Construction Master Builders Australia - Responses to Questions on Notice

Parliamentary Joint Committee on Corporations and Financial Services

Inquiry into Corporate Insolvency in Australia

Public Hearing on Tuesday, 21st March 2023

Question 2 from Chair (p 63)

Could you find out what's held in retention across the sector? If you can't find out, it'd be interesting to know—if that's even a reality. But if it's what I would consider to be a large amount that could be ageing over a period of time, there could be an awful lot of risk of that money disappearing, which might be very much needed by some of the smaller players.

Response from Master Builders Australia

As far as we are aware, there is no consistent, nationwide source of data held on the aggregate value of retention payments in the building and construction industry. At this point it may be possible to generate estimates in several ways:

- Balance Sheet data provided by head contractors and subcontractors to the ATO.
- Through a special survey or research project which could capture this information.
- Through expanding the data collection mandate of the Australian Bureau of Statistics to include regular reporting on business assets/liabilities related to retention payments and any other items of interest.

There are three other matters relevant to this question that Master Builders also wishes to emphasise to the Committee. These matters highlight Master Builders' general policy propositions that policy change must be evidence based, proportionate and carefully designed to most effectively target the relevant policy problem or question. These are:

Proper contextualisation is important

Each week there are tens of thousands of payments made between business entities participating in the building and construction industry that go unremarked. A large head contractor will be likely to make or oversee hundreds of thousands of these payments each quarter.

For example, based on its contribution to general overall national economic activity, NSW is the jurisdiction in which it is likely that the largest number of such transactions would occur. In 2015, a research paper was released that examined the operation of the *Building and Construction Industry Security of Payment Act 1999 (NSW)* which took effect in 2000. The paper "*Adjudication in Australia: A Study of Adjudication - Activity in New South Wales for 2013/14*"[1] noted that during this period there were 817 applications received for adjudication. This level of 817 disputes over a 12-month period in a jurisdiction as large as NSW provides some evidentiary guidance to assist in establishing a realistic context which is sometimes lost.

This paper also highlighted the difference in the amount claimed by applicants, and the amounts that were independently determined to be owed. At the time of the study, only 556 outcomes of the 817 determinations had been released. Of the 556 determinations released, the aggregate of claimed amounts was $221.2 million and the aggregate of adjudicated amounts in the order of AU$80.6 million, suggesting that the actual amounts disputed were just over one third of what was actually owed.

Security of Payment laws

Security of Payment (SOP) laws are often referenced as a 'solution' to consider about the question of industry insolvency. Master Builders notes that such considerations are sometimes misguided as, although SOP laws have some role to play, this is but one of a number of mechanisms in place to claim payment. The dispute resolution provisions, which form the bulk of these laws, are usually only relevant once a payment has not been made and some form of low-cost, easily accessible, and reasonably rapid avenue to resolve any dispute is necessary. They do not deal with ensuring payment is made in the first instance.

[1] *Adjudication in Australia: A Study of Adjudication Activity in New South Wales for 2013/14* Michael C. Brand and Jinu Kim. Delivered at *The 6th International Conference on Construction Engineering and Project Management (ICCEPM 2015)*

It has been Master Builders' observation that over time the above three stated policy aims of such a jurisdiction (low-cost, easy to navigate, rapid outcomes) have been lost and the various state and territory systems have become increasingly complex, difficult to navigate, and frequently very diverse in their specific terms of operation. In simple terms, various State and Territory regimes have become so complex as to no longer meet their stated policy aim or deliver their intended policy outcomes.

Master Builders Australia (as a national body) has a long-standing policy position to support moves to restore SOP laws to better meet their originally stated purpose and policy intent, including through reducing the significant inconsistencies that exist between various jurisdictions so as to generate greater levels of compliance, understanding by industry participants, and swifter resolution of disputes where they occur.

Retention Trusts / Project Bank Accounts etc

These types of arrangements are similarly frequently considered as 'solutions' when addressing industry insolvencies. Again, Master Builders Australia has a long-standing policy position to not support the adoption or mandating of these types of arrangements. The reasons for this position include:

There is no evidence that they achieve the expected policy intent or purpose. There have only been limited instances where, for example, project bank accounts have been trialled in Australia. The results of these trials are either not available publicly, or have been applied to Government funded projects that involve parties who satisfy a range of other extensive minimum criteria in order to be involved in the project in the first instance.

Likewise, where retention trusts laws have been rolled out across a jurisdiction, there is no evidence to suggest that they have achieved the policy outcome expected or made any difference to the level of insolvency. To the contrary, there is growing evidence that the cost and compliance obligations arising from such arrangements are far more significant than estimated, disproportionately and adversely impact small sub-contractors, and have added to the cost of construction for clients and consumers.

Further, such arrangements are usually stated to be a method to 'protect' subcontractors involved in a construction project in the event an insolvency occurs involving a head or principal contractor. In other words, they are only relevant if something has gone wrong and an insolvency has occurred. Master Builders takes the view that, as a general proposition, the focus of debate should instead be on preventing an insolvency event in the first place and ensuring that the level of risk assumed by parties involved in a construction project is shared appropriately to avoid the prospect of an insolvency event occurring.

In addition, such arrangements fail to recognise that construction contracts have in place sophisticated arrangements that not only deal with payment obligations, but also other protections and liability mechanisms, such as set-off rights (e.g for defects), termination and default. Any trust regime has capacity to cut across these long-established and well-known contractual arrangements and adds to the level of complexity faced when seeking to resolve disputes as they arise.