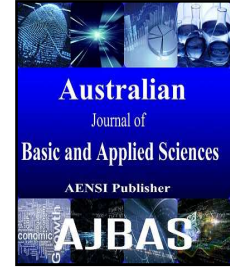




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**Is There any Accurate Solutions: Late Payment, Under Payment and Non Payment Issues in the Construction Industry**

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**ABSTRACT**

**Background:** Payment and business are interrelated. In ensuring the successfulness of business, payment schedule must be followed strictly. Dispute relating to late payment, underpayment and no-payment is sickening to the players in the industry namely the contractors, the sub-contractors and their employees. Everyone needs the reward in the pattern of payment equal to money for development of lifespan. In the industry, money is essential for the growing of the industry and the economy of the nation. Solutions need to be accurate that can be accepted by the parties in disputes. Push and pull method in chasing for payment is not going to work well. **Objective:**To evaluate and analyse the accuracy of theimplication of payment issues in the construction industry, is there solutions to the issue. **Results:** The outcome is to display that payment issues in the construction industry is significant and part of the industry’s tradition that been established in many countriesfocusing in Malaysia. The industry’s way of survival is to recycle the profit gains from one project to another. **Conclusion:** In conclusion, there is no solution yet relating to payment issues in the industry. The implementation of CIPAA is still fresh to the industry and how far is it applicable and acceptable in settling the payment disputes is not been affirmed.

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**INTRODUCTION**

This paper focusing on construction industry disputes arrives from payment issues. Payment in construction industry involves money. Usually money is obtained by the relevant parties or been paid to them after the completion of the task. Sometimes payment is fixed according to stages as agreed in the written contract between the parties. The needs of payment and the amount of money should be paid not an issue as it commonly been discussed and agreed at the contract stages. The people in the industry also understand the concept of obligation to the written contract. To them payment is essential to finance their next project as well as to be at the top ranking in the industry. Without payment the industry cannot progress. In addition, payment issues can make the relationship go sour. This takes place when the payment scheduled is not being bound by the parties to the contract due to circumstances happened to the defaulting parties’

example poor financial management organization. At times the defaulting parties might be able or trying hard to solve this payment issue, yet due to the difficulties that they are facing the total amount paid is insufficient, payment was made not according to the time frame or schedule after several chasing or the worst part is no payment is made. In this type of situations the defaulting parties will get out with reasons to insure their own error in terms of payment. When this issue intervenes, it of course will affect the progress of the construction project.

At times it is not an intention of the parties (owner, contractors, subcontractors, and consultant) to be in the circle of this payment issue but to proceed and survive in the construction business, payment issue is not a new issue, it is normal and present here and there in the industry. Further, other factors such as the stability of the economic climate of a country can affect the industry and the players had no choice but to restrain payment or to hold payment at certain stages.

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Holding of payment might be serious to some state of mind however the parties (owner, contractors, subcontractors or consultant) do take this risk as positive in their dealings. Example the deal is made between the contractor and sub-contractors of a project. The contractor will employ few sub-contractors that are expert in the area that they are looking into and subcontract part of the project to them accordingly. In accepting the project, the arrangement of payment is been discussed, satisfied and agreed between the subcontractors and the contractor. The contractor then will have to deal directly with the owner of the project to ensure no issue arises in terms of financing the project as a whole. The project will then carry on as per written in the paper, the sub-contractors will done their part and request for progress payment until the completion of the task. If payment can be made as smooth as expected in the contract then no problem or issue will arise in terms of continuation of every stages of the project. However, problem intervenes when one parties defaulting in following the schedule of payment and it causes the proposed payment to stuck, money can't be banked in on time, due to not enough or no money to roll in the business, so payment cannot be made as per agreed and the continuation of the construction project is delayed and sometimes abandoned at certain stage.

These are the risk taken by those involved in the industry, if they are depending totally on the payment stage by stage to finance the project instead of having own money. If this took place, they will have to face the risk and having problem to go with other phases. On the part of the contractors who failed to pay, the survival of their business is at the higher ranking, if they can survive after utilize the money in hands they can lead the industry. However, they understand that 'the risk' here means if something happens in the middle of their journey to be at the top, they will lose business in the hands and normally are subject to legal suit etc. Reputation also can be disrepute at this point. They, the players in the industry are aware of the industry's playground, but they still venture and role-play their skills, effort and money. They take this as a challenge to them to grow and created a name in the industry.

The construction industry is a wide industry that will be further developed in line with Malaysia's aim to be a developed nation in 2020. The idea of the 2020 introduced by the former Prime Minister, TunDr. Mahathir Mohammad is to see the growth of the country in all aspects of social and economic. To be awarded and recognised as an industrialized and developed nation, economic growth of the country should be at the highest level. The Construction industry is one of the major contributors to the economic growth of the nation and relevant bodies should pay attention to the matters arising within the industry, find solutions so that the industry will not be affected.

At present, the industry and disputes are synonyms and not easy to be detached. Disputes arose in terms of payment, not complying with the time frame agreed, and also quality of works presented. These three are the main areas that lead to construction disputes. Litigation, adjudication, arbitration and mediation method of settlement were used to resolve the issuesbut it seems no avail. The dispute not easily comes to an end, as there are quite a number of dissatisfied parties around the industry. Therefore the matters prolong from a time to sometimes before it actually gets solutions.

Who are to be blamed? Should we put the blame to the owner, contractors, professional consultants, sub-contractors, employees, etc? The industry has no choice but to cover it, to ensure that our economy is growing steadily as planned in 2020. Give and take is Malaysian culture be applied for payment issues in the construction industry but how long will it sustain. Money is vital for everyone for their own aims, business planning etc. No one in the industry will tolerate much in term of payment as this six alphabet 'payment' is their most necessitated aim to survive in the industry and have a good life.

### 1. Literature Review:

Many writers have touched and discussed in many aspects of payment issues in the construction industry. Some of them did give solutions but still the solutions are not working without the initiative from the players of the industry. They choose the dealing and they should be given right to choose the best solution to settle the issue.

The article title Ethical Issues in the Construction Industry: Contractor's Perspective claimed that the construction industry is categorized as the most fraudulent industry worldwide. These unethical practices such as wasted tender expenses, tendering uncertainty, increased project costs, economic damage, blackmail, criminal prosecutions, fines, blacklisting and reputational risk gives significant impact in the industry. Focusing on issues of payment, from the survey conducted showed majority of the respondents had witnessed various forms of negligence in the construction industry which includes late and short payments, poor quality and inadequate information, lack of supervision, subcontractors' lack of safety ethics, bad documentation and unfair treatment of contractors in tender/final account negotiations respectively (Adnan\* *et al.*, 2012).

We are therefore of the opinion that payment issue is classified as negligence behavior and it actually gives higher impact to the industry in terms of quality of the services and timing of delivery of the task or finishing the project as required. If all the people in the industry are following ethical guidelines the issue of late, underpayment and non-payment will not go up. The industry classification as the most fraudulent industry worldwide also can be

warded off if payment is reconciled at the root level. When it's been patched up at this early point in the industry, the other stages will not be affected and will progress easily.

Further, in the paper "Late and Non-Payment Issues in the Malaysian Construction Industry-Contractors' Perspective (Danuri, Munaaim, & Rahman, 1999) the authors discussed on the main factors, effects and reactions to late and non-payment issues. The authors aim also to identify ways to sustain the issues in the Malaysian construction industry. The research however focused on payment from the employer to the contractors. Delay in certification, poor financial management, attitude and good governance are the factors payment that lead to payment issues. There are two stages of classification of payment issues in the industry; one is between the owner (employer) and the contractors and the other one is among the contractors and the sub-contractors. Yet the main solutions that can be viewed from any of these two stages are good organization or management of the finances of the clientele. If it can be well done, the issue pertained to payment will total to zero level at all levels.

Article on the Nature of Payment Problems in the New Zealand Construction industry, analyses the liquidators' reports and construction payment dispute cases filed in the High Court, to determine the nature of payment losses and delays in the New Zealand construction industry. In addition it reviewed some of the strategies used to deal with delays and losses by parties in construction contracts. Placing of a charging order or caveat registration, bankruptcy and liquidation proceedings, holding money in trust account, direct payment by sureties is been used as a remedy for non-payment.. The author also suggested topic for future researcher to investigate the success of those strategies (Rotimi, 2011)

We can remark that the success of any of the above strategies is depending on the negotiation between the affected and defaulting parties. When payment is not sufficient, or not been made at all, the affected parties will of course think of a solution that can favour their part. Some might not think wisely or long enough to their business sustainable, but proceed to bring legal action for e.g., bankruptcy proceedings that will give satisfaction to them when the defaulting parties is being judged as a bankrupt. This sometimes might not solve their main trouble that is to get payment to finance their project. Therefore the affected parties are to think wisely before make a move to any of the steps. Think the best and the win solutions, especially on their part before proceeding to uphold any of the above remedies.

Additionally, according to (Steve Cannon & Steve Gibson, 2014) in the article Adjudication of Construction disputes in Malaysia A new approach to dispute resolution, CIPAA will have a significant impact on construction and engineering projects in

Malaysia. Good contract management is important to the owner/employer, contractor, subcontractor or consultant so that every payment is made on time. However the challenges are a losing party may successfully challenge the adjudicator's jurisdiction by bringing the dispute to the High Court, where High Court has an enforcement power in their enforcement proceedings. Therefore to our point of view based on the discussion of the authors, CIPAA is not a 100% solution to payment issues. The channel is still open for losing parties and issue of payment in that circumstances will not be ended there instead of may be prolong at the other stages.

The authors (Sambasivan, 2007) in the article Causes and Effects of delay in Malaysian Construction Industry agreed that delay is a global phenomenon where Malaysia is also effected. In Nigeria for e.g. the factors of delay were due to finance and payment arrangements, poor contract management, shortages in materials, inaccurate estimation, and overall price fluctuations. In Malaysia itself the delay is due to (1) Contractor's improper planning, (2) Contractor's poor site management, (3) Inadequate contractor experience, (4) Inadequate client's finance and payments for completed work, (5) Problems with subcontractors, (6) Shortage in material, (7) Labor supply, (8) Equipment availability and failure, (9) Lack of communication between parties, and (10) mistakes during the construction stage.

The article also touched on prescriptions that can be applied to solve the problem. Overall the objective is to make the practitioners (clients, contractors and consultants) have better understanding on the dynamics of project management and make efforts to reduce the incidences of delays.

This article touched on variations in government contract in Malaysia, the authors were of the views that it is impossible to compete a project without variations been done to the plans or during the process. The delays in payment issue intervened as the variations can cause delay to the construction works plan. If the contractor does not have money (RM) or funds to pay the subcontractors, then problem will arise because some contractors are depending on clients' payment to settle the subcontractors' money (Jaspal Singh Nachatar, Abdul Azi Hussin, 2010). It is inter-related with each other and the bonding of payment issues and planning on the construction process is strong to the successfulness of the project.

In addition referring to article title Debts and Interest in the Construction Industry, (Johnston, 1999) the author was of the view that a survey of the payment performance has shown that construction industry, in particular, is disposed to late-payment culture. Looking and reading the article, we might suggest that late payment can be tolerated by discussion or negotiation at some points to assure the right relationship between the proprietor (owner) and

the contractors or the contractors and the sub-contractors. But how far this toleration should be extended? There must be limits to any toleration to avoid back stepping amongst the people in the industry.

In the paper on Issues of Late and Non-Payment among Contractors in Malaysia, (M. Fikri, Hasmori, 2012) the authors intend to study on the major source and effect of late and non-payment among contractors in Malaysia. The finding of the research shows that the potential cause of late and non-payment among contractors is paymaster's poor financial management and the major effect of late and non-payment is creating financial hardship. The findings of this study provide an insight on the issues of late and non-payment and the study also proposes a remedy to cure this problem. But is it workable, it depends on the people who run and manage the industry. Others can give views, propose ideas and solutions but will it work without the enforcement on the part of the individual in the industry.

May and Siddiqi (2006) state that well-timed run of money is required for the achievement of a construction project, commencing from the owner to the contractor downwards to the subcontractors, sub-subcontractors, suppliers, and vendors. If this method is being managed well by all those in the industry the solutions is no issues arise. However referring to the authors views the subcontract, contractors regularly will attempt to transfer the peril of the non-payment by the owner to the employed subcontractors. This will burden the subcontractors too in the circulation of the pyramid.

This is normal in any of the industry not excluding the construction industry, where the dominant parties trying to take control over the weaker parties. Where in construction industry, we can assume the dominant party at the stage of agreement between the contractors and sub-contractors are the contractors. Therefore if they, the contractors received or been paid insufficient amount of money, the money will be first use for the contractors' survival rather than thinking about the sub-contractors problem or survival. So that is the reason why the author above is saying that the peril of the non-payment is passed and be burdened to the sub-contractors.

The paper title Developing Methodology for Subcontractors' Security of Payment under Malaysian Construction Industry discussed and identifies the actual difficulties and legal issues disputed by the sub-contractor relating to payments. The researcher circulated questionnaire to various sub-contractors in Malaysia to ascertain their level of knowledge on the then proposed CIPA Act and also conducted semi-structured interviews with selected sub-contractors to evaluate various avenues to improve the payment process in the construction industry. According to the authors, most of the small-sized sub-contractors have limited knowledge on the

proposed 'Security of Payment Legislation' or the CIPA Act and while waiting for the implementation of CIPA Act, the sub-contractors have to bear with the current and problematic payment mechanisms in the standard forms of construction contracts. The authors did highlighted avenues that can be chosen to improve payment problems in Malaysia. Some of the suggestions are suspension of work or going slow, Eradication of "pay when paid", adjudication, liens, payments bond etc. (Supardi, Adnan, Rashid, & Yusuwan, 2012)

Pay and paid maybe a serious suggestion that need to be tried to get the actual taste of it in the industry. To our viewers this being practiced in the minor circle of the industry, but is it really been practiced accurately and being enforced strictly is still in the dark. Or what is the term pay and paid for them?

## **2. Late Payment:**

Late payment means delay in making payment according to schedule after the agreed work had been completed. Late payment also can be defined as payment made after the due date. In several contracts, the terms 'time is the essence of the contract' binds the schedule of payment. Parties to the agreement must comply with the terms on payment by following strictly the schedule agreed. Delay of payment or late payment can cause the ongoing project to be disrupted and some projects cannot even move or proceed to another phase. Sometimes due to this 1st step of late payment, it could contribute to the progress of work been stuck or unmoved. The contractors are waiting for employer's money to pay the sub-contractors and the subcontractors will utilize the money to pay his employee. This connection ties each other's work and payment related issues. In other situations the suppliers have not been paid or there was a late payment to the suppliers that make them stop supplying materials which is needed for the work to progress as promised.

Who is to be blamed on this matter? It is unanswered issue. Sometimes this has been looked into but the answers to it is not clear, the judgment to the solutions whom to be blamed or responsible for the action is quite difficult to be justified. Not all the contractors, subcontractors or the suppliers take in their own money to proceed in all stages, they are depending totally on the payment within stages to proceed level by level.

This late payment issue is not a new born baby in the mouth of the industry. It has been widely spread and been highlighted as one of the major problems facing by people in the industry. Studies have been conducted on the issues and new Act being implemented to settle it, but the question on the effects of those are still ambiguous. Those who manage each and separate portfolio in the industry, especially account side need to stay focused and be

aware of the work done to avoid late payment issue intervention. In other words, governance or management strategy of account controller is vital. The accountant must update each payment case and give notice relating to next due date before the times run. Safe and effective management system not solving the issue, 100%, but at least can serve reduce the challenges faced in payment related issues. We can put it that the financial management sides compulsory to know the time frame or timeline of payment to avoid delay in payment as the delay give big impact to the development of a project. Once put ourselves in the industry, working capital for the growing of the business is the serious matter. The impact of slow or no payment can be devastating. Slow payment erodes the profitability of the sale or, where profit margins are tight, eliminates it altogether. Uncertainties over the timing of payment make cash flow management and banking relationships, even more difficult. Chasing payment puts a strain on the owner-manager as well as on customer and supplier relations. Where slow payment progresses to protracted default and bad debt the whole viability and survival of the business can be at risk (Howorth & Wilson, 1998)

How to solve this? It actually depends on the attitude of those who manage the financial line of the company. The Company also can be the cause of the late payment issue, if the company did not manage their finances well and at certain point realized that they have difficulties or unable to release payment on time. The fault of one party in calculation and following strictly the schedule may cause other companies or individual being affected. This issue has prolong and quite difficult to be solved, although the contract has drafted the time frame. Honesty is the best policy and discipline is the best word that can assist reducing or put the issue of payment at satisfactory level i.e. zero stage issue. Here is the possibility of the financial management is well managed but there is no money that can be run off or utilize by the company to make payment as they need income to make payment and at the same time find other business for the company.

The concept of rolling of profit and trying luck in other related businesses makes the company unable to make payment on time. Money being spent and located here and there for the advancement of the company businesses and at the end, the problem of settling the debt or payment issues arises if the businesses not succeed as planned. At businesses line no one is perfect and no company is really strength, if they did not take the risk or have no braveness in tackling the challenges. They will have to try and achieved it through luck and hard work with full of risk which no one other than those who managed it knows better.

Attending talk, seminar and also amendment and implementation of the law to strengthen or showing the seriousness of payment issues is a failure if the

individual did not manage and prepared their financial desk well. Each situation has separate and different ways to tackle as there are quite a number of issues that are related to the issue of late payment. Attending seminar and talk about payment issue is just to create awareness and some of the speakers did provide suggestions and solutions but it won't succeed as individual mentality and behaviour control human and human controlled and managed themselves, their employee and the company.

### 3. *Underpayment :*

The term 'underpayment referred to payment made which is lesser than the proposed money or amount that should be received after the work has been completed either following phase per phase payment or at the full completion of the work. Some contractors for e.g. have difficulties to proceed to another phase or stages if the underpayment concept is being practiced. They have no money or not enough working capital to proceed. Sometimes they might have the money, but it is not sufficient or not enough for their next project. Therefore the work has to be delayed or at the worst side be abandoned if no further payment was made after the underpayment for some period of time.

Who is at fault here? No definite answer. Can they refer to binding contract to claim for underpayment amount? The answer to this is obviously 'yes', however when the law and regulations comes into picture, the procedures taken to solve the issues is taking longer than the duration of payment should be made. The claimant need to appoint solicitors, get advice and proceed with the claim. The Claim been filed in the Court, the process of servicing it to the defaulting parties, time limit that need to be complied, documents and evidence to be gathered and trial of the case is taking much hassle to the claimant. At the end whether justice is to be in the claimant favour or otherwise, or is a percentage solution is in the hands of the Court. We could not impliedly determine who the Court will decide for. Therefore the aim to get full payment on time is ambiguous and it will sometimes lead to unsatisfactory.

In the contract that been mutually signed and agreed between parties, e.g. the contractors and subcontractors, the terms were very nicely written. However, in the practical part of it, will the parties comply with the terms? Why are they still making default on the issue of payment or practice the concept of underpayment? The answer normally given is common i.e. they do not have enough money at that moment to make full payment or paid as agreed. When the money comes through other projects payment will be made. The negotiation took place for certain period of time and this might cause problem to the development of the project if the contractor itself are relying totally on the payment to proceed. They will have to stop at those stages whilst

waiting for payment and once again this cause others to be effected. Therefore what are the accurate solutions that can be suggested to throw underpayment issues from construction industry? Currently, this issue has not been satisfactorily settled. The implication of the underpayment issue is still at the mouth of the industries. The CIPAA been introduced to tackle payment issues, however as new legislation, CIPAA has limitation. The industry need time to study and familiar themselves with the Act and issue of applying or complying with Act is a further problem.

Hence the best solution at this stage, will be avoiding underpayment, paid as agreed and please care about others business as the same as you care about yours. All businesses need money and money is the mover of the businesses, without payment, no money and without money business will go hire wire. All in all underpayment is better than no payment, at least there is something rather than nothing to finance the next level of a project but still the outcome or target is unreachable. The industry's man must change their business tune from the older method of recycling the profit for project to spending when you are capable to. Means you have to get ready the solution for payment issue that is 'money' before decided to be part of the contract or to venture into the industry. This is just an advice solution which will not be practical in practice if people in the industry's not putting concern on this issue but are aiming on the profit target that they set in their business plan. Whether the target will give negative or unfair implication to others to be realized is the 2<sup>nd</sup> concern to them. Move fast like a bunny and risk thinking is later. Those who succeed and achieving the aim target is well done, but those who failed to achieve it, then the problem of payment to the involvement party as party to the contract will arise and together losses have to be shoulder. Back to back discussion, the prescription is still on the management of business and finance of the business.

#### **4. Non-payment :**

The word non-payment in logical meaning or common sense is no payment been made at all, it equal to work completed or done without any consideration. To be valid under the contract law, consideration is necessary in dealings between parties. Without consideration the agreement entered into or executed is considered void, unable to be enforced. Therefore occasionally in contract there exist an exchange of items with money as consideration and in the industry the same method apply where for e.g. the sub-contractors should be paid for the work done. Work done is equal to money and this is considerations from one to another. In this new era of the development nation, method of exchange of things is not acceptable; it is not considered as relevant at all. Payment is crucial. When someone been engaged e.g. subcontractors in

the industry been engaged to do the wiring project for the constructed building, the payment expected by them is in terms of RM. If they are not been paid with this RM it is considered no payment been made by the contractors.

Work done in construction industry by the contractors or even the subcontractors must be paid. They need to survive in the industry and will only survive with payments from the completed projects or stages payment according to the contract. No such words as gratuitous work been done with the intention to finance the pockets of other parties. Your hard work should be paid. It is unfair for those who have done their work as per agreed, to do another work of chasing payment that is deserved by them. This term chasing look not proper to the industry but it happened in the circle of the industry as non-payment issues are common to the industry.

The alternative to the solution might be legal proceedings been taken against the defaulting parties. However they (either owners, contractors, subcontractors) are used to the proceedings, and the technic of delay will still stand, time constraint to get payment on time for next project now been dragged longer when the matter is been brought to the Court. Other alternative would be to negotiate settlement by using the mediation method. How far this method been trusted? Can the negotiation at this facilitator stage prevail? Sometimes the answer is positive, it is successful and sometimes it is half settled and agreed but payment did not been made to the account as arranged. Delay and delay and delay always intervene in this non-payment issue with all types of excuses that at the end is non-fruitful to the innocent party. Pity them but that is the reality in the industry. However not all contractors, owner, subcontractors is facing with this issues. If you are unlucky you will be part of the issues, if you are lucky, your project move well with on time payment as agreed.

The ingredient that directs to the intervention of nonpayment issue is again the poor financial management. No money in the job or office account to be utilized for the front of the line. Again, here the weaker party will be involved as the enemy in the clientele, they move small and demand payment after completion of their project but they terminate up with closing their line of work as it cannot hold longer due to no credit payment into office account.

#### **Conclusion:**

Is there an accurate solution to the issue? It is hard to voice out. The organization of the project, communication, trust and confidence amongst the players are essential. Talk to each other as it is the best remedial solution. Negotiation, toleration can lead to beneficial ideas and settlement to the issues. is present and it can lead to beneficial ideas and settlement to the issue.

Lastly, trust and confidence is needed. It is solution for every problem. However please stand

away from the word betray and suspicious when you are in business relationship as it could lead to interruption of trust and confidence. Parties need to prove to each other their trust and confidence level and do as promise.

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