Contractor may exercise a common law right (unless the contract has already express provided therefore) to treat the contract as repudiated.

As a summary, where a sum due under a construction contract is not paid in full by the final date for payment and no effective notice to withhold performance for payment has been given, then the person to whom the sum is due has the right to suspend the performance of his obligations under the contract.²⁶ Another

²⁵ Kah Seng Construction Sdn.Bhd.v Selsin Development Sdn.Bhd.[1997]1 CLJ Supp 448

²⁶ Part II- Construction Contract, Section 112(1) Housing Grants, Construction and Regeneration Act 1996

important point to be noted is that a Contractor could only suspend the work for non-payment when the contract contains a written clause which gave the right to the Contractor to do so.

The study shows that not all the local forms of construction contract contain such a provision. At the same time, the study also shows that a Contractor may also find himself in breach of contract if he failed to observe the correct procedures as may be stipulated in the contract, when attempting suspension.

b) Slowing Down THE Work

i) Provisions in the Standard Forms of Contract

A study of the various standard form of contract in Malaysia i.e. PAM 98/2006 standard form, PWD 203A standard form and CIDB 2000 standard form shows that there is no express provision that give the Contractor the right to slow do0wn the progress of the work on reason of late or non payment by the Employer. Therefore, in whatever the circumstances, the Contractor should not slow down his work because he is not being paid or payment was unduly delayed by the Employer, unless there is a written provision in the contract that allows him to do so.

ii) Analysis of Case Laws

Although a particular contract may give the parties certain rights, there is no general right for a party to go slow even if payment is wrongly withheld. The case of *Supermal v. Federated Homes*,²⁷ is in line with this principle except that there is a breach of condition or a fundamental breach of contract per se which does not absolve the other party from performing the rest of his obligation under the contract.

According to Lim (2005), the right to slow down the execution of the work is not recognized under the common law (refer to the case of *Supermal Ltd v. Federated Homes Ltd*²⁸) apart from the right to suspend the work. Currently, such right is excluded by all the Construction Contract Act around the globe. It is a sensible approach to include that provision in the Malaysian

²⁷ (1981) Con.L.R. 25

²⁸ Ibid no 83

Construction Contract Act as sometimes it is not worthwhile for the Contractor to suspend the work altogether because there is a situation whereby the machinery and equipments left idling on site and the fact that the Contractor is obliged to pay for the hiring cost.

iii) The Provisions under Common Law

The common law gives no permission to the Contractor to slow down the progress of the work when the Employer delays or fails to pay the Contractor.²⁹

c) Claim for Interest

The question of whether a Contractor is entitled to damages or interest due to late or non-payment by the Employer is still unclear. Let us look into the various standard forms of construction contract, law cases and the provisions under the common law and determine whether a Contractor has the right to claim for interest if the Employer unduly delayed the interim payment to the Contractor.

i) The Provisions in the Standard Form of Contract

PWD 203A Standard Form of Contract

There are no express provision in this form of construction contract which entitled the Contractor to claim for interest for late or non payment by the Employer.

PAM 98/ 2006 Standard Form of Contract

There is also no express provision in this form of contract that give the Contractor the right to claim for interest for late or non payment of interim certificates by the Employer. However, clauses 34.4(vi) and (vii) provide that the arbitrator is given expressed powers to award pre-award interest (that is, interest on amounts awarded from the date of the award) and post-award interest at whatever rates which the Arbitrator considers just.

Under the new PAM Form of Contract 2006, the Contractor is given the right to claim for interest in case of late or non payment by the Employer. This is clearly stipulated in clause 30.17.

²⁹ Mr. Steve Chan (2006), Another 50 Contractual Problems Relevant to Malaysia and Their Solutions, Kuala Lumpur

CIDB 2000 Standard Form of Contract

Under this standard form of contract, the Employer has the right to pay the Contractor a sum in addition to the certified amount which can be considered as an interest to late payment. Clause 42.9(b) of CIDB Form of Contract 2000 provides for a payment of simple interest to the Contractor at the rate stated in the Appendix in respect of any sum unpaid from the date due until the date of actual payment. This provision can be used in the event of the failure of the Employer's to make the whole or part payment within the Period of Honouring Certificate. At the same time, Clause 42.12 requires the Employer to pay damages, whether by way of interest or otherwise, in the event of any delay or failure by the Superintending Officer to certify payments due to the Contractor.

It can be seen that, under the CIDB Form of Contract 2000, the Contractor not only entitled to claim for interest for late or non-payment by the Employer but also for failure of the Contract Administrator to issue payment certificates.

ii) Analysis of Case Laws

Now let us see the various law cases on the issue of interest for late or non-payment by an Employer to the Contractor. In *Lojan Properties Pte Ltd v Tropicon Contractors Pte Ltd*,³⁰ the contract between the parties is based on the Revised Standard Form of the Singapore Institute of Architects (SIA). The judge held that when the Contractor faced with late or non-payment of interim payment, the he may claim for interest. In case of *Newacres Sdn.Bhd. v. Sri Alam Sdn.Bhd.*,³¹ the judge held that:

"It is only fair that interest be awarded against the person who wrongfully deprives another from the use of the latter's money". Mere replacement of the money after more than a decade is insufficient compensation. As such, the landowner should be compensated by an award of interest for the loss thereby occasioned to them.

In the case of *Wallersteiner v Moir*,³² it was held that whenever money is misused by an executor or a trustee or anyone else in a fiduciary position i.e.

³⁰ [1991] 2 MLJ 70

³¹ [2000] 2 MLJ 353

³² [1975]1 All ER 849 CA at p855

who has misapplied the money and made use of itself for his own benefit, there must be an equity awards or interest. The court presumes that:

“ the party against whom relief is sought has made that amount of profit which persons ordinarily do make in trade, and in those cases the court directs rests to be made i.e. compound interest”.

In the case of *Lian Hup Manufacturing Co Sdn.Bhd v Unitata Bhd*,³³ the contracting parties had agreed to include in the arbitration clause of their contract that, the construction, validity and performance of the clause were to be governed by Malaysian law. Under s11 of the Civil Law Act 1956, the court has the discretionary power to award interest for the recovery of any debt or damages. As such, the court held that the arbitrator had the same power as that of the court to award interest at such rate as he thinks fit.

In the case of *FG Minter Ltd v Welsh Health Technical Services Organization*, a claim for interest due to late payment was upheld by the Court of Appeal. The reason for this is that the claim for interest for late payment is considered as direct loss and/or expense equivalent to a claim for damages as decided by the case in *Hadley v Baxendale*³⁴ which has been codified under section 74 of the Contract Act 1950.

However, the test in *Hadley v Baxendale* as to whether damages in the forms of interest can be paid for, depends on the question of whether the likelihood of the occurrence of damages was anticipated by both parties at the time when the contract was made. It is regarding the knowledge of the parties at that time when the contract was made.

In such a case, if the Employer was aware that the Contractor is forced to borrow the capital, the Contractor may be able to claim interest or financing charges for late or unpaid payment. Therefore, a clear wording in the contract is required to provide contractual mechanism for the Contractor to claim for interest or financing charges.

But, in case of *Woon Hoe Kan & Son Sdn.Bhd. v. Bandar Raya*

³³ [1994] 2 MLJ 51

³⁴ (1854) 9 Ex 341

Development Sdn.Bhd.,³⁵ no evidence of agreed rate- interest payable nevertheless. The Architect would not normally be authorized to add interest into certificates unless specifically provided. In this case, Contractor cannot claim of interest on reason of late or non payment.

iii) The Provisions under the Common law

There is a case where a claim for interests due to delay in honouring certificate can be founded in common law and in this case the rule in *Hadley v. Baxendale* ³⁶ has been applied. In summary, the injured party should be entitled to damages (i) either arising naturally (according to normal course of things) from the breach or (ii) such as may be reasonably be in the contemplation of the parties at the time contract was made as the probable consequent of the breach. In section 74 illustrations (n) of the Contract Act 1950, the unpaid Contractor may commence an action against the Government to recover of payment together with the Interest.

d) Application for Summary Judgment

Summary Judgment is defined in the Dictionary of Law as: “*Procedure where the court decides a claim or particular issue against claimant or defendant without trial*”³⁷. It means that a plaintiff may at an early stage of proceedings try to obtain judgment on his claim or part of his claim without going to trial. It will save time and cost for trial and hearing process.³⁸ The procedures of application for summary judgment is mandatory and the party who apply must strictly complied with the procedure governed stated in Order 14 of HCR, Order 26A of SCR or other alternatives such as Order 81, Order 73 and Order 18.

i) The Provisions in the Standard Form of Contract

None of the local standard form of construction contract provides the application for summary judgment as one of the remedies available for the Contractor in the case of late or non-payment by the Employer. There is some misunderstanding among contractors, contract administrators and employers

³⁵ [1973] MLJ 60

³⁶ (1854)9 Ex 341

³⁷ L.B Curzon (2004). *Dictionary of Law. 2nd Edition*. International Law Book Services.

³⁸ Nasser Hamid, S. S. Ravichandran (1993). *Summary Judgment*. Central Law Book Corporation

on this matter. They are of the opinion that the present of an Arbitration clause in the condition of construction contract bars the Contractor from applying to the court for Summary Judgment. We have to remember that the arbitration clause is meant for settlement of disputes in connection with the project. In most the late and non-payment cases, Contractors were not disputing the amount certified by the Contract Administrator. They were only claiming their rights to be paid promptly and fully except when there are specific reasons (as allowed by the contract) for delaying or withholding it.

ii) Analysis of Case Laws

In *Sri Hartamas Development Sdn Bhd v MBF Finance Bhd*,³⁹ the Supreme Court held that summary judgment via litigation may be obtained for unpaid certified payment claims.

The famous case involving an application for summary judgment under the building contract was the case of *Pembinaan Leow Tuck Chui & Sons Sdn Bhd v Dr Leela's Medical Centre Sdn Bhd*.⁴⁰ In this case, the appellant (Contractor) sued the respondent (Employer) and sought summary judgement under Order 14 of the Rules of the High Court (RHC) alleging that the Employer was under an obligation to promptly pay the Contractor the sum written in the certificate issued by the architect. It is a question of whether under the building contract, the Employer is obliged to pay the contractor promptly upon being served the interim certificate. In this case, the court held allowing the appeal the Contractor.

iii) Provisions under Common Law

Under the common law, the Contractor may apply to the court for a summary judgement under Order 14 of the Rules of the High Court 1980 on the ground that the Employer has no defence to the claim except as to the amount of damages claimed. If a claim for payment can be brought within the scope of Order 14, considerable advantages accrue in terms of both speed and

³⁹ [1992] 1 MLJ 313

⁴⁰ [1974] 2 MLJ 94

cost.

The most frequent approach taken by the Employer in resisting an Order 14 application is to apply to the court. The court action will more often than not attract an application for a stay of the court proceedings pending arbitration pursuant to Section 6 of the Arbitration Act 1952. The Contractor has then to weigh his chances of obtaining summary judgment quickly against the possibility of the application for a stay of proceedings dragging its way through the courts before final decision, which may be in the Employer's favour thereby causing the Contractor further expense and delay.

e) Winding Up Petition

The primary function of insolvency procedure is to maximize the returns to the existing claimants: that is to implement the most efficient plan for the company. On one hand this could be end up selling the company for cash – either as piecemeal or as a going concern. On the other hand the company could be reorganized, with a new financial structure (creditors agree to forgive some of the debt, perhaps in exchange for cash and or equity) and possibly with new management.

The secondary function is the preservation of priority. This is also a criterion for a good insolvency procedure. The question arise on present insolvency procedure is whether it can guarantee the preservation of priority.

i) Provision in the Standard Form of Contract

The law in Malaysia distinguishes the treatment of insolvency between natural and legal persons, contained in respective bankruptcy and corporate legislation. With regard to corporate insolvency, the Companies Act 1965, outline two basic types of insolvency measures that, are familiar to readers in the common law world. In the first case, creditors are to appoint a receiver and manager in respect of the debtor company (Part VIII, Companies Act 1965)

Furthermore, an application may be made to court for the commencement of winding up proceedings, which may be further subdivided into three types: member's voluntary winding up, creditors voluntary winding up and winding up by court (Part X, Companies Act 1965). Apart from the two insolvency-related measures, general company law offers to a company the possibility of

entering into a scheme of arrangement for the reconstruction of its finances (Part VII, Companies Act 1965). Scheme of arrangement is a procedure principally applicable to companies in a situation of imminent or technical insolvency and whose primary purpose is to avoid the inevitable consequences of winding up, which are the liquidation of assets, destruction of viability and consequent loss of employment.

It is possible for the Contractor to force the pace by making a demand for its claim by filing a winding up petition under the Companies Act 1965. Section 217(1) (b) allows any creditor of the company to file a winding up petition. The grounds and circumstances in which a company can be wound up are laid down in section 218(1). In the case of unpaid interim certificates, the Contractor may file petition on the ground that the Employer's company is unable to pay its debt (section 218(1) (e)) or it is just and equitable that the Employer's company be wound up (section 218). Section 218(1) (e) mentioned:-

“The Court may order the winding up if the company is unable to pay its debt”.

From this clause clearly show, the Contractor may request from the court to wind up the Employer's company in case Employer failure to pay the Contractor amount due.

ii) Analysis of Case Laws

In case of *Kemayan Construction Sdn.Bhd. v Prestara Sdn.Bhd.*⁴¹ the Employer withheld a certified interim payment that is due to the Contractor on the ground that the Contractor failed to complete the works and rectify the defects as per the Architect's list of defects. The Contractor filed a petition as well as the statutory notice of demand pursuant to section 218 of the Companies Act 1965.

In dismissing the petition, the judge held that the Contractor had an obligation to comply with the architect's instructions and rectify the defects. The failure by the Contractor to comply with the architect's instruction to

⁴¹ [1997] 5 MLJ 608

rectify the defects gave the Employer a right to set off under clauses 2(1) and 22 of the contract and it followed that the debt was in dispute.

The Employer was thus justified in refusing to pay the petitioner Contractor. On whether it was just and equitable to wind-up the Employer's company, the judge held that the court would only exercise its discretion if it can be reasonably ascertained that the existing and probable assets of the Employer's company will be insufficient to meet the existing liabilities. The judge held that on the facts of the case, the Contractor failed to satisfy as the Contractor will have to establish the true financial positions of the Employer's company.

In *BMC Construction Sdn Bhd v Dataran Rentas Sdn Bhd*,⁴² the respondent (the Employer) was unable to pay its debts. The respondent was alleged to be indebted to the petitioner (the Contractor) in the sum of RM173, 096.18 in respect of four (4) unpaid progress payment certificates for building works executed by the petitioner and demanded in the notice pursuant to s 218 of the Companies Act 1965.

In opposing the petition, the respondent alleged that it had a cross-claim or set-off against the petitioner for loss and damage for defective works. The respondent also produced letters from its bankers stating the outstanding amounts on its banking facilities and receipt of payment from one of the respondent's creditors dated in 1997 to evince that it was solvent and had the means to settle the claim of the petitioner. The judge made a decision by ordering the respondent be wound up.

In the practical world, this requirement will be very difficult to satisfy as the Contractor will have to establish the true financial positions of the Employer's company before the Contractor taking this action.

f) Termination of Contract

For most construction contract, payment within the contractually agreed framework is not specified to be "of the essence" and therefore a failure to make

⁴² [2001] 1 MLJ 356 Company Winding-Up No 28-87 Of 1998

payment would not be a breach that went to the root of the contract.⁴³ Under the law of contract, failure to pay on time what is due will not be treated as a sufficient breach to justify the other party in terminating the contract.⁴⁴ Failure to pay on time what is owed on another contract will not be a repudiatory breach.⁴⁵ However, while late payment is not in itself repudiatory, a continued refusal to pay may become so.

a) Provisions in the Standard Forms of Contract

PAM 98/PAM 2006 Standard Form of Contract

PAM 98 provides for an abandonment of the contract by the Contractor as a ground for termination by the Employer. Termination under the PAM standard form of contract by the Contractor is provided for by clauses 26(1) (a) to (c).

The Employer's default as listed in Clause 26 entitled the Contractor to terminate his own employment under the contract. These defaults include the Employer's failure to pay the Contractor the amount due in the interim certificate within the period of honouring the certificate. It is noted that such notice is drafted into the contract to afford an opportunity to the Employer to remedy his default within that 7 days period. Failure by the Employer to pay within the stipulated time would entitle the Contractor to terminate his employment under the contract.

PWD 203A Standard Form of Contract

The PWD203A form of contract does not contain any express provision which allow the Contractor to terminate his employment due to late or non-payment by the Employer. When the Contractor faced with the problem of late or non-payment by the Employer, he may refer his case under common law or any statutes.

CIDB 2000 Standard Form of Contract

The CIDB 2000 standard form of contract contains a provision that allow the Contractor to determine the contract if there is a default by the Employer. It is stated in Clause 45.1- Determination by Contractor with Notice.

⁴³ Decro –Wall International v Practitioners in Marketing [1971] 2 All ER 216

⁴⁴ Mersey Steel & Iron Co v Naylor, Benzon & Co (1884) 9 App.Cas.434

⁴⁵ Small & Sons Ltd v Middlesex Real Estates Ltd [1921] W.N.245

b) Analysis of Case Law

In the case of *Ban Hong Joo Mines v. Chen & Yap Ltd*,⁴⁶ the court find out that the Employer intentionally refused to pay the interim payment to the Contractor without reasonable cause. The Employer deliberate and unjustifiable refusal to make the payments already due together with his unjustified order to the Contractor to stop work was held to be a repudiatory breach.

However, one has to be wary that not all refusals to pay amount to a repudiation of the contract. One has to look at the circumstances of the case at hand first. The judge held that the Contractor can claim for damages for late in payment by Employer but the Contractor cannot terminate the contract. In the case of *Yong Mok Hin v United Malay States Sugar Industries Ltd*⁴⁷ the judge held that, delaying the payment did not really show that the Employer rejected the contract. The Contractor cannot terminate the contract just because the client delays in making payment. The judge held that, the Contractor may only claim for damages. But the Contractor's right to determine his employment under the contract remains enforceable under the common law and the Contract Act 1950.

c) The Provisions under the Common Law

There are also provisions under the common law allowing the Contractor to terminate the contract if the Employer fails to pay the former upon presentation of the interim certificate within the time laid out. The Contractor is entitled to terminate a contract if the Employer does not pay the Contractor what is due to him. Non payment is an obvious ground for termination in the absence of any reasonable defence to which the Employer can argue. An Employer who does not pay his Contractor upon presentation of the interim certificate shows that the Employer does not want to be bound by the terms of the contract regardless of how well the Contractor has performed his part of the contract.

In section 40 the Contract Act 1950 – “Effect of refusal of a party to

⁴⁶ (1969) 2 MLJ 83

⁴⁷ [1967] 2 MLJ 9

perform the promise wholly” it is stated that:-

“when a party to a contract has refused to perform, or disabled, himself from performing, his promise in its entirety, the promisee may put an end to the contract, unless he has signed, by words or conduct, his acquiescence in its continuance”.

Termination at common law can only take place where one party commits a breach of contract, and that breach amounts to a repudiatory breach. A party is said to have repudiated a contract if he expressed by his words or conduct that he does not intend to be bound by the contract or to perform his obligations. Normally, refusal by the Employer to pay sums due is clearly a default⁴⁸ and Contractor can take action based on such reason. But, failure to pay one installment out of many is not ordinarily sufficient to amount repudiation.⁴⁹

In the case of *Lep Air Services Ltd v. Rolloswin Ltd*,⁵⁰ it had been held that when out of 24,000 sterling pounds due, only 10,000 sterling pounds had been paid, there was repudiation. This case clearly shows that when the Employer only paid 10,000 sterling pounds out of the 24,000 sterling pounds to the Contractor, it was considered breach of contract because the amount not paid was considered very large and can be construed that the Employer does not intend to be bound by the contract or to perform his obligations.

In case of *Lubenham v South Pembrokeshire District Council & Anor*,⁵¹ it was stated that ‘the Contractor shall be entitled to payment of the sum stated in the Interim Certificate to be due to the Contractor from the Employer’. The Employer has to act on the copy sent to him by the Architect and make payment promptly on or before the due date. Failure to pay by the Employer is a breach of contract.

A contract can be voidable if one of the parties failed to perform his obligation within the specified time, especially if they have agreed that time is an essence to the performance of the contract. Section 56 Contract Act 1950-

⁴⁸ *Moschi v Lep Air Services* [1972]2All ER 393

⁴⁹ *Mersey Steel & Iron Co Ltd v. Naylor* (1884) 9 App Cas 434 (H.L.)

⁵⁰ [1973] A.C. 331

⁵¹ (1986) 33 BLR 39

“Effect of failure to perform at fixed time, in contract in which time is essential” explained that:-

“(1) When a party to a contract promises to do a certain thing at or before specified time, or certain things at or before specified times, and fails to do any such thing at or before the specified time, the contract, or so much of it as has not been performed, becomes voidable at the option of the promisee, if the parties agreed that time should be of the essence of the contract”.

In general, failure to pay on time what is due under a contract will not normally be treated as a sufficient breach to justify the other party in terminating that contract.⁵² Failure to pay on time what is owed is even less likely to be a repudiatory breach.⁵³ But based on Section 56 of the Contract Act 1950, if time is essential to the performance of the contract, the contract maybe voidable. In case of *Dawnays v Minter*⁵⁴ the judge held, the Employer must pay the Contractor the amount due on an interim certificate without any set-off saves for liquidated or established claims.

7. Conclusion

To conclude this paper, it is rightly to present a table of actions that a Contractor can take in the event of late or non-payment by the Employer as provided for in the various forms of construction contract and common law. See Table 2.0 below

<i>LIST OF ACTIONS</i>	<i>PAM 1998</i>	<i>PAM 2006</i>	<i>PWD 203A</i>	<i>CIDB 2000</i>	<i>COMMON LAW</i>
Suspension Of Work	×	√	×	√	×
Contractor Go Slow	×	×	×	×	×
Claim for Interest	×	√	×	√	√

⁵² *Mersey Steel & Iron Co v Naylor, Benzon & Co* (1884) 9 App Cas 434

⁵³ *Small & Sons Ltd v Middlesex Real Estate Ltd* [1921] WN 245

⁵⁴ (1971) 1 WLR 1205

Summary Judgement	×	×	×	×	√
Winding up company	×	×	×	×	√
Determine the contract	√	√	×	√	√

Table 2.0: Summary on Actions that can be taken for Late or Non Payment

(√ - Action Could Be Taken × - Action Could Not Be Taken)

The study shows that there is no provision in JKR2007 or PAM 1998 that allow the Contractor to **suspend** the work in the event of late or non payment by the Employer. Suspension of work is also not allowed under the common law. However, the Contractor may suspend the work if the contract is based on PAM 2006 and CIDB 2000.

Cases such as *Kah Seng Construction Sdn.Bhd. v Selsin Development Sdn.Bhd*, *Ban Hong Joo Mines Ltd v Yap Ltd*, *Jia Min Building Construction Pte Ltd v Ann Lee Pte Ltd* have all disapproved suspension of work as a remedy for late or non-payment by the Employer.

The study also suggested that, in all circumstances, the Contractor should not **slow down** the progress of the work even though the Employer has delayed in making payment. The Employer is entitled to terminate the employment of the Contractor on reason of “*the Contractor fails to proceed regularly and diligently with the work*”⁵⁵, if it is proven that he (Contractor) had slowdown the progress of work on site.

PAM 98 and PWD 2007 contain no provision that entitles the Contractor to **claim for interest** in the event of late or non-payment by the Employer. The new PAM 2006 and CIDB 2000 do allow the contractor to claim for interest for late or non-payment. Under the English law, contractual parties were only able to recover interest on late payment if their contract gave them the right to do so.

Common law principles allows the Contractor to claim for interest if there is late or non payment, as stated in Section 74 of Contract Act 1950. Refer to cases such as *Lojan Properties Pte Ltd v Tropicon Contractors Pte Ltd*, *Newacres Sdn.Bhd. v. Sri Alam*

⁵⁵ Clause 51 (a) (ii) PWD 203A

Sdn.Bhd, Woon Hoe Kan & Sons Sdn.Bhd v Bandar Raya Development Bhd.

Analysis of standard form of contract showed that the provision about **application for summary judgement** with regard to interim payment was not clearly spelt out. Under common law principles i.e. Order 14 High Court Rule, the Contractor may apply to the court for summary judgement to secure the payment of the money certified in the interim certificate. Some of the related cases are the KM *Quarry Sdn Bhd v Ho Hup Construction Co Bhd* and *Pembinaan Leow Tuck Chui & Sons Sdn Bhd v Dr Leela's Medical Centre Sdn Bhd*.

The analysis carried out, showed that the Contractor can apply the action to **wind up** the Employer's company if faced with non payment from the Employer. However, the Contractor needs to refer to the Companies Act in order to take this course of action. Some of the cases related to this line of action are *Kemayan Construction Sdn.Bhd. v Prestara Sdn.Bhd* and *BMC Construction Sdn Bhd v Dataran Rentas Sdn Bhd*.

The study shows that PAM 98, PAM 2006 and CIDB 2000 standard forms of contract contain the provisions allowing the Contractor to determine his Employment in the case of non-payment by the Employer. PWD 2007 does not contain such provision. Under the common law, termination is permissible only if the contractor can clearly shows that the Employer has refused to perform, or disabled, himself from performing, his promise in its entirety. Reference is made to the cases of *Ban Hong Joo Mines v. Chen &Yap Ltd*, and *Yong Mok Hin v United Malay States Sugar Industries Ltd*.

However, the final action to be taken by the Contractor would depend on the situation in which the late or non payment occurs. Firstly, the Contractor would need to refer to the standard form of contract used i.e. whether or not actions for late or non payment is stated. If this action is not stated in the standard form of contract, then the Contractor would need to refer to previous cases. Common law principles will only be referred to if actions for late or non payment are not stated in both the standard form of contract and previous cases.

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Appendix A

Table 3.0: Summary in Interim Payment and Certification

ELEMENT	PWD 203A	PAM 98/2006	CIDB 2000	COMMON LAW
Provision of Payment	Clause 47	Clause 30	Clause 42	Entire Contract
Schedule of Payment	Monthly Payment	Monthly Payment	Monthly Payment	Lump Sum
Time of issue Interim Certificate	Stated in the Appendix or 30 days after valuation	14 days after valuation or stated in the Appendix	21 days after receiving Statement of Work Done	Not applicable
Timing of Payment	30 days after date of Interim certificate	14 days after date of Interim certificate	21 days after date of Interim certificate	Project completed
Failure to pay amount due	Not Breach of contract	Breach of contract	Breach of contract	Not applicable