

Parliamentary Inquiry into payment for subcontractors

Public hearing to the Environment and Planning Committee

29 May 2023



Department
of Transport
and Planning

Overview of presentation

The slides cover:

1. Overview of Building Framework
2. Overview of Security of Payment Framework
3. Importance of SOP Framework for a well-functioning building industry
4. Additional government levers to support flow of payments across building industry
5. Additional context on operation of the SOP Framework
6. Overview of work underway by DTP

Not intending to cover all slides in Opening Statement – but can be used where relevant in questions.

1. Overview of Building Framework

Building Act 1993

- Establishes the Victorian Building Authority (VBA) and other entities
- Licensing and registration requirements
- Building approvals
- Enforcement of non-compliance

Building Regulations 2018 Plumbing Regulations 2018

- Specific technical and procedural matters
- Categories and classes of licensing and registration
- Gives effect to the National Construction Code
- Forms

National Construction Code (Building Code of Australia and Plumbing Code of Australia)

- Performance requirements for building and plumbing work

Australian Standards

- Technical requirements (including where referenced in the NCC)

1. Overview of Building Framework – other legislation

Architects Act 1991

Establishes the Architects Registration Board Victoria
Regulation of architects

Building and
Construction Industry
Security of Payment Act
2002

Framework supports statutory entitlements for progress payments and provides an adjudication process to recover payments.

VBA monitors operation of the Act and oversees the adjudication process

Focus of today's presentation

Residential Tenancies Act
(Part 14 only)

**Not administered by the Minister for Planning except for Part 14
(regulation of caravan parks)**

Cladding Safety Victoria
Act 2020

Establishes Cladding Safety Victoria

Domestic Building
Contracts Act 1995

Minimum requirements for domestic building contracts
Establishes Domestic Building Dispute Resolution Victoria

Not administered by the Minister for Planning

2. Overview of Security of Payment Framework

Victoria's Security of Payment Framework

Building and Construction Industry
Security of Payment
Act 2002

Building and Construction Industry
Security of Payment
Regulations 2013

For persons carrying out construction work or providing relevant goods/services, the SOP Framework seeks to meet two key objectives:

1. Persons are provided **statutory entitlements** to receive timely payments for work undertaken; and
2. Persons are able to access a **process to recover payments** for work undertaken without the need for litigation.

If the first objective of the SOP Framework is working effectively (entitlement to timely payments), subcontractors and tradespeople *would only require a process to recover payment by exception*.

3. Importance of SOP Framework for a well-functioning building industry

An effective, efficient and strong SOP Framework ensures the flow of payments across the industry, which is critical to:

1. Support the building and construction industry – a critical sector that supports economic growth and jobs in the Victorian economy.
2. Mitigate the impacts of structural vulnerabilities in the industry, which lead to higher insolvency rates in the industry, particularly for subcontractors.
3. Support the financial viability of businesses and workers.

Despite the role of the SOP Framework to manage payment issues, the process does not resolve all payment issues experienced by subcontractors for at least two reasons:

- The matter is resolved outside of the SOP Framework (e.g. informal agreement)
- The SOPA adjudication outcome is not accepted and is then referred to relevant court.

3. Importance of SOP Framework for a well-functioning building industry

Mitigate the impacts of structural vulnerabilities in the sector

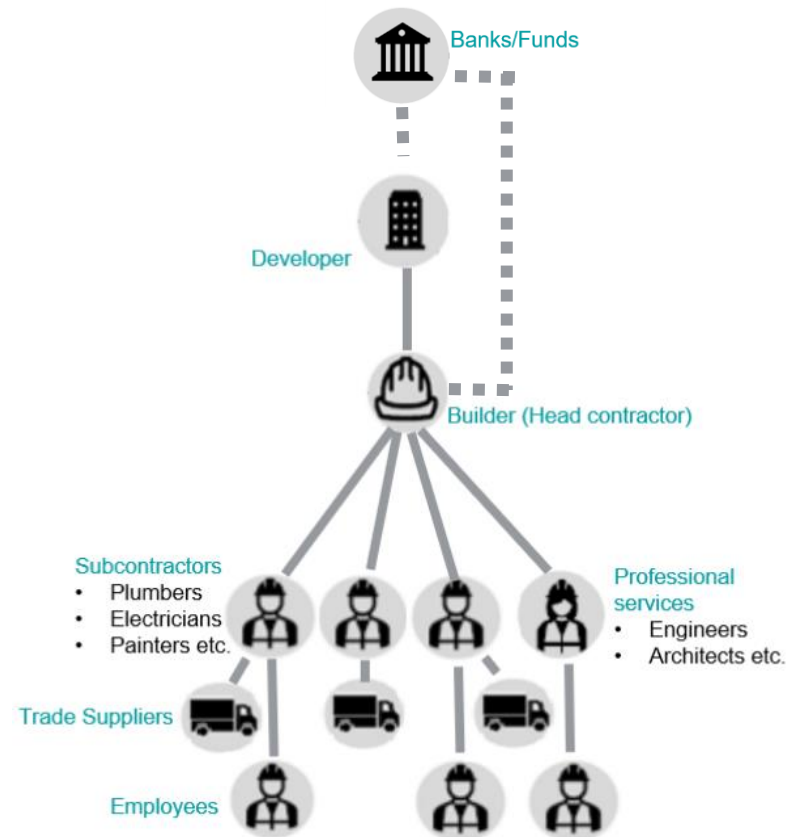
The SOP Framework is particularly important due to structural vulnerabilities in the sector, which lead to higher insolvency rates, particularly for subcontractors.

Structural vulnerabilities in the sector include:

- a lack of capital held by firms
- a fragmented market encouraging underquoting
- vulnerability to input price increases due to fixed-price contracts.

Anecdotal evidence suggest that payment practices are less than best-practice due to the structure of the contract-chain in the sector (see Figure 1). Late payment pushes cash flow risk down the contract-chain to parties less able to manage it.

Figure 1: Contract-chain for residential builds



4. Additional government levers to support flow of payments across building industry



In addition to the SOP Framework, government has a number of key levers to ensure the flow of payments in the industry:

- The *Domestic Building Contracts Act 1995* (Minister for Consumer Affairs – DGS).
 - Legal requirements for contracts a consumer enters into with a builder.
 - Limits on deposit amounts, restrictions on the stages of when payments must occur and statutory warranties for the consumer.
 - Establishes the Domestic Building Dispute Resolution Victoria which seeks to resolve disputes for both consumers or builders prior to a court or tribunal process.
- Victorian government procurement policies and procedures (Assistant Treasurer – DTF).
- Programs and supports to lift business acumen (Minister for Small Business – DJSIR).
- Relevant industrial relations rules (Minister for Industrial Relations – DPC).

Industry can also play a key role to support government efforts including:

- Developing and promoting programs to lift business acumen; and
- Supporting and promoting efficient dispute resolution processes.

5. Additional context on operation of the SOP Framework

Statutory entitlements to receive progress payment provided through SOP framework:

- A progress payment is effectively due 30 days after construction work was first carried out or goods and services were first supplied (if contract is silent). This consists of:
 - A statutory entitlement to make a claim for payment 20 days after construction work was first carried out or goods and services were first supplied (if contract is silent)
 - The due date for the progress payment is 10 business days after a payment claims is made (if the contract is silent)
- The amount of the progress payment is calculated on the basis of the value of the construction work carried out / value of goods and services
 - Definitions of 'claimable variations' and 'excluded amounts' can impact claim
- If a progress payment becomes due and payable, the claimant is entitled:
 - to exercise a lien on the unpaid amount over any unfixed plant or materials supplied

Should these statutory entitlements not be effective, the second key objective of the SOP framework can be drawn on by tradespeople to recover progress payments.

5. Additional context on operation of the SOP Framework

For 2021-22, key observations and findings from SOP adjudication process:

- Subcontractors initiated most claims. Most claims were made against a head contractor or developer.
- The majority of the number of claims made were less than \$50,000
- 39% of applications did not proceed to adjudication. Of these, 50% were withdrawn and 23% saw early settlement.

Recent decrease in adjudication applications due to pandemic disruptions (table 2)

Table 2: Number of adjudication claims

Year	Number claims
2021-22	324
2020-21	397
2019-20	551

Figure 3: Application by claimant (2021-22)

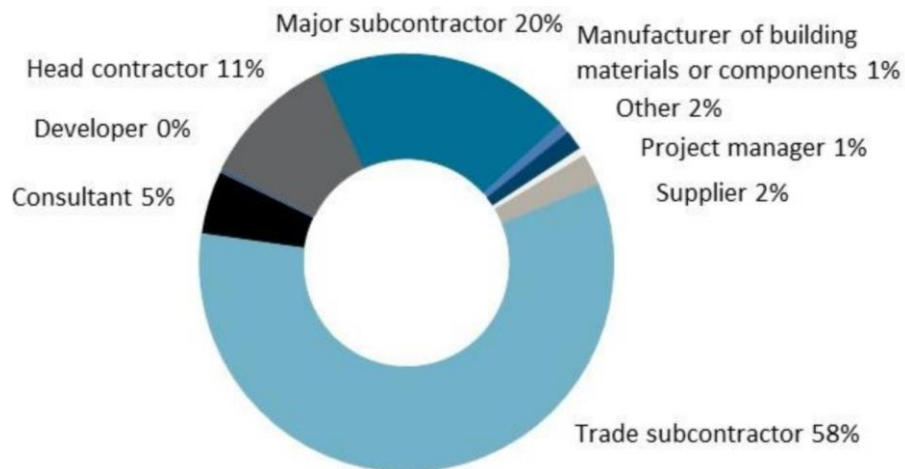
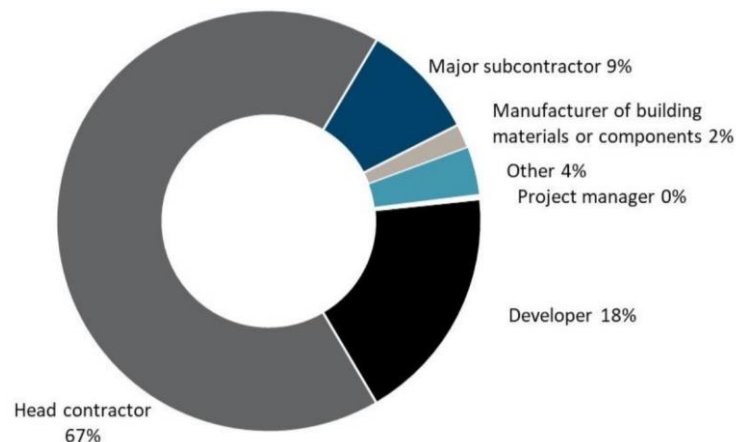


Figure 4: Application by respondent (2021-22)



5. Additional context on operation of the SOP Framework

Table 3: Victoria-wide distribution of adjudication applications (2021-22)

Region	No.	%
Ballarat	2	1%
Geelong	7	2%
Hume	1	0%
Latrobe – Gippsland	23	7%
Melbourne	249	77%
Mornington Peninsula	15	5%
North West	19	6%
Shepparton	4	1%
Warrnambool & South West	3	1%
Multiple	1	0%
Total	324	100%

Table 4: Melbourne distribution of adjudication applications (2021-22)

Melbourne area	No.	%
Melbourne – Inner	67	21%
Melbourne – Inner East	22	7%
Melbourne – Inner South	32	10%
Melbourne – North East	20	6%
Melbourne – North West	30	9%
Melbourne – Outer East	14	4%
Melbourne – South East	29	9%
Melbourne – West	35	11%
Total	249	77%*

*less than 100% since this is a sub-set of table 1

5. Additional context on operation of the SOP Framework



Table 5: Total number and value of claimed and adjudicated amounts by range (2021-22)

\$ Claims value Range	CLAIMED		ADJUDICATED		
	No.	Total \$ (mil)	No.	Total \$ (mil)	Total (% vs claim)
< \$25,000	136	\$1.6	84	\$0.6	40%
\$25,000 – \$99,999	91	\$4.5	59	\$2.0	44%
\$100,000 – \$499,999	75	\$16.0	46	\$6.1	38%
\$500,000 – \$999,999	13	\$9.7	6	\$3.5	36%
\$1,000,000 - \$9,999,999	7	\$15.6	3	\$6.8	43%
> \$10,000,000	2	\$68.8	1	\$11.1	16%
Total	324	\$116.2	199	\$30.1	26%

6. Overview of work underway by DTP

Key work underway by DTP to improve the operation of the Building system

- Review of Victoria's Building system
 - The Expert Panel, chaired by the Commissioner for Better Regulation, is undertaking a comprehensive review of Victoria's building system (e.g. the *Building Act 1993*)
 - This Review will be complete by the end of 2023, with supporting legislative reforms to be considered by government.
- Victoria's Cladding Rectification Program:
 - In 2019, the Victorian Government announced a \$600 million package to rectify higher risk private residential buildings with combustible cladding
- Supporting a more effective SOP Framework
 - Remaking the SOP Regulations, which will include consultation with industry.
 - Responding to any relevant recommendations arising from the Inquiry.



Questions and discussion