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Are "Pay When Paid" Provisions Unenforceable under the SOPA Even for Terminated Contracts?

Introduction

The Building and Construction Industry Security of Payment Act ("**SOPA**") seeks to facilitate payments for construction projects, and also sets out certain restraints on construction contracts. In *Frontbuild Engineering & Construction Pte Ltd v JHJ Construction Pte Ltd* [2021] SGHC 72, the Singapore High Court considered the issue of whether certain provisions take primacy over the other provisions in the SOPA, in particular:

- (a) Section 4(2)(c) provides that the SOPA will not apply to a terminated contract in the specified circumstances; while
- (b) Section 9 of the SOPA renders "pay when paid" provisions in a construction contract unenforceable and of no effect.

In considering the interaction between these provisions, the Court had to determine whether the SOPA goes so far as to render "pay when paid" provisions in a construction contract unenforceable notwithstanding the termination of the contract.

The Court held that section 4(2)(c) of the SOPA does not take primacy over section 9 of the SOPA. Therefore, if a contractual provision engages both section 9 and section 4(2)(c), the Court will first consider if the provision is rendered unenforceable under section 9; if the provision is not found to be unenforceable, the Court will then consider if section 4(2)(c) applies to exclude the application of the SOPA.

The contractual provision in this case purported to suspend payments upon termination of the contract until the main contract works had been completed. The Court found this to be a "pay when paid" provision which was thus unenforceable.

This Update provides a summary of the decision and highlights the key points.

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Brief Facts

The Plaintiff contractor had appointed the Defendant sub-contractor pursuant to a Sub-Contract, in which the Defendant was to perform certain sub-contract work on a project. The Sub-Contract included a Clause 9, which provided that the Plaintiff could terminate the Sub-Contract on certain grounds, upon which no further payment would be made to the Defendant until the whole of the main contract works were completed.

Following a dispute, the Plaintiff purported to terminate the Sub-Contract pursuant to Clause 9. The Defendant issued a payment claim on the Plaintiff for work done after the purported termination of the Sub-Contract. The claim was referred to adjudication, whereupon the Adjudicator issued a determination ("AD") in favour of the Defendant.

The Plaintiff sought to set aside the AD, submitting that the Adjudicator had failed to consider the applicability of section 4(2)(c) of the SOPA, and that the SOPA did not apply to the relevant Sub-Contract, having been terminated under Clause 9. The Defendant in turn submitted that Clause 9 of the Sub-Contract was a "pay when paid" provision and accordingly, was rendered unenforceable by virtue of section 9 of the SOPA.

Holding of the High Court

The Court found in favour of the Defendant and declined to set aside the AD.

Priority of SOPA provisions

The relevant provisions are set out below:

- (a) Section 4(2)(c) provides that the SOPA will not apply to any terminated contract to the extent that it contains provisions relating to termination that permit the respondent to suspend progress payments to the claimant until a date or the occurrence of an event specified in the contract (provided the date has not passed or the event has not occurred).
- (b) Section 9 of the SOPA provides that "pay when paid" provisions are unenforceable and have no effect in relation to any payment for construction work carried out or undertaken to be carried out, or for goods or services supplied or undertaken to be supplied, under the contract.

The Court held that section 4(2)(c) of the SOPA does not take primacy over section 9 of the SOPA. Therefore, when section 4(2)(c) of the SOPA is construed to determine if the SOPA applies to a particular terminated construction contract, any termination and suspension of payment provisions in

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that contract are to be given effect only if they do not fall foul of section 9 of the SOPA. The Court emphasised that, based on the definition of "contract" in the SOPA, which includes contracts that have been terminated, section 9 of the SOPA is also intended to invalidate "pay when paid" provisions in terminated construction contracts.

The Court reasoned that such an interpretation would allow a harmonious construction of section 4(2)(c) and section 9, and would also be consistent with the purpose of the SOPA, which is to ensure that sub-contractors are not left at the mercy of main contractors: (a) withholding payments for reasons unrelated to the sub-contractors' performance; and (b) making such payments contingent on performance of some other contract. The Court reiterated that section 9 is one of the provisions in the SOPA designed to ensure that the SOPA's overarching purpose, i.e., of facilitating sub-contractors' cash flow, is achieved.

Application

Following from the above, the Court held that when an adjudicator construes a termination clause in a construction contract that also contains a provision on the suspension of further payments to the counterparty following termination of that contract, the adjudicator should consider if that provision also falls within the ambit of a "pay when paid" provision under section 9 of the SOPA. If it does, the adjudicator is obliged to disregard the provision as unenforceable and of no effect.

On the facts, the Court found that Clause 9 of the Sub-Contract did, in substance, operate as a "pay when paid" provision. The Court thus disagreed with the Plaintiff's argument that the Adjudicator had failed to consider section 4(2)(c) of the SOPA, finding that the Adjudicator had in fact considered the interplay between section 4(2)(c) and section 9, and had concluded that the Defendant's payment claim fell within the ambit of the SOPA.

Concluding Words

The Court's decision clarifies the priority of the respective provisions in the SOPA. In particular, it highlights that section 9 of the SOPA, which restrains the operation of "pay when paid" provisions, cannot be easily circumvented through "clever" contract drafting. Parties to construction contracts should thus be aware of the risks of relying on such provisions.

For further queries, please feel free to approach our team below.

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