

TRANSCRIPT

LEGISLATIVE ASSEMBLY ENVIRONMENT AND PLANNING COMMITTEE

Inquiry into Employers and Contractors Who Refuse to Pay Their Subcontractors for Completed Works

Melbourne – Thursday 8 June 2023

MEMBERS

Juliana Addison – Chair

Martin Cameron – Deputy Chair

Jordan Crugnale

Daniela De Martino

Sam Groth

Martha Haylett

David Hodgett

WITNESSES (*via videoconference*)

Mr Pawel Podolski, Executive Director,

Mr Kent Johns, Head of Government Relations and Regulatory Affairs,

Ms Irma Beganovic, Government Relations Manager, and

Mr Chris Van Der Kooi, Councillor, National Electrical and Communications Association, Security of Payment Industry Forum.

The CHAIR: Hello, everyone. Thank you very much for joining us today. The committee is hearing evidence today in relation to the Inquiry into Employers and Contractors Who Refuse to Pay Their Subcontractors for Completed Works. This evidence is being recorded.

All evidence taken is protected by parliamentary privilege as provided by the *Constitution Act 1975* and further subject to the provisions of the Legislative Assembly standing orders. Therefore the information you provide during this hearing is protected by law, but if you go elsewhere and repeat the same things those comments may not be protected by this same privilege. Any deliberately false evidence or misleading of the committee may be considered a contempt of Parliament.

All evidence is being recorded. You will be provided with a proof version of the transcript following the hearing. Transcripts will ultimately be made public and posted on the committee's website.

For the Hansard record, can you please state your name and the organisations that you are appearing for.

Kent JOHNS: Kent Johns, Head of Government Relations and Regulatory Affairs for NECA.

Chris VAN DER KOOI: Chris Van Der Kooi, NECA Vic Councillor.

Pawel PODOLSKI: It is Pawel Podolski from NECA Victoria.

Irma BEGANOVIC: Irma Beganovic, Government Relations from NECA National.

The CHAIR: Would you like to commence by giving us an overview and making a presentation? And then we will move to questions.

Visual presentation.

Pawel PODOLSKI: Okay. Good afternoon, committee, and thank you for this opportunity. We would like to make a short opening statement on behalf of subcontractors from within various pockets of the construction industry. My name is Pawel Podolski, and I am the Executive Director for the National Electrical and Communications Association, or NECA for short, in Victoria. With me today are Mr Chris Van Der Kooi, who is a NECA Councillor; Mr Kent Johns, NECA's head of government affairs; and Ms Irma Beganovic, NECA's Government Relations Manager.

I wish to start by acknowledging the traditional owners of the land on which we are meeting. I pay my respects to their elders past, present and emerging.

The work presented in our submission is a joint effort and the reflection of effective collaboration of Victorian subcontractor associations – thank you – collectively representing thousands of Victorian workers, where we denote the commitment and important contribution these associations have made in the development of this submission on behalf of the respective members during what is an incredibly difficult time in the sector.

I go to the next slide. Nearly 360,000 Victorians are employed by the subcontractor sector relevant to the themes represented by our submission. Ninety-three per cent of these construction businesses are either sole traders or small businesses hiring up to four employees. Recent collapses of many builders in Victoria reflect the conditions facing the construction industry, with them leading to unprecedented risks of financial stress, insolvencies, job losses and reputational damage. That is because of reported year-to-date figures of 518 construction insolvencies in Victoria, which roughly represents just under 30 per cent of all insolvencies

nationally. This also represents an increase of about 45.5 per cent, almost double that of last year. Such pressures on subcontractors often go beyond the financial impact and affect the wellbeing of business owners, their employees and their families. We have heard firsthand of the impacts on the mental health of our subcontractor members, and the impacts can be quite devastating.

Through the outcomes of this inquiry and the subsequent recommendations, we believe that the government not only has an obligation to support and act in supporting the troubled sector but has a tremendous opportunity to implement changes which will ensure the building sector in Victoria is fair for all its participants.

We come to the last slide. The industry is recommending that the government enact stronger security-of-payment laws through the implementation of the Murray review as it applies to the state of Victoria. It is important for the government to ensure that the draft legislation reflects the recommendations in the Murray review, including provisions for cascading statutory trusts in favour of subcontractors and those further subcontracting to these below in the hierarchy. Simply put, any legislative change must ensure that subcontractors are paid for the work that they do. Subcontractors cannot be treated as a means of cheap funds and cash flows to undercapitalised builders and head contractors.

Also, the use of unfair contract terms in construction subcontracts is strongly linked to security-of-payment issues, and greater protections against unfair contracting are also urgently needed. We recommend that the government review our enhanced contract provisions in the sector to mirror the recent amendments introduced by the federal government. We also recommend that the government prohibits the use of certain types of unfair contract terms. In relation to government procurements, we believe that policy enhancements are needed to proactively require head contractors to strictly comply with security-of-payments and unfair contract laws.

Before we throw over to questions, I will introduce Chris Van Der Kooi, who is not only a NECA Councillor but also a business owner himself, to talk to a real-life story. Chris's example is at the very heart of the purpose of this important inquiry, with his experience being just one of thousands in Victoria.

Chris VAN DER KOOI: Thanks, Pawel. Previous construction projects part of Victoria's Big Build have left contractors unpaid, leading to financial distress and bankruptcies. In its current form the security of payment Act has not protected subcontractors. Small businesses have suffered losses due to non-payment for works completed; so in essence the government has paid for the work, the contractors like mine have done the work, but the builder in the middle has mismanaged funds or gone broke, leaving small businesses like mine holding the bag.

There is a need for stronger protections from unfair contract terms used in the construction industry. When large builders are awarded projects, they often enforce contracts with unfair terms that contravene the government procurement guidelines. This further disadvantages small businesses by removing rights and privileges that were once in the head contract, or worse, adding in terms like 'power of attorney' or changing security and warranty terms.

In a specific case we suffered a financial loss on a government project due to delays in payment from the main contractor going into administration. Attempts to recover our payments through the security of payment Act were ineffective, as the company was being liquidated. To make matters worse, false claims made by the builder impacted us when we were re-engaged in subsequent project works – that is, they claimed for work being completed, but they never passed on the dollars to us, so the end client would not pay for the same work twice.

We have experienced uncapitalised builders using cash securities of subcontractors as working capital for projects. They do not release funds when they are contractually obliged, thereby delaying approval of project milestones.

I will leave full recommendations for the security of payment Act to the NECA team, but as a contractor, I do find it strange that I have to pay \$5 up-front for a coffee, yet a builder offers \$500,000 for a new medical centre and he strings me out for 45 days. Thank you for your time.

The CHAIR: Thank you very much, Chris. I am really sorry for the stress and the mental anguish and the impact that what has happened to you will have had on your family and your life. We really appreciate hearing your story because often we hear about figures, dates and numbers and stuff like that but do not see the human

face of what is occurring. Thank you so much. I am sure you are a very busy person, and we really appreciate you making the time to be here.

I will open it up to the group for questions. We have got Martin Cameron, the Deputy Chair, Member for Morwell; David Hodgett, the Member for Croydon; Jordan Crugnale, the Member for Bass; Daniela De Martino, the Member for Monbulk; Martha Haylett, the Member for Ripon; and Sam Groth, the Member for Nepean. Members, I open the floor to you. Who would like to start? Daniela, thank you.

Daniela DE MARTINO: I will kick it off. Hello. Thank you very much to all of you for coming along, and in particular Chris for sharing that, because I am sure that was not easy for you. Thank you. I am probably putting this out to everyone there and whoever feels best placed to answer. How prevalent would you say the non-payment of subcontractors is across the construction sector of Victoria, and how prevalent would the underreporting of that non-payment be? We have the stats on how many people have gone through the SOPA system. I suppose what we are trying to also uncover is how many people are actually not even using that. If you have got a sense of it, it would be great if you could please share. Thank you.

Pawel PODOLSKI: Look, I might kick off. We have got a lot of experience in the room here, who have probably gone through exactly the scenario that you have put in. And, again, I think having Chris as a live voice for that will probably be good to close up, but it is very prevalent. As the industry body representing electrical and talking to all our colleagues in the broader subcontractor suite that you have seen, we hear this every day. We support our members through a number of commercial activities, through either legal and/or other commercial mechanisms, and this is a theme that we hear all the time. We also support our members through some of the mental health challenges that they go through as a result of that, and I can say to you very categorically that right now the demand for and the need for that kind of support is probably the biggest I have ever seen historically. I mean, people are really impacted – this is driving their lives. They are living and breathing it, they worry at night, and this is not something that is a one-off case in a few individual scenarios. This is impacting a very large proportion, some to various extents. I think, as Chris said, you need to pay for a coffee up-front, yet with a builder, any builder – or any head contractor, by the way, because it is not just always the builders – you have to wait for your money. This plays on everybody's minds.

In terms of the second part of your question, how underreported it is, I think it is hugely underreported. In terms of people who actually choose to tap into securities of payments, there will be a very small percentage. I do not have a number that I could refer to as a strong reference point. That is one of those silent killers in the industry, if you like, that people do not sort of call out, but we all know and we all experience that the current legislation is inefficient. It demands a very, very quick response time. A lot of our contractors, as I said before – and this is not just in our industry but industries across the board – are small businesses with four or less employees, but even the larger ones have six or 10 employees. They are not experts. They do not have legal teams. They do not have accountancy teams generally on their books. This is a very complex system for them to navigate. I will leave it at that. I am sure there will be follow-up questions, but this is a very prevailing issue.

Daniela DE MARTINO: Thank you for that.

Martin CAMERON: A question for you, Chris. Can you walk us through the process? Obviously you are working, and you have got family commitments and everything like that. When was the trigger point for you to reach out and seek help? Was it years down the track? Was it something that you were able to access straightaway? Or were you relying on getting paid, but you had started the next job and all of a sudden you had nowhere to go? Can you just walk us through that process of how you found it?

Chris VAN DER KOOL: Yes, sure. Currently, because of how contracts work, generally we start building the switchboards, we order / procure items to build everything, we pay all our suppliers and we pay all our wages instantly. Then with most projects we cannot do a claim essentially until a month down the track – and unfortunately because of how contracts work – we have got to keep on working. It is not until we are maybe 30, 60 or 90 days into arrears that we find out they have not paid their invoice. We do not have the mechanism to stop work because then we are in breach of contract. They are still legally allowed to string us out for 60, 90 days. Unfortunately what happened to my business was we got told, 'Oh, yeah, we'll pay, we'll pay,' and then essentially 60 days went past, another couple of days went past, and then bang, we got a letter saying they were in administration. All the fees went to the lawyers and all the security that we tried to enforce with our

invoices with the SOP Act unfortunately was all for nothing because the company was in liquidation before we could actually do anything about it.

Martin CAMERON: Thanks, mate. I really appreciate you laying that out there for us.

The CHAIR: Chris, have you seen companies do this before and then reappear, like phoenixing and stuff like that? That must be very difficult to swallow – when you have not received payment or have seen non-payment and then they turn up on another job under a different name. I will open up to the group. How prevalent is that in the industry?

Chris VAN DER KOOI: I think unfortunately there is too much churn and burn, as in what a company will go through. We have had some builders who will on purpose put a lot of their assets into a holding company, so all their plant, all their machinery, is held off to the side. They have a project that goes bad, they churn and burn to put it into their wife's name and then start up again with the exact same people. As a contractor, yes, it is extremely frustrating, but they are my bread and butter, so I cannot really throw them under the bus either, because when they do pay, they are paying our bills. I am not too sure what to do about it, but it is prevalent in the industry.

Kent JOHNS: I think that is a great question. The first question I think you asked, Chair, was, 'Why isn't it reported?' Because, if you are reporting it, your client is going to be that person. Whether they are phoenixing or restarting a new company, that is your business model. The reason that the under-reporting does go that deep is that our members find that you cannot make the complaint, otherwise you are going to ruin your business. And in the case of one of our other members \$100,000 was lost, and then he had to go back and work for the same people a month later to finish the job that he was not paid for just to pay for his family. I can genuinely tell you that that member was almost in tears having to explain to his family that not only did he not make money that year, he was in debt \$100,000. So they are not reporting it because – to be able to survive as a small business. And NECA represents – the majority of our businesses are full-time equivalents of less than five. These are small businesses, and they cannot go into liquidation because their collateral is their family home.

The CHAIR: Daniela.

Daniela DE MARTINO: This is a big question to ask, but maybe you can throw some light on it. I am not expecting the answers to everything, but what struck me is, just listening to these practices, the delays in payment. I was a business owner, but I had a retail shop. So if someone wanted an apple, they paid me at the time that they took the apple out of the door, which was, you know, helpful, because cash flow is king. I am wondering: where is the money going? So when the head contractor gets paid, why is that not that cascading down? What is happening to it? If anyone can throw some light on that, you know, that would be really, really helpful. Thank you.

Pawel PODOLSKI: I will have a first crack. Unfortunately, Daniela, I do not think there is one single answer to that question. It is a multifaceted problem. But look, if we simplify the many challenges behind the repercussions of this conversation, the business model that we are operating under is somewhat flawed.

The business model that we currently structure construction around is that it is from the bottom up – from the grassroots up. That is where the cash flow and the financing happens. By the way, Chris is a great example, because he is an example of a sub-subcontractor. So if you think of switchboards, which he mentioned, switchboard builders work for electricians, electricians work for builders/head contractors – so he is down the chain. The lower you go, whoever is at the bottom of the chain – ultimately, you know, it feeds itself up. And those parties, those subcontractors, are funding uncapitalised builders and/or head contractors. The actual scenarios for each case are probably different, but the underlying fundamental root cause, I would say, to a large extent, stems from a business model deficiency. They are using cash to fund their liquidity – their working capital – if you like.

Daniela DE MARTINO: Thank you for that.

The CHAIR: This is for the broader group. We have heard evidence from different peak bodies – from the Master Builders, from HIA and from the union movement – as well as from John Murray, who came and spoke to us. There have been changes made in New South Wales to legislation. There have been changes made in

Queensland to legislation and also WA. In terms of NECA's view, do you have a view on which state is doing it best? What could Victoria learn from other models?

Pawel PODOLSKI: Irma, I might hand off to you first, and then we will go to you, Kent, as well.

Irma BEGANOVIC: Yes, so we believe that the New South Wales model as well as the WA model provide a good starting point for Victoria, but ultimately, the recommendations made by John Murray are the ones that we would be advocating for, which includes cascading statutory trusts to ensure that the funds, the moneys, are held in trust and that subcontractors are legally entitled to them rather than through other mechanisms that are in place. But if we are talking about step-by-step approaches, I think New South Wales provides a very effective framework for maintaining cash flow as a starting point.

But we firmly believe that the Victorian government has an excellent opportunity to lead national reform in this space. We also know that federally the government made a pre-election promise to implement the Murray review, as you know from John's evidence as well, so this inquiry is that perfect opportunity to bridge the gap between what is happening in Victoria now. The significant rates of insolvencies at the moment demonstrate the extent of it. So we do see the ASIC figures, but they do not necessarily represent the end result and the end impact.

Sorry, Kent. Did you want to say something as well?

Kent JOHNS: Yes. I would probably put it in stronger terms. I do not think any state government has got it perfect yet, because the funds of the people that have undertaken the work are not quarantined. Until they are quarantined, whether it be a cascading trust or a statutory trust, whichever way works best to keep solvency and cash flow in the industry, unless those funds are quarantined from the tax department and from the banks, who know their commercial risks when they go into these enterprises – our members are not banks, they are not the tax department and they do not have the oversight of their clients' many corporate structures. So I do not think you could say that any state is a model. I think Victoria has a real opportunity, as we push for the federal changes, to actually put a model in where, having a trust situation, the responsibility would be sitting with the builder. He would then be breaching significant laws. Also the trust allows for the quarantined funds to be paid to the subcontractors for the work they have done before the head contractor can remove their profit and their fees, so all of a sudden you will also get payment times shortened dramatically. I think that is why, if you look at the subcontractors and the specialist contractors that have put in submissions to yourselves and the federal government, they are also being backed by significant employee groups such as the CFMEU and in particular – and we are grateful for them – the ETU for supporting this. Employer and employee groups are actually seeing this, because it is, for want of a better word, wage theft by a different name for our subcontractors.

The CHAIR: Martin, did you want to say something?

Martin CAMERON: No, I am all good. I am enjoying listening. Thank you.

The CHAIR: Kent, can I just ask: with the Victorian legislation, do you see that the Act needs to be amended or do we really have to start from the beginning using the 86 recommendations from Murray as the way to build our Act?

Kent JOHNS: If we can agree to that today, I am happy to leave. John Murray's has to be the platform. That is the only way – via the quarantining of our subcontractors' funds. That has to be the base. We have even seen in Queensland, where they have put what we thought was model legislation through, that it is still having teething issues and issues where payments are not being made. We are hoping that Victoria becomes the exemplar and adopts the Murray recommendations. NECA and Pawel and his team are more than happy to work with the government on that. John Murray, I must admit, while extremely passionate, knows this sector well. If you were to take his advice, I do not believe that that would be the wrong way to go.

The CHAIR: Can I just ask: if we had the Murray recommendations in place, what would it mean for someone like Chris? Can we sort of talk through Chris's situation and how the Murray recommendations would protect someone like Chris and his business?

Kent JOHNS: The main protection there is the quarantining of the funds. Whether it is a virtual trust or an actual trust, the moneys would come into the account, and the moneys could not leave. The subcontractors

would provide their invoices to the head contractor. I will give you a prime example: a plumber, an electrician and a carpenter all put in \$100,000 worth of invoices each. That is their bill, so there is \$300,000. The head contractor may put his margin on there – call it another \$200,000 – so there is \$500,000 there. The head contractor cannot remove his \$200,000 until he has paid \$100,000 to the plumber, \$100,000 to the electrician and \$100,000 to the carpenter, and then he can take his funds away. That quarantine guarantees that (a) he is going to pay quicker and (b) he is not going to use those funds for possibly another contract that is not working as well or to prop up a poor balance flow or a poor business decision; those funds are guaranteed. With the example of a government contract – and this is occurring on government contracts as well – the government knows that the work that has been done for that government has not only been paid for to their contractor but has also been paid to the people that did the work.

Irma BEGANOVIC: I think in the submission made by Mr Murray he identifies some of the deficiencies in the Victorian legislation and provides recommendations for that as well. Some of the current provisions simply are unfair and undermine the integrity of the current legislation. But in terms of how someone like Chris would benefit, I will just throw that to Pawel for a bit of an explanation of how the statutory trust framework could work.

Pawel PODOLSKI: Look, I think actually, Kent, you did a pretty good job. In essence, it needs to be defended, so I do not think I will go through the trust explanation. I think you did a pretty good job without getting too technical about it. But the other ways or the other repercussions of how businesses like Chris's and many others would benefit is the simplicity. So every time there is a dispute around this, there are legal costs incurred, and many of those small businesses either do not have the technical expertise or the know-how to know when to go and seek legal advice such that they meet the time frames or simply churn through another \$20,000, \$30,000 just to get what is rightfully owed to them. So I think what Kent explained as a cascading trust structure, which is fairly simple and would not carry the complexities of a full statutory trust, which can – and we both know in other industries that there are complexities in managing that. So in keeping to the spirit of speed, agility and simplicity, cascading trusts certainly have a lot of benefits and are probably the biggest game changer in the conversation here. But as a result there are things like legal cost reductions.

It also takes care of the multiple layers in the hierarchies of subcontractors because that principle needs to be applied down. So it is not only about a particular segment of the industry being the bad guys versus good guys, and we are certainly not here to demonise any part, because there are some very, very good builders out there. There are some very, very good head contractors as well. But, as I said before, I think it is a business model structural issue. So subcontractors who are employing subcontractors would also have to do the right thing. And by the way, there are probably subcontractors which do not do the right thing by their subcontractors. So it is a game that I think creates a level playing field.

So John Murray's report is absolutely something we do strongly support to a large extent. Just on that reason alone, I think that sort of solves a lot of the problems without getting into the nitty-gritty of some of our other complications.

Irma BEGANOVIC: I think it is important to note that the application of statutory trusts does not in fact create an enormous administrative burden to businesses who already have accounting practices in place. So that is a myth in itself, so to speak. And it really depends on the appetite of the Victorian government – to what degree they wish to improve the current situation within the state. I believe that the Murray recommendations provide an excellent guideline, and I think it is important to conceptualise where Victoria was at the time of the drafting of the review and take into account John's recent submission and what the last five years really represent in the sector for this state.

The CHAIR: Thank you for that. Looking to the committee, is there anything else you would like to add while we have NECA here? Well, that is all good. Was there anything else that you would like to share with us before you finish today? Is there anything else that you would really like to make sure is strongly reinforced?

Pawel PODOLSKI: So I will hand off to Irma in a minute to maybe provide some last inputs, but one thing I just want to re-emphasise: going back to the initial recommendations, we talked a lot about securities of payment structure and the need, but one thing we should not forget about is the aspect pertaining to unfair contracts as it relates to this broader conversation, because one sort of follows the other. They are slightly different, but I think they cannot be held as siloed conversations, because unfair contracts drive some of the

behaviours that we have got here and the deficiencies, and therefore the cycle continues. So I just want to remind the committee the three-pronged approach and the three-pronged recommendation from NECA is for a reason. That is the reason I think we need to ensure that that gets driven forward collectively. Irma, for you to finish.

Irma BEGANOVIC: Absolutely, I agree. On unfair contracts, I think the disproportionate allocation of risk, the imbalance of bargaining power, is a very important aspect to consider as part of the reform. In terms of procurement, government is a significant purchaser and has the opportunity to ensure that government projects really do secure payments not only at the top level but all the way down the contractual chain.

If I can just add, from NECA's point of view we again collectively commend the committee for conducting this important inquiry. I think your terms of reference were excellent. I have read some of the submissions from various participants, and I think whilst aspects such as industry education are important, we just believe that that is not enough to make a change and to ensure that at least the effects of insolvencies are not felt as widespread as they are now. We are more than happy to support the committee from a subcontractor's point of view with all our industry partners who have collaborated with us on this, who have worked really hard and contributed their views and their experiences. We can certainly help with industry sessions, consultation sessions, whatever it is, to help inform the further work of the committee, the report or the government's work down the track hopefully. I do not know if Kent and Chris want to say anything else.

Kent JOHNS: Sometimes I say it too bluntly, but I think in regard to government procurement, 'outlawed' is not the right word, but subcontractors should not be expected to sign contracts that are more onerous than the government contract that the head contractor is provided. That is happening in our industry a lot, and not only is it not fair, it should be illegal, because the benefits and the risks that are associated with those contracts should be shared proportionately. We are finding that the risks are being pushed down to our subcontractors and not accepted where they belong. That is probably the last part of it. I think, Chris, you might want to reinforce that with the contracts you have had to perform.

Chris VAN DER KOOL: Yes, definitely. We are in the trenches, we are doing the work, and it just feels like we are getting whacked over the head because we do not have the bandwidth to fight them. We need to have some sort of mechanism there to say, yes, it is outlawed. We want to do the work – we are part of the Big Build; we are being engaged to do this – but I feel like we are getting clobbered a little bit. And it is disproportionate to what we do. I appreciate the time. Thank you.

The CHAIR: Terrific. We are indebted to you all for coming to talk to us. I do not know about the others, but I really like some bluntness, Kent, so thank you very much to you. Chris, thank you for sharing your experience. I hope things are a lot more positive as you move forward, but really that live, up-to-date version of what is happening in the industry, hearing it from you, has been really powerful. Thank you, Pawel and Irma, for making yourselves available. I know how busy you all are. Thank you also to the organisations that you represent.

We will make sure that you receive a copy of the transcript in the next few weeks for proofreading. We look forward to sharing our inquiry report with you. Thank you for being so generous with your time and insights today.

Committee adjourned.