



SENATE ECONOMICS REFERENCES COMMITTEE

INSOLVENCY IN THE AUSTRALIAN CONSTRUCTION INDUSTRY

SUBMISSION BY THE
CONSTRUCTION, FORESTRY, MINING AND ENERGY UNION
1 MAY 2015

CFMEU



***In the construction industry,
success comes as a result of your
ability to use other people's money.¹***



¹ Quoted in the Collins Inquiry Final Report, page 77.

EXECUTIVE SUMMARY

1. Corporate insolvency in the Australian construction industry is not simply a matter of poor business practices. It is a major area of unlawful and unethical behaviour and has been for many years.
2. Thousands of civil and criminal breaches by companies and their directors are reported to the corporate regulator ASIC by external administrators each year. Hundreds of millions of dollars are lost to businesses, employees and taxpayers through insolvency in the industry. Large contractors are delaying and diverting funds away from the reach of smaller operators who perform the majority of the work. Unscrupulous operators are deliberately abusing the corporate form to defeat legitimate creditors. When these contractors collapse - and they regularly do - they take other businesses with them. Livelihoods are destroyed.
3. The fiduciary responsibilities imposed on company directors by the Corporations Act are obligations on paper only for many people associated with insolvent companies in the construction industry. Most of the individuals responsible for these practices are never held accountable for their actions.
4. In the last ten years, more than one in five of all insolvency events occurred in the construction industry. The industry has consistently ranked either first or second amongst all industry categories for the number of mandatory reports lodged with ASIC by external administrators.
5. The most conservative possible estimate is that insolvent companies in the construction industry had a total shortfall of liabilities over assets for their creditors of \$1.625 billion in the 2013-14 financial year. A more realistic estimate for the year, based on median figures, puts the amount at \$2.72 billion. Sixty seven companies in the industry reported a shortfall of over \$10 million each in that year.
6. Unsecured creditors such as smaller subcontractors (and their employees), usually bear the brunt of corporate insolvencies. In 2013-14, the chance of an unsecured creditor receiving nothing from an insolvent company in the industry was almost 92%. Yet many small contractors remain reluctant to go public about the problem for fear of commercial consequences.
7. According to external administrators' reports, unpaid employee entitlements of companies in the construction industry experiencing an insolvency event in 2013-14 amounted to almost \$57 million at the lower end, up to a median amount of almost \$137 million, about \$63 million of which was unpaid superannuation.
8. ASIC administrators' reports put the figure of unpaid taxes and charges for construction industry companies for 2013-14 at a lower end figure of \$178 million to a median amount of \$487 million (in round terms). Since its introduction, the cost of the taxpayer-funded Fair Entitlements Guarantee scheme and its predecessors across all industries has been \$1.3 billion, of which only 14% been recovered through the liquidation process.
9. More than three quarters of all administrators' reports lodged in 2013-14 identified some form of civil or criminal misconduct by insolvent companies and their directors. The construction industry accounted for more than 20% of these. In that year alone, there were 2393 potential breaches of the general fiduciary duties of directors and the duty to prevent insolvent trading, reported for the construction industry.
10. Across the entire economy ASIC reported only two 'enforcement outcomes' under the heading 'insolvency' for the full two year period 2013 and 2014. For 2014, there were 51 'corporate governance' enforcement outcomes, including only 19 'actions against directors'. Forty company directors were disqualified in that year.
11. There has not been a single prosecution taken under s 596AB of the *Corporations Act* - a section directed to agreements or transactions that prevent the recovery, or reduce the amount of, recoverable employee entitlements. The section was introduced by the Howard Government in 2000 following the public outcry over a spate of high profile corporate collapses.
12. The Federal Government has recently cut ASIC's funding by \$120 million over a four year period. In the current financial year it will lose 12% of its operating budget and 209 staff. By contrast, the Government has increased funding for the industrial watchdog, FWBC.

13. Across its entire area of corporate and marketplace responsibility, ASIC obtained civil penalties against companies/directors of just over \$3 million in the six months to December 2014. FWBC obtained \$2.26 million in penalties, mostly against unions and workers, in the 2013-14 financial year.
14. There is an urgent need to reform the industry to deal with the insolvency problem at a national level.
15. A statutory trust scheme along the lines recommended in the 2012 Collins inquiry in NSW, coupled with a mandatory rapid adjudication process is a central part of a suite of measures which should be considered. Others include:
 - a revision of section 596AB to provide a workable mechanism to capture transactions which have the effect of denying workers their lawful entitlements;
 - the introduction of appropriate personal liability and director disqualification measures;
 - minimum capital investments for new companies run by directors who are the subject of previous adverse reports; and
 - a more active intervention on the part of the regulator to deter unlawful behaviour.



INTRODUCTION

The Australian construction industry accounts for a disproportionately high number of corporate insolvency events. The most recent ASIC statistics² show that 22.8% of all companies entering into some form of external administration in the 2013-14 financial year came from the construction industry. This was the second highest of all the industry categories, behind the 'Other (business and personal) services' category.

The profile of these failed construction companies shows that they are usually small, undercapitalised and based on the Eastern seaboard, most likely New South Wales. Typically, they operate on tight profit margins and eventually collapse because of poor cash flow. When they collapse they have no assets and hundreds of thousands of dollars in liabilities. Whilst these companies may not necessarily have secured creditors, employees will typically be owed somewhere between \$0 to \$100,000. Statutory creditors such as the Australian Taxation Office (ATO) and Office of State Revenue (OSR) will be owed up to \$250,000 or more in some cases. Trading creditors, such as suppliers and subcontractors, may also be owed many thousands of dollars. The chances of any creditor seeing one cent or more for each dollar owed to them is less than 9%.

Disturbingly, a significant number of these corporate failures are no mere product of poor business practices or the boom/bust economic cycle of the construction industry. There is a longstanding problem of 'phoenix companies' in the industry. This involves individual business operators deliberately misusing the corporate form to avoid paying legitimate creditors. Eventually the debt-laden company is wound up leaving creditors with no realistic prospect of recovering their money. Within a short period - in some cases a matter of days - the same individuals re-emerge in a new corporate form and the cycle is repeated.

The economic and social impacts of corporate insolvencies in the industry are far-reaching. Unpaid debt in an industry which is characterised by an hierarchical and interrelated system of contracts and sub-contracts can have an impact not just on those with immediate dealings with the insolvent business.

Often the problem has a cascading effect on businesses and employees in other parts of the contractual chain or on unrelated projects. And while some businesses have the economic wherewithal to absorb some level of bad debt, many do not.

A company collapse in the construction industry can spell economic disaster for other businesses and unemployment and lost entitlements for employees who are many steps removed from the insolvent company. Where a collapse involves a head contractor it is often the unsecured subcontractors (and their employees) who bear the brunt of the financial impact, since they stand behind administrators, banks and direct employees in the payment queue.

Collapses can also cause project delays, reduce the industry's overall productivity and build in costs to the construction process which must be borne by other contractors and clients, both public and private. The risk of company failure is a fact of life in a process that is by its very nature, replete with uncertainties.

The adverse effects of corporate insolvencies extend well beyond the construction industry. Public revenue authorities such as the ATO are regularly amongst the creditors of these companies, particularly where 'phoenixing' is involved. Revenue lost as a result of this phenomenon increases the burden on Australian taxpayers and diminishes the capacity of the Government to provide essential public services.

It is a fundamental principle that those who perform the work should be paid for it. Unpaid commercial debt is a clear infringement of that principle. Corporate insolvencies in the construction industry represent a serious structural problem which cannot be tolerated.

Existing laws and regulatory arrangements have failed to reverse a situation which has prevailed for far too long.

A strong, nationally coordinated response from Government is urgently needed.

² ASIC Report 412 September 2014.

1. THE CAUSES OF INSOLVENCIES

Brief Industry Overview

Over a number of decades the Australian commercial construction industry has been transformed from an industry dominated by construction companies with large, directly employed skilled workforces to a pyramid of contractual relationships involving a head contractor at the top and multiple layers of smaller specialist subcontractors underneath.

Typically, the management of major projects is assigned to a head contractor who is not a direct employer of any significance of the labour on the project. These head contractors contract with the owner/developer on one side and with major specialist subcontractors who undertake packages of work, on the other. Depending on the value and scale of the project, the greater proportion of works is then sub-let to other specialist subcontractors. As a result, there is often no direct contractual relationship between the persons performing the bulk of the work being undertaken on the project and the head contractor who is being paid by the client. This structure has the immediate consequence that the entity being paid to deliver the project will be receiving payments which for the most part, is for work performed or materials supplied by, someone else.

In 2012, the NSW Government received a report it had commissioned from Bruce Collins QC, on the insolvency problem in the NSW construction industry. The report followed a series of high profile collapses in that state where subcontractors and suppliers were left owing millions of dollars. An extensive consultation process was undertaken with industry participants, including the CFMEU. The Collins Report observed:

In the modern world of building and construction, approximately 80% of the amount of money claimed in a builder's progress payment will be claimed as a result of work carried out by one or more subcontractors and suppliers.

Imbalance in Resources

Another widely recognised feature of the industry is that there is often a lack of commercial sophistication and resources in many entities at the lower end of the subcontracting chain. Large major contractors are

able to impose and take advantage of favourable contractual terms that allow for unreasonable progress payment schedules and offer little recourse in the event of delayed or reduced payments. The Collins Report noted that the due date for progress payments for subcontractors can range anywhere from 14 to 80 days, with the average payment term falling somewhere between 45 to 60 days. The Report observed that it was common practice that payments were delayed or reduced to the detriment of subcontractors.³

The lack of sophistication, combined with the unequal resources and bargaining power between subcontractors and major contractors, the legal distance between many subcontracting entities and the head contractor, and the financial interdependency inherent in the hierarchical system of subcontracting, all contribute to the insolvency problem that confronts the industry.

Vertical Integration of Major Construction Companies, Risk Shifting and Profit Taking

In the last decade or more there has also been a major restructuring in both the commercial property market and role of major construction companies in that market. This has had significant implications for the contracting process and the allocation of financial risk within the industry. This change has seen many of the major corporations move away from the traditional model of domestic constructor supplying and managing the supply of construction services simpliciter, to major multinational corporations with strong links to the capital markets and a diverse role in financing, developing and managing major projects. One need only look as far as the current model of the two major Australian construction groupings – Leighton Holdings and Lend Lease – to observe this phenomenon. Some commentators have described this transformation as construction companies today being *'as much about investment banking and risk trading as putting up buildings'*.⁴

As Rafferty et al have argued, the commercial property market has become a distinct and more liquid asset class into which global investors can allocate and remove capital through for example, real estate investment trusts, in a way not previously available to traditional property owners. In this

³ Page 42.

⁴ *Risking It All - Financialisation and Labour in the Construction Industry* - Dick Bryan, Michael Rafferty, Phil Toner and Sally Wright

context the major head contractors themselves, or entities within their corporate group, have seized the opportunity to play an important role in financing and developing projects and even managing the property trusts that have come to own and manage completed projects. They are also careful to ensure that their contractual arrangements allocate as much of the financial risk and responsibility as possible to others and that they reserve as much of the discretion in the payment process to themselves. Particularly in the case of the construction process, these risks are foisted onto those who are less well-resourced and further down the contractual chain. Importantly however, there are also few if any limitations on the use of the funds from one project which is temporarily in the hands of a major contractor, to fund unrelated investments or projects. Thus subcontractors on one project can be exposed because of failures elsewhere, including on those ventures that have been bankrolled by monies that should have flowed on to them in the first place.

Whilst the extent to which these factors directly cause insolvencies in the industry might be debatable, there can be little doubt that they heighten pressures already built in to the hierarchical system of contracting in which the major contractors hold most of the important cards. This includes the capacity to delay the timely release of funds to subcontractors who have done the work and the ability to temporarily allocate capital to destinations outside of the project itself.

The Collins Report described this latter phenomenon as being *'firmly and repeatedly supported by all the evidence'*. It said:

'...payments or leakages from the project payment cycle to any of the five 'leaked' destinations outside of the project pyramid, is unacceptable. These external payments may be broadly summarised as:

- *paying off the tail of other jobs or paying claims relating to other jobs;*
- *paying off or reducing a bank overdraft or other loans or debts;*
- *purchasing property;*
- *discretionary expenditure of a personal nature; and*

- ***perhaps, most importantly of all given its susceptibility to cyclical movements in the financial market and the economy generally, collateral development activity engaged in by the builders.***

These five destinations described in detail later in this Report are the means by which the rights of subcontractors to be paid are compromised. They are unacceptable and in the view of the Inquiry each must be placed beyond the power of the head contractor to accomplish.' (emphasis added)

Some Figures

In the last ten years the construction industry has accounted for a significant proportion of all insolvency events nationally [see Table 1]. In the last three completed financial years, the construction industry was ranked either first or second, alternating with the *'Other (business and personal) services'* category, for the number of mandatory reports lodged with ASIC by external company administrators (liquidators, receivers and voluntary administrators).⁵

Table 1

Financial Year	Number of Construction Industry Insolvency Events	Construction Industry Insolvencies as a Percentage of all industries
2004/05	935	20.1
2005/06	1177	20.3
2006/07	1396	20.3
2007/08	1517	21.9
2008/09	1760	22.8
2009/10	1905	24.1
2010/11	1862	23.1
2011/12	2229	22.1

Initial external administrator's reports require administrators to specify one or more of thirteen categories of nominated causes of company failure. For the construction industry, the single category *'inadequate cash flow or high cash use'* represented almost 19% of the nominated causes of failure. Many nominate multiple causes of failure.

⁵ ASIC Report 412 – Insolvency Statistics: External Administrators' Reports (July 2013 to June 2014) – September 2014, page 6.

The Scale and Incidence of Insolvency in the Construction Industry

Table 2 – Nominated causes of failure – Construction Industry – (1 July 2013 to 30 June 2014)

Causes of Failure	Number Nominated in Administrator's Reports
Under capitalisation	435
Poor financial control, including lack of records	660
Poor management of accounts receivable	336
Poor strategic management of business	892
Inadequate cash flow or high cash use	1,000
Poor economic conditions	558
Natural disasters	17
Fraud	30
Deed of company arrangement failed	35
Dispute among directors	52
Trading losses	698
Industry restructuring	50
Other	611
Total	5,374

According to the NSW Collins Inquiry Final Report⁶, the most commonly cited causes of insolvency in the industry are:

- insufficient capital together with excessive debt;
- poor financial management skills;
- an inability to manage the scope of projects;
- lack of requisite expertise for a particular project;
- low margins;
- payments withheld or not paid;
- fraud; and
- poor economic conditions.⁷

Whilst the Collins Report recognised that there is often not a single causal factor in cases of insolvency, it also noted that *'one of the most powerful additional causal factors of insolvency applying to the subcontractor, is the insolvency of the head contractor itself'*.⁸

⁶ Bruce Collins QC - Independent Inquiry into Construction Industry Insolvency in NSW – November 2012.

⁷ Page 40

⁸ Ibid

CASE STUDY:

Profile of a Crash – Steve Nolan Constructions Pty Ltd

On 4 February 2014 NSW based company Steve Nolan Constructions Pty Ltd went into voluntary administration. The administrators immediately advised all creditors that the company had ceased trading some time before their appointment, that the company would not be trading and that they would not be accepting responsibility for outstanding orders or requiring further supplies.

Reports at the time of the collapse estimated that there were in the order of 200 creditors owed up to \$30 million. Lawyers for the company said the amount outstanding was 'not in excess of \$8 million or \$9 million', not including the \$16 million owed to secured creditor, St George Bank. [<http://www.afr.com/business/construction/in-administration-but-steve-nolan-constructions-profit-funded-property-portfolio-20140212-ixt0q>]

The large number of unpaid subcontractors were told they should cut their losses and finish the work. It was also reported that just prior to the company failure it had built up a significant property portfolio. The company's sole client Ralan said that it had paid the company for every outstanding invoice and even lent it \$3.5 million in 2013 to keep the business afloat. 'Where was that money coming from to purchase those properties?' Ralan Group managing director William O'Dwyer said to *The Australian Financial Review*. 'It's a property empire built up coincidentally over the last four, five years during the time he was building projects for me.'

AEC records also revealed that the company had donated \$150,000 to the LNP in New South Wales, and \$50,000 to the LNP nationally, in late 2012 and early 2013 [<http://periodicdisclosures.aec.gov.au/Donor.aspx?SubmissionID=51&ClientID=32934>] and \$50,000 to the Free Enterprise Foundation [<http://periodicdisclosures.aec.gov.au>Returns/51/RFY18.pdf>]

At the time of writing, the administrator's advice as to the likelihood of dividends being paid to unsecured creditors was 'not known'.

2. AMOUNT OF MONEY LOST TO CREDITORS INCLUDING EMPLOYEES, SUPPLIERS, SUBCONTRACTORS, GOVERNMENTS.

Unsecured Creditors

Unsecured creditors, generally subcontractors (and their employees), usually bear the brunt of construction industry insolvencies.

All external administrators' reports filed with ASIC for 2013-14 identify unsecured creditors as being owed money at the time of the insolvency.

More than three quarters of all insolvent companies in the industry are indebted to less than 25 unsecured creditors. But whilst almost 60% of these companies owe their unsecured creditors less than \$250,000, in 2013-14, of all the industry categories, the construction industry had the second highest number of insolvencies - twenty-four - of those where unsecured creditors are owed in excess of \$10 million.

Table 3: Number of Unsecured Creditors and Amounts Owed – Construction Industry (1 July 2013 – 30 June 2014)⁹

Number of Unsecured Creditors	Number of Reports	% of Total Reports for the Construction Industry
Less than 25	1667	77.4
25-50	231	10.7
51-200	217	10.1
More than 200	15	0.7
Unknown	23	1.1
Total	2153	100

Amount Owed to Unsecured Creditors	Number of Reports	% of Total Reports for the Construction Industry
Less than \$250,000	1283	59.6
\$250,000 - \$500,000	296	13.7
\$500,001 - less than \$1 million	224	10.4
\$1 million - less than \$5 million	279	13
\$5 million - \$10 million	47	2.2
Over \$10 million	24	1.1
Total	2153	100

Disturbingly, over 90% of companies which owe money to unsecured creditors will, according to the external administrators' reports, return nothing to those creditors through the administration process.

Table 4 – Amount Payable to Unsecured Creditors – Cents in the Dollar Dividend – Construction Industry (1 July 2013-30 June 2014)¹⁰

Cents in the Dollar Dividend	Number of Reports	% of Total Reports for the Construction Industry
0 cents	1974	91.7
Greater than 0 but less	104	4.8
11 – 20 cents	32	1.5
21 – 50 cents	23	1.1
51 – 100 cents	20	0.9
Total	2153	100

Unpaid Employee Entitlements

Employees are a particularly vulnerable category of creditor in the event of corporate failure. Unlike other creditors, they are not able to spread the risk by diversifying their exposure across a range of businesses. Nor are they able to obtain a security over their accumulated entitlements¹¹. If their employer collapses, it can mean the loss of entitlements built up over many years. This includes amounts such as superannuation, which should have been paid to a superannuation fund periodically and prior to the collapse. Because of this exposure and the particular hardship that employees can suffer in insolvency situations, they are ranked as priority unsecured creditors, though this priority is only valuable where there are funds available to meet their claims.

A few key points relating to employee entitlements can be drawn from an analysis of the 2013-14 data:

- In relation to all categories of unpaid employee entitlements and across all ranges of amounts owing, the construction industry consistently rates as either the highest or second highest as against all other industries.
- About 19% of all construction company administrators' reports reported on unpaid wages (22% for annual leave, 14% for pay in lieu of notice, 11% redundancy, 9% for long service leave and 37% for superannuation)

⁹ Report 412 ASIC Insolvency Statistics: External administrators' reports (July 2013 to June 2014).

¹⁰ Ibid

¹¹ *The Protection of Employee Entitlements in Insolvency: an Australian Perspective* H. Anderson MUP 2014

- On the basis of the shortfalls in employee entitlements identified in administrators' initial reports set out in Table 5 on page 11, and taking the lowest possible figure at each of the ranges described, it can be estimated that at an absolute minimum, employees in the construction industry were owed almost \$57 million in entitlements by insolvent companies in the 2013–14 year [Table 6 on page 12].
- More realistically, if the median amount in each range is used, the figure for employee entitlements jumps to almost \$137 million for that single year [Table 6].
- Unpaid superannuation stands out amongst all the entitlements as the most significant loss for employees in dollar terms [Table 6].
- The outstanding amounts for superannuation and redundancy is of particular concern given that the industry superannuation and redundancy schemes that operate in the construction sector generally require regular monthly contributions. For industries which have quarterly superannuation contributions and no portable redundancy funds, it would be expected that these entitlements might be lost for even longer periods of service.

CASE STUDY:

Q Structures Pty Ltd

Q Structures [formerly Quality Structures Pty Ltd, formerly Adelaide Precast Pty Ltd] was one of a group of Adelaide related family companies [the MWS group] operating in the construction industry. The head of the company group was Mr. P Maione.

In approximately July 2013, without notice to its employees, Q Structures closed its doors overnight leaving approximately 32 employees and various suppliers, and subcontractors unpaid.

The employees and the CFMEU tried unsuccessfully over a number of weeks to contact Maione to discuss the employees' outstanding entitlements. Eventually the union commenced proceedings in the Industrial Relations Court of South Australia against the company and Maione to recover the unpaid entitlements of over \$560,000. These entitlements included unpaid wages, wages in lieu of notice, annual leave, long service leave, redundancy and superannuation.

One of those employees, Mr S, was a long term employee with some 8 to 9 years of service and was owed tens of thousands of dollars. Another employee, who was making salary sacrifice contributions to his superannuation account, found out that although the amounts of some \$8000 were being deducted, they had never been paid by the employer to the superannuation scheme.

On 9 September the Court made orders in favour of all of the employees against the company which was represented but did not oppose the making of the orders. Later that month, the company was formerly placed into liquidation. Proceedings against the company were stayed.

By February 2014 Maione was declared bankrupt and although the CFMEU continued to argue for penalties against Maione personally for his role in the underpayments, his lawyers argued that all legal action be discontinued.

About a year after the original closure the employees, with the assistance of the CFMEU, recovered a large percentage of their outstanding entitlements through the FEG scheme. It is understood that many of the suppliers and subcontractors received only a few cents in the dollar through the liquidation process.

Another Insolvent Company – or Two:

In May 2013, another Maione company, Ferro Con [SA] Pty Ltd, was fined \$200,000 for the failure to provide a safe workplace on the Adelaide desalination plant which resulted in the death of a 35 year old rigger, Brett Fitch and a near miss for another worker, in July 2010. Maione personally was also fined \$200,000 for his failure to take reasonable steps to ensure the company complied with its safety obligations.

CASE STUDY: continued

The Scale and Incidence of Insolvency in the Construction Industry

CASE STUDY: continued

Ferro Con was placed into liquidation prior to the penalties being imposed, as were two other MWS (Maione) companies, MWS Coatings and Maione Enterprises. However Ferro Con had in place an insurance policy which indemnified it and its directors for fines imposed for criminal conduct. Because the company was in liquidation and had no assets, it could not pay the \$10,000 excess on the policy. Maione paid it personally and thereby avoided the consequences of the monetary penalty imposed by the court. In sentencing, the Court said:

*'In my opinion Mr Maione's actions are so contrary to a genuine acceptance of the legal consequences of his criminal offending that they dramatically outweigh the benefits to the justice system of the early guilty plea and statement of remorse.'*¹²

Table 5 - Initial External Administrators Reports Unpaid Employee Entitlements 1 July 2013 – 30 June 2014
Construction Industry

Employee Entitlements											
Wages	\$1-\$1,000	\$1,001 - \$10,000	\$10,001 - \$50,000	\$50,001 - \$150,000	\$150,001 - \$250,000	\$250,001 - \$500,000	\$500,001 - less than \$1.5m	\$1.5m - \$5m	Over \$5m	Not Applicable	No. of reports
Construction	61	178	116	31	10	4	2	0	0	1,748	2,150
Total [all industries]	287	875	468	148	32	23	9	2	1	7,591	9,436
Annual Leave	\$1-\$1,000	\$1,001 - \$10,000	\$10,001 - \$50,000	\$50,001 - \$150,000	\$150,001 - \$250,000	\$250,001 - \$500,000	\$500,001 - less than \$1.5m	\$1.5m - \$5m	Over \$5m	Not Applicable	No. of reports
Construction	54	171	161	62	18	6	1	0	1	1,676	2,150
Total [all industries]	201	851	706	306	62	35	12	6	1	7,256	9,436
Pay in Lieu of Notice	\$1-\$1,000	\$1,001 - \$10,000	\$10,001 - \$50,000	\$50,001 - \$150,000	\$150,001 - \$250,000	\$250,001 - \$500,000	\$500,001 - less than \$1.5m	\$1.5m - \$5m	Over \$5m	Not Applicable	No. of reports
Construction	46	90	105	36	11	3	1	0	0	1,858	2,150
Total [all industries]	176	415	445	168	41	19	15	1	2	8,154	9,436
Redundancy	\$1-\$1,000	\$1,001 - \$10,000	\$10,001 - \$50,000	\$50,001 - \$150,000	\$150,001 - \$250,000	\$250,001 - \$500,000	\$500,001 - less than \$1.5m	\$1.5m - \$5m	Over \$5m	Not Applicable	No. of reports
Construction	41	53	61	48	23	11	1	1	0	1,911	2,150
Total [all industries]	135	162	261	201	76	54	24	5	9	8,509	9,436
LSL	\$1-\$1,000	\$1,001 - \$10,000	\$10,001 - \$50,000	\$50,001 - \$150,000	\$150,001 - \$250,000	\$250,001 - \$500,000	\$500,001 - less than \$1.5m	\$1.5m - \$5m	Over \$5m	Not Applicable	No. of reports
Construction	43	58	60	23	3	4	1	0	1	1,957	2,150
Total [all industries]	144	224	340	152	27	20	4	3	3	8,519	9
Superannuation	\$1-\$100,000	\$100,001 - \$250,000	\$250,001 - \$1m	Over 1m	Not Applicable	No. of Reports					
Construction	707	72	20	3	1,351	2,153					
Total [all industries]	3,368	400	148	17	5,526	9,459					

Source: ASIC Report 412 op cit

¹² <http://www.austlii.edu.au/cgi0-bin/sinodisp/au/cases/sa/SAIR/2003/22.html?stem=0&synonyms=0&query=maione>

The Scale and Incidence of Insolvency in the Construction Industry

**Table 6 – Unpaid Employee Entitlements –
1 July 2013 – 30 June 2014 Construction Industry**

	Minimum Amount Owed \$ Million	Median Amounts Owed \$ Million
Wages	6.4	12.4
Annual leave	9.6	18.0
Pay in Lieu	5.8	11.0
Redundancy	11.2	19.6
Long Service Leave	8.8	12.2
Superannuation	15.2	63.5
Totals	56.9	136.6

Source: ASIC Report 412 op cit

Secured Creditors

Secured creditors are less likely to feature in construction industry insolvencies. Over two-thirds of insolvent companies in the construction industry are not indebted to secured creditors at the time of the insolvency.

**Table 7: Amount owed to Secured Creditors
Construction Industry (1 July 2013-30 June 2014)**

Amount Owed	Number of Reports	% of Total Reports for the Construction Industry
\$0	1457	67.7
\$1 – less than \$500,000	436	20.3
\$500,000 – less than \$1 million	77	3.5
\$1 million – less than \$5 million	101	4.7
\$5 million – \$10 million	28	1.3
Over \$10 million	54	2.5
Total	2153	100

Source: ASIC Report 412 op cit

Cost to Public Revenue

It is not only private businesses and employees in the private sector who lose out through corporate insolvencies. Government revenue loses hundreds of

millions of dollars each year from the construction industry alone through the unremitted taxes of insolvent companies. These include unpaid PAYG tax and state payroll tax.

In many cases, when companies start to get into financial difficulties, the remittances to taxation authorities are often the first payments that cease to be made. In other situations, companies deliberately trade without making the necessary remittances until their indebtedness reaches a certain level or attracts the attention of these authorities, at which point they are voluntarily wound up.

**Table 8 - Amount owed in Unpaid Taxes and Charges –
Construction Industry – (1 July 2013-30 June 2014)**

Amount Owed	Number of Reports	% of Total Reports for the Construction Industry	Estimated Total Debt (Minimum) \$ Million	Estimated Total Debt (Median) \$ Million
\$0	303	14.1	0	0
\$1 – \$250,000	1404	65.2	0	176
\$250,000 – \$1m	358	16.6	90	224
Over \$1m	88	4.1	88	88
Total	2153	100	178	487

Source: ASIC Report 412 op cit

A 2009 Commonwealth Government paper put the estimate of lost tax revenue alone at \$600 million per annum.¹³ Anderson et al point out that taxpayers lose out because suppliers' bad debts are also tax deductible.

The Tax-payer Safety Net

It is not merely lost taxation remittances that result in losses to public revenue. The cost to the Australian taxpayer of the various iterations of Government safety net schemes (EESS, GEERS and FEG) since their establishment in 2000 has been (for all industries) in the order of \$1.3 billion of which just \$180 million (or 14%) has been recovered through the liquidation process. These costs have risen from a modest \$7 million in 2000-01 to over \$261 million for 2012-13.¹⁴

¹³ Commonwealth of Australia, 'Action Against Fraudulent Phoenix Activity Proposals Paper' [2009 Phoenix Proposals Paper], [2]. Available at http://archive.treasury.gov.au/documents/1647/PDF/Phoenix_Proposal_Paper.pdf, Quoted in 'Business Set-up, Transfer and Closure Productivity Commission Issues Paper December 2014'

Submission by Associate Professor Helen Anderson, Professors Ian Ramsay and Ann O'Connell, Melbourne Law School, and Associate Professor Michelle Welsh, Department of Business Law and Taxation, Monash University. 11 February 2015, page 3.

¹⁴ Anderson' op cit pages 42-43

The Scale and Incidence of Insolvency in the Construction Industry

The 2012 PwC report on phoenix companies commissioned by the Fair Work Ombudsman noted that the pay-outs to employees of insolvent companies through the GEERS scheme (now FEG) should also be factored in in determining the net impact on government revenue. The report concluded that for 2009, the total exposure of government revenue to phoenixing alone, but across all industries, including GEERS payouts, ranged between a lower bound estimate of \$600,770,293 to an upper bound figure of \$610,553,018.

Total Deficiency

The total shortfall between the estimated assets and estimated liabilities for insolvent companies in the construction industry for 2013-14 is set out in Table 9 at right.

Whilst 45.6% of these companies recorded a deficiency of \$250,000 or less, a staggering 67 companies had a deficiency of more than \$10 million in that year. This was the highest figure for any industry category. Indeed the construction industry outscored all other industries for each category of deficiency above \$500,000.

Table 9 shows that at the most conservative possible estimate, that is, taking the lowest dollar figure from each deficiency category, insolvent construction industry companies had a total shortfall of \$1.625 billion for their creditors in the 2013-14 financial year. A more realistic estimate for the year, based on median figures, puts the amount at an astonishing \$2.72 billion (in round figures).

In dollar terms, there is clearly a concentration in the deficiency of liabilities over assets at the range of \$500,000 and above (90.7% of total value of the deficiency), even though the number of companies reporting deficiencies in this range (37.1%) is much smaller than those in the less than \$500,000 range (62.9%). In other words, the figures support the notion that large scale indebtedness amongst larger operators (principal contractors) has flow-on consequences for a much larger number of small operators (subcontractors) who then themselves become insolvent because they have lost money to those higher up the chain.

Table 9 - Amount of Deficiency - Construction Industry - (1 July 2013 to 30 June 2014)

Deficiency Categories	Number of Reports	% of Total Reports for Construction Industry	Estimated Total Deficiency (Minimum) \$ Million	Estimated Total Debt (Median) \$ Million
\$0 - \$50,000	280	13%	-	7
\$50,001 - \$250,000	701	32.6%	35	105
\$250,001 - less than \$500,000	373	17.3%	93	140
\$500,000 - less than \$1 million	299	13.9%	150	224
\$1 million - less than \$5 million	372	17.3%	372	1,116
\$5 million - \$10 million	61	2.8%	305	457
Over \$10 million	67	3.1%	670	670*
Total	2,153	100%	1,625	2,720

Source: ASIC Report 412 op cit

* No median figure for this category. Lowest figure within the range has been used.

3. THE ECONOMIC AND SOCIAL EFFECTS OF INSOLVENCIES

If we are all “six missed meals from anarchy”, as someone once said, then the construction industry is two missed progress payments from insolvency.¹⁵

Some Case Studies

CASE STUDY:

ACT – The Payment Problem

A small bricklaying contractor E Bricklaying Services, employs approximately ten employees and contracts to perform bricklaying work on a commercial site for a medium sized builder in the ACT. Work commences in August 2012 on a ‘schedule of rates’ basis. Under the contract, invoices from the subcontractor are to be submitted by the 25th of each month and payment is required 45 days later, i.e. on or about the 10th of the second month after the invoice date.

From the commencement of the job, payments to the bricklaying contractor are late. In some cases payment is not received until 90 days after the invoice is provided. The quality of the work is not disputed by the builder. When payment is finally received the cheques are all dated the 10th of the month irrespective of when they are actually provided.

The bricklaying contractor manages to deal with delayed payments through cash flow from other projects but the delay places great pressure on the business’s finances. Eventually the bricklayer refuses to perform further work at the site until payment for the last invoice is brought up to date. The builder disputes the invoice valued at approximately \$80,000 and in August 2014 terminates the contract of the bricklayer relying on a contractual term allowing termination at the convenience of the builder. The bricklayer commences ‘security of payment’ processes to recover the outstanding amount. That process is ongoing as at the date of this submission.

A further \$80,000 is held as retention by the builder [usually 5% – 10% of the contract price]. Fifty per cent of this amount is meant to be provided on practical completion and a further 50% one year later at the expiry of the defects liability period. The bricklaying contractor expects this will also be disputed by the builder. The business has suffered financial hardship because of the amounts owed.

Other subcontractors on the project experience similar problems. Only one of the original subcontractors remains on the project which is 18 months behind schedule.

The bricklaying contractor supports the introduction of a trust fund system into the industry.

‘At least we know the money is there. At the moment builders are using our money to fund their lifestyle. With a trust, if a builder goes broke, it is their problem, not ours.’

The bricklaying contractor is willing and available to appear before this inquiry on a confidential basis.

¹⁵ Duncan Glaholt quoted in Collins Report page 157.



CASE STUDY:

Federal Government Project Canberra ACT

A medium-sized earthmoving and civil contractor employed approximately sixty employees and had an annual turnover of \$10 million. The company contracted for a \$1.2 million package of work from a large, well established civil contractor (Y Contractors) who is in turn contracted to a major construction company on a significant Federal Government funded project in Canberra.

Y Contractors becomes embroiled in major contractual disputes with the head contractor. Despite the fact that it is a large company with management expertise and 30 years' experience, it is unable to secure a regular flow of payments to Y from the head contractor.

Payments from Y to the earthmoving contractor dry up. Eventually the earthmoving company claims around \$700,000 from Y for unpaid work which is adjudicated in its favour. An agreement is reached in September 2012 whereby amounts will be repaid by Y in instalments. One week after this agreement, Y enters into voluntary administration and the payments are frozen. The earthmoving company continues to trade with severe difficulty until March 2013 by relying on other projects. Y also trades on for a period but is eventually placed into liquidation owing creditors around \$10 million.

The banks ultimately withdraw financial support from the earthmoving business and its principal who had provided personal guarantees to underwrite the company's operations. The company collapses. The principal is declared bankrupt, loses his house and his ability to obtain finance. He says:

'The culture on this job was – "How can we catch these subcontractors out? How can we find a way to dispute and delay their payment?'"

The major builders have got the resources to outlast even the largest subcontractors and they know it. Instead of fostering cooperation, they create problems and make it more difficult for subbies. This isn't in the interest of the project or the client. Only the builders win out of it.'

This contractor does not wish to be identified because of the personal toll the experience has taken on him and his family.

CASE STUDY:

Victoria

A Victorian bricklaying contractor has worked in the commercial construction industry for over 25 years. The business employs approximately 20 workers and prides itself on its reputation for quality work. The company won a contract for the masonry package at the Ararat Prison project in regional Victoria. The head contractor was St Hilliers.

The job proceeds without problems until everyone on site is told that the payments would stop as the company is placed into external administration. Around 250-300 employees, including many from the economically depressed local area, are suddenly without work. The contractor meets with other subcontractors. It is estimated that over \$20 million is owed to the various contractors and suppliers.

Months pass without any payments. Eventually the head contractor is placed into liquidation. A number of subcontractors are also wound up. Ultimately a number of banks arrange for finance to complete the job. A new head contractor is appointed and the bricklayer returns with a minimum crew to complete the work. Some but not all of the outstanding money is paid.

The contractor says:

'I've seen two other collapses recently. I've seen people lose their life savings, people in tears at meetings. On one job the money stopped and the owners of the building company disappeared. They couldn't be contacted on the office or mobile phones. Eventually I went to the office and was greeted by a bouncer at the door who turned me away. I put in a security of payment claim but it was too late, the company had gone under.'

The contractor has been a spokesperson for other subcontractors who have been affected by insolvencies and is willing to attend before the Committee.





CASE STUDY:

CTR Pacific Brick and Blocklayers

CTR was a brick/block laying business established in the early 1990s in the ACT. One of its co-directors was Mr. O'Sullivan. The company at various times employed between 30 and 80 employees, including apprentices.

Mr O'Sullivan says the effects of insolvency in the industry have been getting progressively worse since his business was established. Delay in payments became commonplace around 2000 at which time there was no security of payments legislation which could be relied on by small contractors. Delayed, disputed or straight out non-payment can send many small contractors to the wall. Many construction industry insolvencies have resulted in no, or very limited, returns to creditors.

The global financial crisis brought on a lot of payment disputes as a result of solvency issues throughout the industry. Many of the major builders also followed the example of mid-tier builders by extending payment periods in the standard terms of their contracts. Mr O'Sullivan was told by one senior manager that some of his company's jobs were deliberately priced with little or no margin but with an eye to keeping turnover high and holding the payments to subcontractors for 60 days. That way the money could be placed on the short term money market where the company made more money with less risk. The company in question was placed into voluntary administration in 2012.

Mr O'Sullivan can cite numerous examples of the effects of insolvencies and delayed or non-payment from his personal experience in the industry. He says there is an urgent need to take insolvencies and disputes about payment off the table and focus on the job outcome and training. He says the most effective means of achieving this would be through a mandatory trust scheme from which payments are disbursed coupled with a modified security of payments regime which includes a rapid adjudication process, and licensing for all trades.

Mr O'Sullivan is also currently the president of the Masonry Contractors Association of NSW and the ACT and says virtually every member of his association has been personally affected by these issues. He says he has dozens of members who are willing to attend a Senate Committee hearing and describe their experience.

4. THE INCIDENCE OF 'PHOENIX COMPANIES' IN THE CONSTRUCTION INDUSTRY, THEIR EFFECTS AND ADEQUACY OF EXISTING LAW

A particularly concerning species of corporate insolvency in the construction industry involves the use of 'phoenix companies.'

What is 'Phoenixing'?

Phoenix activity has been variously defined by a range of different authorities and in the course of numerous public inquiries.¹⁶ The essential elements are not disputed and can be summarised as involving, cumulatively:

- the use of the corporate form in the operation of a business;
- the accumulation of debts by [a] company/ies in the course of trading, including outstanding taxation remittances and accumulated employee entitlements;
- the deliberate failure of the company by those individuals in charge with the intention of denying creditors the amounts owing to them; and
- the continuation or re-emergence of the business by the individuals behind the failed entity through a separate/new corporate entity.

The ATO points to a number of indicators that suggest phoenix activity by a new business. These include that the directors of the new entity are family members or close associates of the director of the former company, a similar trading name is used by the new entity and the same business premises and telephone number (particularly mobile number) are used by the new entity.¹⁷ However it should be borne in mind that setting up multiple or successive company structures, even where one or more of these companies fails, does not necessarily involve illegal phoenix activity. It is the deliberate use of multiple corporate entities to avoid creditors which is the essence of the practice of phoenixing.

A typical phoenix company will collapse owing unremitted group tax, state payroll tax, superannuation contributions and workers compensation premiums. These payments are only required periodically and default or delay in payment

is often not acted on immediately by those who are owed the money.

The phoenix phenomenon is not confined to the construction industry, though the industry is notorious for the widespread use of phoenix companies and some of the most flagrant examples of the practice. The Cole Royal Commission noted that the construction industry had a number of characteristics – project based work, competitive pressures, cash flow problems, lack of administrative skills and the limited asset base of contractors – which made it particularly vulnerable to phoenix activity.¹⁸

Phoenixing in Australia

The lack of any statutory definition or even any specifically designed statutory provisions directed to phoenix activity poses some challenges in determining its full extent and cost as well as the effectiveness of existing regulation and enforcement mechanisms. Legally, phoenix activity is generally dealt with in the broader context of breaches of director's duties and insolvent trading provided for in the *Corporations Act 2001* (Cth) though these types of prosecutions are limited. Similarly, as Anderson et al point out, disqualification of directors associated with phoenix-like behaviour also seem somewhat of a rarity.

A search of ASIC's media releases for the years January 2004 - August 2014 reveals that only 49 directors were disqualified by the regulator under s 206F during this period where the media release specifically mentions the term 'phoenix activity' (21 directors) or else implies illegal or problematic phoenix activity (28 directors). None of these ASIC media releases reveal any applications by ASIC to the court requesting it to disqualify a director pursuant to s 206D for engaging in behaviour that could be described as illegal phoenix activity. In fact, this enforcement mechanism appears to be rarely used. A search of the Austlii database disclosed only one case issued by ASIC pursuant to this section during this entire period and the events that gave rise to that application do not appear to involve illegal phoenix activity: See ASIC

¹⁶ See for example Cole Royal Commission Final Report Volume 8 page 113 which refers to a definition used by the Victorian Law Reform Commission or PwC Report June 2012 page ii. See also N Couburn, 'The Phoenix Re-examined' [1998] 8 AJCL 321 at 322 where a phoenix company is described as a limited liability company 'housing individuals, or the directors by name or otherwise, who abuse the corporate form by dissolving one company and creating another to avoid the payment of debt.'

¹⁷ <https://www.ato.gov.au/General/The-fight-against-tax-crime/Our-focus/Fraudulent--phoenix--activities/>

¹⁸ Final Report Volume 8 page 133.

v Elm Financial Services Pty Ltd [2005] NSWSC 1065 [21 October 2005], [2005] NSWSC 1033 [13 October 2005], [2005] NSWSC 1020.¹⁹

Section 596AB of the *Corporations Act* which prohibits agreements or transactions entered into with an intention to prevent the recovery of employee entitlements, has not been successfully relied upon since it was introduced in 2000.²⁰ More will be said about that below.

PwC Report

In 2012 PwC delivered a report (*Phoenix Activity – Sizing the Problem and Matching Solutions* PwC 2012) to the Fair Work Ombudsman on the incidence and costs of phoenix activity across the Australian economy. The report concluded that the total impact of phoenix activity to be between \$1.78 billion and \$3.19 billion per annum (see Table 10).

Table 10: Costs of Phoenixing

	Lower Estimate \$ million	Upper Estimate \$ million
Cost to employees	191	655
Cost to business	992	1,925
Cost to government revenue	601	611
Total impact	1,784	3,191

Importantly, these quantified costs are not an exhaustive assessment since the report also noted:

A range of impacts of phoenix activity on employees (such as superannuation), businesses (such as unfair advantage) and government (such as monitoring and enforcement costs) and the environment (such as avoidance of regulatory obligations) have not been included in the modelling.²¹

According to these figures, the cost of phoenixing to employees is in the order of 10% to 20% of the total cost. Given that lost superannuation is excluded from these figures and knowing the extent to which unpaid superannuation features in the unpaid employee

entitlements of insolvent companies in the construction industry (see Table 5 above), it could reasonably be assumed that the actual percentage for employees is much higher.

The figures published in the same report show that the cost borne by employees in the construction industry represents between 55% to 60% of the total costs to employees across all of the industries analysed.

Table 11 - Phoenixing – Cost to Employees

	Lower Estimate \$ million	Building and Construction Industry Percentage of Total	Upper Estimate \$ million	Building and Construction Industry Percentage of Total
Building and Construction Industry	105	55%	395	60%
Combined Industries Total	191		655	

22

In 2003 the Cole Commission reported that the ATO had finalised 400 investigations into phoenixing since 1998, 85% of which related to the construction industry. These investigations had raised \$140 million in taxes and penalties of which \$126 million came from NSW and \$110 million (or 79%), was from the construction industry.²³ At that stage, ASIC appeared less active. In 2001-02 it had commenced only five phoenix investigations compared with 150 by the ATO.

A number of Commonwealth Government agencies, including the ATO and ASIC have now combined to form an Inter-Agency Phoenix Taskforce to focus on phoenix activity across all industries. That Forum has now been declared a prescribed taskforce by the Federal Government allowing for a freer flow of information between its constituent members.²⁴ Membership of that body includes the AFP and ACC because as Anderson et al note, phoenixing can also be linked to money laundering, tax fraud, fictitious transactions, abuse of migrant labour and other criminal behaviour.²⁵

¹⁹ *Business Set-up, Transfer and Closure: Productivity Commission Issues Paper* December 2014, Submission by Associate Professor Helen Anderson, Professors Ian Ramsay and Ann O'Connell, Melbourne Law School, and Associate Professor Michelle Welsh, Department of Business Law and Taxation, Monash University, 11 February 2015

²⁰ *The Protection of Employee Entitlements in Insolvency – An Australian Perspective* Anderson page 2.

²¹ Page iii.

²² Summarised form PwC Report pages 19-20.

²³ Vol 8 page 127. For each \$1 spent by the ATO on phoenix activity in 2001-02, \$8 in revenue was raised. Vol 8 page 140.

²⁴ Anderson et al pg 4.

²⁵ Ibid

The Phoenix Continues to Rise in the Construction Industry

The Cole Royal Commission cited a number of variations on the phoenix theme in the construction industry which were referred to that inquiry by the CFMEU. These included the 'one after another' model and the 'labour hire' model.²⁶ This latter model generally involves a group of companies, one of which is virtually assetless and which employs the workers and another which holds assets, receives income from the trading activities of the group and which provides just enough income to the employing entity to cover wages.

CASE STUDY:

Walton Constructions (Qld) Pty Ltd

Walton Constructions collapsed without notice in late 2013. A small regional masonry company was engaged on a project for Walton on a commercial project in North Queensland. They were owed in excess of \$250,000 by Walton for outstanding progress payments and retention at the time of the collapse. They had to immediately lay off nine of their twenty two employees. It is estimated that there was in the order of \$70 million outstanding across a number of Walton projects in Queensland and Victoria. Almost immediately after the collapse, new entities with links to Walton began operating.²⁸ These entities traded for a few months before themselves being placed into administration.

The contractor, who remains unpaid, says:

'In the last few months before the collapse we were asked to work harder and faster. We did that and there were never any complaints about our work. We even paid for some of Waltons' materials towards the end, at their request. Those things make it even harder to accept on top of the money that we are owed for the work.'

It is very hard for a small company to take this sort of loss. It was hard putting off some of our workers. They are all breadwinners and when they lose their jobs there are nine families in our area that are affected. We saw one other contractor lose everything – his business, his marriage. In the end he was sleeping in his car.

One of the worse things is knowing there was nothing we could have done differently to avoid this and thinking that it could happen all over again.'

In 2014 media reports said that a property trust linked to the LNP received \$430,000 in rent from Walton Construction in the last financial year at a time when it was about to collapse. According to these reports the 'rent' paid by Walton to the LNP entity varied substantially from year to year.

In 2009-10 the AEC was informed \$105,994 had been received from Walton. In 2010-11 the amount was \$353,315, in 2011-12 it was \$516,966, and in 2012-13, \$431,082.

The 2010-11 payment was initially declared as \$211,988.94 but was amended on May 27, 2013, to the amount above.²⁹

CASE STUDY: continued

²⁶ Vol 8 page 116-117

²⁷ Note however the ASIC submission to Cole that its statistical data did not support a conclusion that phoenix company activity was a significant issue. Volume 8 page 130.

²⁸ <http://www.abc.net.au/news/2014-05-05/how-the-walton-collapse-happened/5429396>

²⁹ <http://www.sunshinecoastdaily.com.au/news/Bankrupt-builder-Walton-still-donated-430000-toLNP/2164311/>

CASE STUDY: continued

The reports quoted the liquidator as telling creditors that the company had been trading insolvent from as early as 1 July 2012.

A subsequent report stated that the trust which is described as a 'fundraising arm of the LNP', subsequently made significant amendments to its AEC return.

The amendments add \$1.9 million received from the LNP to the total receipts received by the property trust, increases total payments from \$104,000 to \$3 million and reduces total debt from \$100,794,170 to \$10,204,901.

They also show Altum creditors as the Liberal National Party which is owed \$1,887,251 [down from \$2,049,665 in the original return] and LNP Nominees as Trustee for the 6 St Paul's Terrace Trust, which is owed more than \$8 million where the original showed no debt.³⁰

CASE STUDY:

Melbourne Transit

In the matter of *Cahill v CFMEU and Mates*³¹ the ABCC brought proceedings alleging that the CFMEU and an official had unlawfully coerced an employer to engage certain employees, including OH&S officers, on a site in Heidelberg Victoria and had engaged in unlawful industrial action for the purpose of preventing a crane company from working at the site. There was also evidence before the court suggesting that a number of sub contractors of Melbourne Transit had not been paid and it was these contractors who had picketed the site.

According to the Court, the evidence in the interlocutory proceedings showed that a company known as Transit Joint Venture Pty Ltd (TJV) had been engaged on the site since December 2003 and had employed construction workers on the site through another company, Melbourne Transit Pty Ltd (Melbourne Transit). The sole director of both companies was Mr. Anthony John Goss. From December 2005 Melbourne Transit began to make a number of employees redundant. A new company 117 918 064 Pty Ltd was incorporated on 17 January 2006, and in late January TJV contracted with that company predominantly for the supply of labour to the site. Goss was the sole director of that company.

In August 2006 Melbourne Transit was the subject of very strong criticism by the County Court of Victoria in relation to the workplace fatality of one of its employees that had occurred in September 2004. Judge Gaynor said:

I regard the defendant company's actions before and after this accident to be reprehensible in the extreme, involving a dismissive and careless approach to the safety of its employees, such that a young life was cut short by what was clearly an easily avoidable accident... In my view the company was seriously at fault and its moral culpability was high

A fine of \$100,000 was imposed even though the Court acknowledged that as the company was in receivership the fine would not be paid.

³⁰ <http://www.sunshinecoastdaily.com.au/news/LNP-fundraising-100m-altum-property-aec-walton/2247446/>

³¹ [2006] FCA 196

Personal Liability Measures

In 2012, new measures were introduced to extend the director penalty regime applying to unremitted PAYG withholding to unpaid superannuation guarantee contributions. Under these arrangements directors can become personally liable for a penalty equivalent to the unremitted superannuation contributions following the issuing of a penalty notice by the ATO.

The CFMEU supported these measures at the time of their introduction and during the public consultation

period, suggested amendments to tighten their operation. We continue to support such measures and note with interest the ATO submission to this Committee which indicates that some 1500 businesses in the industry have received these notices since the measure was introduced. In our view the Committee would benefit from further information from the ATO on the success or otherwise of these measures, including how much superannuation has been recovered through the penalty notice process.



5. THE IMPACT OF INSOLVENCY ON PRODUCTIVITY

When people go to a job and get paid and know that if the work is done properly there won't be a problem getting paid, they are usually passionate about producing quality work. But if you go onto a job where the guys are being mucked around on payment, morale suffers and so does quality. If the industry is to thrive and standards of workmanship are to be maintained, the security of payment problem has to be fixed.

Len Coyte – Senior Project Manager with over 30 years' industry experience.

As with insolvencies generally, an insolvency event in the construction industry results in a cessation of the insolvent company's operations - output ceases, orders for work and materials stop and employees' contracts of employment are brought to an end. Unfortunately though, because of the interconnectedness of the industry players, the project-based nature of the work and the hierarchical contracting system, the flow-on effects of insolvency in the construction industry can be compounded beyond those experienced elsewhere.

Needless to say, the insolvency of a head contractor usually brings an entire project to a halt.

Subcontractors and their employees who might otherwise be productively engaged in bringing a project to completion cease work and are often occupied for long periods in negotiations, in lieu of production, to try to secure payment for work undertaken to that point.

Subcontractors are often unable or unwilling to walk away from a project where the head contractor has collapsed until payment arrangements are in place. For example, subcontractors stayed on for many weeks at the various Steve Nolan sites in NSW in an attempt to obtain commitments for payment.

For clients, a head contractor insolvency can mean losses in various forms. Firstly, the insolvent company may not have passed payments on to subcontractors before they became insolvent. This can result in claims by subcontractors against clients for work which they have performed and which the client has the benefit of but for which they have already paid. Secondly, there is an inevitable cost in the process of finding a suitable replacement contractor. Delay to the project's completion date can mean capital tied up in the project is left idle, or finance capital incurs interest charges, or returns from the realisation of the completed project remain unfulfilled.

Lost productivity can also result on projects unrelated to the project on which the original insolvency event occurred. If a subcontractor such as a crane hire company is affected by a collapse on Project A, this can bring its operations on Projects B, C and D to a halt, which in turn can delay those latter projects because of the critical role crane operations can play in the sequential construction process.

Delayed payment, often a precursor to insolvency, also has a negative effect on productivity. Because insolvencies are so common in the construction industry many take a poor payment record as an indicator that a more serious financial crisis is inevitable. Employees whose own employers are unable to meet commitments to wages and entitlements on a regular basis because of difficulties in extracting progress payments, are unlikely to feel engaged in the process of making the project a success.

Whilst the official figures show that the vast majority of companies for which initial external administrator's reports are lodged are smaller enterprises in terms of employee numbers - [80.6% of such companies across all industries have fewer than 20 employees] - given the sheer number of insolvency events in the construction industry (2,153 or 22.8% of the total for 2013-14), there can be little doubt that given the number of employees and businesses affected, insolvency has a major impact on industry productivity,³² though we do not attempt to quantify that loss in this submission.

³² ASIC Report 412 page 17.

6. THE INCIDENCE AND NATURE OF CIVIL AND CRIMINAL MISCONDUCT RELATED TO INSOLVENCIES

Whilst many corporate contraventions may never come to the attention of the regulator, an insolvency event triggers a requirement that an external administrator prepare a report for ASIC about any potential unlawful act which they become aware of.

The 2013-14 ASIC Insolvency Report 412 sets out the details of possible civil and criminal misconduct based on details provided in those initial reports by external administrators. In that year, external administrators alleged some form of misconduct in 7,218 (or 76.3%) of all reports lodged. An average of between two and three breaches was reported in each case where alleged misconduct was identified.

The alleged misconduct across all industries is broken down into possible civil and criminal contraventions. Of all these allegations, 76.6% involved potential breaches of civil obligations. Criminal misconduct under the Corporations Act was said to have occurred after the appointment of the external administrator in 15.6% of cases and pre-appointment in 6.6% of cases. Ultimately ASIC required 802 supplementary reports from external administrators in relation to the alleged misconduct but no figures are provided in the Report as to the number of prosecutions arising out of the administrator reports. Since 2012, prosecution information has been separately published in ASIC 'Enforcement Reports' (see below).

Construction Industry Misconduct

According to the latest ASIC insolvency report, the top three potential criminal contraventions consistently nominated by the external administrator's reports over the past five financial years are:

- (i) Insolvent trading – s. 588G[3]
- (ii) Obligation to keep financial records – ss. 286 and 344[2]; and
- (iii) Good faith, use of position and information – s. 184.

The same report lists as the top three potential civil contraventions consistently nominated by the external administrator's reports over the past four financial years as being:

- (iv) Insolvent trading – s. 588G[1]-[2]
- (v) Obligation to keep financial records – ss. 286 and 344[1]; and
- (vi) Care and diligence, directors and officer's duties – s 180.

By number of potential contraventions in each category, the construction industry ranks as the highest or second highest of all industries for 2013-14 and has the second highest overall total for that year in terms of both civil and criminal contraventions.

Table 12 – Possible Breaches of Civil Obligations by section of the Corporations Act July 2013 – June 2014

Section of Corporations Act	Construction Industry	Total All Industries	Construction Industry Percentage of Total
Section 180 Care and diligence – Directors' and officers' duties	507	2542	19.9
Section 181 Good faith – Directors' and officers' duties	280	1302	21.5
Section 182 Use of position – Directors, officers' and employees' duties	196	900	21.7
Section 183 Use of information – Directors, officers' and employees' duties	73	295	24.7
Section 286 and 344[1] Obligation to keep financial records	782	3486	22.4
Section 588[1]-[2] Insolvent trading	1220	5425	22.4
Total for industry	3058	13950	21.9

Table 13 - Possible Pre-Appointment Criminal Misconduct by section of Corporations Act July 2013 – June 2014

Section of Corporations Act	Construction Industry	Total All Industries	Construction Industry Percentage of Total
Section 184 Good faith, use of position and use of information – Directors' officers' and employees' duties	42	255	16.4
Section 206A Disqualified persons not to manage corporations	10	36	27.7
Section 286 and 344(2) Obligation to keep financial records	48	333	14.4
Section 471A Powers of other officers suspended during the winding up	4	26	15.3
Section 588G(3) Insolvent trading	75	381	19.6
Section 590 Offences by officers or employees	25	116	21.5
Section 596AB Agreements to avoid employee entitlements	1	5	20
Other criminal offences under the Corporations Act	12	47	25.5
Total for Industry	247	1199	20.6

Prosecutions

ASIC has an extremely broad oversight role as the national corporate, markets and financial services regulator. Its enforcement role is central to ensuring that legal compliance is maintained across the entire commercial spectrum and for this reason it must be

clear, in the words of the recent report of the Senate Economics References Committee, *'that ASIC has the necessary enforcement tools and resources and is ready to use them to uphold accepted standards of conduct and the integrity of the markets.'*³³

The most recent ASIC report on enforcement outcomes³⁴ disclosed that in the six month period to December 2014, ASIC achieved a total of 348 'enforcement outcomes'.³⁵ Of these, 172 involved an outcome for a criminal matter under the small business compliance and deterrence heading of 'action against directors'.

ASIC also commenced 94 investigations, completed 94 investigations, charged 14 individuals with 174 offences and disqualified a total of 16 company directors.

In that same period the report shows that there was not a single enforcement outcome achieved under the heading 'insolvency'³⁶ and in fact only two such outcomes, neither of which involved criminal proceedings, are recorded under that heading for the full two year period January 2013 to December 2014.³⁷

The larger number of criminal prosecutions against directors under the 'Small business compliance and deterrence' category would, on the basis of previous reports on enforcement outcomes,³⁸ appear to reflect outcomes for what ASIC itself describes as 'technical' offences such as failure to keep proper books and records, for which penalties are often relatively light. The footnote that recorded this in previous reports does not appear in the 2014 report.

Whilst it can be readily accepted that no regulator will pursue, let alone bring to a successful conclusion, every alleged compliance issue that is brought to their attention, it is apparent from the above figures that enforcement outcomes for ASIC are very low compared to the number of matters identified as potential breaches, just in the insolvency area alone, by well-informed external administrators with access to company records.

³³ Performance of the Australian Securities and Investments Commission, Senate Economics References Committee, June 2014 – Executive Summary.

³⁴ Report 421 January 2015

³⁵ Defined to include any formal action taken to secure compliance about which ASIC has made a public announcement and 'small business compliance and deterrence' formal findings. This includes court determinations, administrative remedies, negotiated settlements, public warning notices and enforceable undertakings

³⁶ Although there is recorded 11 outcomes under the heading 'Corporate Governance – action against directors' and 172 criminal prosecutions against directors under the 'Small business compliance and deterrence' category.

³⁷ Although there is recorded 22 outcomes under the heading 'Corporate Governance – action against directors' and 749 criminal prosecutions against directors under the 'Small business compliance and deterrence' category.

³⁸ <http://download.asic.gov.au/media/2195189/rep299-published-11-september-2012.pdf>

The Scale and Incidence of Insolvency in the Construction Industry

The Senate Economics References Committee report observed that *'It would be unrealistic to expect that ASIC could be funded at a level where all breaches or allegations of misconduct were pursued.'* However in the May 2014 federal budget, ASIC's funding was cut by around \$120 million over a four year period. According to its annual reports, in the current financial year, ASIC will lose 12% cent (\$44 million) of its operating budget and 209 staff, which is in addition to the 59 already lost in the past year. ASIC concedes that it will also be forced to reduce levels of proactive surveillance.³⁹

All of this stands in very stark contrast to the Government's industrial watchdog in the construction industry, Fair Work Building and Construction.

According to its 2013-14 annual report, the FWBC conducted 406 investigations into suspected breaches of workplace laws. Of these, 327 were new investigations commenced during the financial year.

As at 30 June 2014, 283 investigations were finalised and 106 were ongoing. It also boasted that it had doubled the number of penalty proceedings from the previous year to 25. The report showed that it obtained court imposed penalties, overwhelmingly against unions and workers (62% for 'unlawful industrial action') of \$2,262,350. For its entire sphere of corporate responsibility and regulation, ASIC had obtained civil penalties of just over \$3 million for the six month period to December 2014.⁴⁰

The Federal Government also increased funding to the FWBC, which received an additional \$5 million from the Federal Government for the re-establishment of the ABCC.⁴¹ This increase in funding occurred even though the FWBC offloaded to the Fair Work Ombudsman the major function of recovery of unpaid employee entitlements, which when the current Director took over, made up over 40% of the agency's investigations.⁴²



³⁹ Annual Report 2012-13, ASIC, 10 October 2013 and Annual Report 2013-14, ASIC, 10 October 2014.

⁴⁰ Aggregate civil penalty figures for the January to June 2014 period are not included in the report for that period, though it does note two significant individual court-imposed penalties of \$1.2m on Newcrest Mining and \$1.5m on GE Capital Finance.

⁴¹ FWBC Annual report 2013-14

⁴² Ibid – Director's Foreword

7. THE EXTENT AND POTENTIAL FOR UNPAID DEBT TO ATTRACT NON-INDUSTRY PARTICIPANTS FOR THE PURPOSE OF DEBT COLLECTING AND THE EXTENT OF ANTI-SOCIAL/ UNLAWFUL CONDUCT RELATED TO DEBT COLLECTING.

For many years the CFMEU has assisted members in their efforts to recover lost monies caused through company insolvencies. This includes employee entitlements and outstanding payments for subcontractor members. Recent media reports have implied that the CFMEU has used 'non-industry participants', including motorcycle gang members, as industry debt collectors. A media story in 2014 which included CCTV footage of persons attending the private residence of a building industry participant and behaving in a threatening manner over a disputed debt was presented in a way that suggested that the CFMEU was somehow connected to this incident. It was not. Unfortunately, these allegations have been recycled in the media and by various politicians.

The CFMEU does not engage 'non-industry participants' for that purpose and does not condone anti-social or unlawful conduct relating to debt collecting. The CFMEU completely disavows such conduct. These matters should be reported to and dealt with by the police.

We have however witnessed the intense anger and frustration experienced by those who have carried out work and not been paid. We have seen long-term

employees lose thousands of dollars in accumulated entitlements, though this has been alleviated to some degree through the taxpayer-funded safety net schemes. A number of contractors have expressed their feelings of powerlessness to address obviously unjust situations. They say that the current mechanisms for recovery are ineffective, too slow or simply not worth the time and money required to see the matters through to the end. They say that larger contractors use their superior resources to deny payments knowing that they can simply outlast and outspend smaller businesses. In many company liquidations, there is simply no money available to creditors in any event and the amounts must be written off.

Unfortunately, for as long as the current system remains in place, there is a potential for unlawful conduct to arise in relation to unpaid money.

The CFMEU urges the Federal Parliament to adopt the measures advocated by this submission, including a statutory construction trust requirement and a mandatory, simplified rapid adjudication process for disputed amounts, to ensure that the potential for unlawful conduct is minimised.



8. THE ADEQUACY OF THE CURRENT LAW TO REDUCE THE LEVELS OF INSOLVENCY

Section 596AB Corporations Act

This section was introduced by the Howard Government in 2000. It prohibits transactions entered into with the intention of depriving employees of their entitlements or reducing the recovery of them and imposes a criminal sanction for breach.

Anderson has noted that the absence of a single prosecution under this section, even though clear instances have arisen which fall within its scope, makes the deterrence value of the section in its current form, 'highly doubtful'.⁴³ Perhaps the section's political architects were aware of its limitations at its inception. Certainly the Australian Institute of Company Directors did not think it was of sufficient concern to resist its introduction.⁴⁴

Fifteen years is more than enough time for a statutory provision to prove its uselessness. For the reasons set out by Anderson, the CFMEU supports amendments to this section which removes the requirement to prove subjective intention, introduces a parallel civil penalty contravention in similar terms and extends the application of the section to all forms of external administration.

Director's Duties, Disqualification and Liability

The *Corporations Act* sets out a statutory version of the various fiduciary duties which would otherwise apply to directors of corporations under the general law. Section 180 imposes a general duty of care and diligence, section 181 a duty to act in good faith and for proper purposes and sections 182 and 183 prohibit the improper use of position and information. Each of these sections is a civil penalty provision attracting a maximum penalty of \$200,000.⁴⁵ Section 184 creates a criminal offence where breaches of ss. 181 to 183 occur through reckless or dishonest behaviour. On their face, a number of these sections could apply to insolvency situations. Section 588G, which imposes civil and criminal sanctions for a breach of the duty to prevent insolvent trading, is specifically directed towards insolvency.

Tables 12 and 13 above show that in relation to these sections alone there were 11,100 possible contraventions reported by external administrators for the 2013-14 year, of which 2393 (or almost 22%), related to the construction industry. Determining

exactly how many of these translate into ASIC prosecutions or other forms of enforcement action from official statistics is not a straightforward exercise.

According to the ASIC enforcement reports for the calendar year 2014 there were 51 'corporate governance' outcomes for that year. This includes a category for 'actions against directors'. If one discounts the actions against liquidators, auditors and other forms of corporate governance misconduct, one is left with only 19 of these 'actions against directors' outcomes in total for the year (14 criminal and 5 civil matters).

The same reports also include a category of 'action against directors' under the heading 'small business compliance and deterrence'. There are a total of 362 of these for the year. Fifty one of them are recorded as involving 'administrative remedies', the remainder involve criminal sanctions. As is noted above however, previous ASIC reports have indicated that these matters include 'technical' breaches such as failure to keep records. In that case it seems unlikely that they represent successful criminal prosecutions for breach of the general duties under s. 184 or the insolvent trading provision in s. 588G(3).

In the body of the reports three prosecutions are cited as case studies under the heading 'Director's Duties'. Beyond this it is possible to look through individual media releases made throughout the year in an effort to find which if any of the more high profile matters might involve breach of director's duties and insolvent trading. When this was attempted, a number of these releases were not available on the ASIC website.

External administrator's reports are only one source for potential ASIC investigations. ASIC conducts its own surveillance and investigation process and presumably receives referrals of potential misconduct from other agencies and the general public. Nonetheless the most recent enforcement reports give very little confidence that beyond a handful of high profile prosecutions, the general duties provisions of the *Corporations Act* are being utilised in any serious way against illegality, either in an insolvency context or otherwise. One commentator has opined:

It seems clear that something should be done to match expectations with performance. If ASIC lacks the resources to pay proper attention to the

⁴³ Chapter 7

⁴⁴ Anderson Chapter 2 page 23

⁴⁵ Sections 1317E and 1317G

*multitude of reports of suspected director misconduct, where a liquidator claims to have documentary evidence in support, an alternative should be devised. It is frustrating for insolvency practitioners to spend the time completing reports in the full expectation that ASIC will not investigate further or prosecute breaches for which the insolvency practitioners hold documentary evidence. If it is a matter of capacity and resources, ASIC needs to make the case for more funding.*⁴⁶

Use of director disqualification provisions to deal with the insolvency problem has its limitations. Notably in the phoenix situation, experience has shown that phoenix operators have little difficulty in arranging for family members, friends or business associates to take on the role of director of a company in which the phoenix operator, disqualified or not, remains the true guiding hand. It has also been suggested that ASIC may invoke the disqualification provisions as an easy alternative to pursuing more extensive orders under the general duties provisions.⁴⁷ In any case, disqualification as a remedy has hardly been over-utilised. There were 28 disqualifications by ASIC or the courts in 2004-05 (up from just 9 in 2002-03). In 2005-06, ASIC announced that it had banned 23 directors from managing corporations.⁴⁸ In the first half of 2014, 24 directors were disqualified.

The 2007 ANAO Report also noted that disqualification was primarily a protective measure to minimise the chance of individuals being able to repeat their anti-social conduct. It does nothing to reverse the effects of monies lost through insolvency.

The CFMEU supports the use of director disqualification measures in appropriate circumstances such as where there has been a deliberate or reckless use of the corporate form to avoid creditors. Disqualification should be retained and utilised as part of a suite of measures to deal with the insolvency issue. The current requirement that a person be an officer of two or more corporations before the ASIC disqualification process can be invoked is arbitrary and unjustified.⁴⁹ That requirement should be repealed.

Personal Liability

Some consideration should also be given to the question of personal liability of directors for unpaid employee entitlements. There are circumstances where personal liability would provide the most just outcome as well as contributing to the deterrence measures needed to address the employee entitlements problem. Phoenixing and obtaining commercial and/or personal advantage by deliberately trading a company into a situation where entitlements cannot be met are obvious examples.

Two general points need to be made. First, the imposition of personal liability would be targeted and accompanied by reasonable defences. These might include circumstances where a director has taken all reasonable and available steps to prevent the company from being unable to meet employee liabilities. There are precedents for these types of provisions. The *Industrial Relations Act 1999* [Queensland] contained such provisions which made executive officers liable for employee entitlements subject to a number of defences. These provisions were repealed by the LNP Government in late 2013.

The second point is that any personal liability provisions are more appropriately included in industrial legislation rather than the *Corporations Act*. Since the provisions essentially relate to the recovery of employee entitlements and since it is likely that orders for payment would involve an element of discretionary decision-making taking into account the industrial circumstances, the union's view is that industrial courts and tribunals are much better placed to determine applications of this kind. Employees, unions and the Fair Work Ombudsman should all have standing to bring these types of applications.

Mandatory capital investment or security deposit for directors of new companies subject to previous adverse reports

There are other measures which might be taken to reduce the number of 'repeat offenders'. Anderson notes that in Ireland where directors are subject to

⁴⁶ Anderson Chapter 5 page 70

⁴⁷ Anderson Chapter 5 page 65

⁴⁸ 'ASICs Processes for Receiving and Referring for Investigation Statutory Reports of Suspected Breaches of the Corporations Act 2001'-ANAO Audit Report No 18 2006-07, pages 79 and 82.

⁴⁹ S. 206F. See also s. 206D.

adverse liquidators reports they are required to provide a minimum capital commitment to any new company or effectively 'show cause' as to why they should be permitted to have a directorship without that requirement.⁵⁰

A similar situation prevails here in relation to unremitted taxes in circumstances of possible phoenix operations. In this situation the ATO can invoke a process which ultimately imposes personal liability on directors for unremitted amounts. Anderson notes that this process could be extended to cover employee entitlements and ASIC could administer the requirement to provide what would essentially be a security deposit.⁵¹ The CFMEU supports these measures.

Section 127 Industrial Relations Act NSW 1996

In the construction industry there is a longstanding practice, expectation and in some instances legal requirement, that the head contractor on a project must assume overall responsibility for the site and the work that occurs there. For example a head contractor has a responsibility to ensure that there are acceptable health and safety standards maintained on their projects. In relation to payments, the former Victorian Building Industry Agreement provided that head contractors were ultimately responsible for any unpaid employee entitlements on projects. Unions regularly sought redress for their members from head contractors relying on this aspect of the agreement.

In NSW there is also a longstanding statutory provision⁵² which requires head contractors to obtain declarations from subcontractors to the effect that the entitlements of the subcontractors' employees have been paid. In the absence of these declarations, the head contractor can be held liable for any unpaid employee entitlements.

There are instances where subcontractors can face insolvency because of events on just one of their many projects. A head contractor may not be aware of difficulties being experienced elsewhere by their subcontractors. However where a head contractor has received the benefit of the work of subcontractor employees it is only reasonable that they take some

steps to monitor the payment of those employee entitlements and make good payments where they fail to do so. Section 127 is one such mechanism. It has proven effectiveness in providing minimum levels of oversight and responsibility on the part of head contractors and a means of redress for employees who have not been paid for their work.

The CFMEU supports not just the retention of s. 127, but the enactment of equivalent provisions at a national level.

An Industry Trust – The Time is Now

Central to the conclusions of the NSW Collins Inquiry was the recommendation for the introduction of a statutory construction trust. This proposal may be summarised as consisting of a statutory provision specific to the industry under which payments from the principal downwards must be made into separate bank accounts and which funds are then held in a series of cascading trusts. The report described the essential features of this trust scheme as follows:

- *The principal is to be required to pay the moneys agreed to be due and payable to the head contractor within 15 days of the receipt of a progress payment in the proper form.*
- *The head contractor is to pay to the subcontractor or subcontractors as the case may be, the amounts not in dispute and properly set out in the progress payment.*
- *The payments from the head contractor to the subcontractor and suppliers cascading downward should be paid into and retained in a separate bank account.*
- *If there is a dispute as to what is due and payable either to the head contractor by the principal or by the head contractor to one or more of the subcontractors, then such dispute is to be dealt with in accordance with the provisions of SOPA.*
- *Once the principal, the head contractor or the subcontractor have paid moneys into the relevant respective construction trust account, then each beneficiary claiming to be entitled to the payment of moneys out of that account is entitled to call upon the trustee to provide up-to-date details of trust account details in the form of copies of the current account balances.*

⁵⁰ Op cit Chapter 7

⁵¹ Ibid.

⁵² Section 127.

- *After payment by the principal into the original trust account, the contractor shall be entitled to deposit the progress payment into an account with any one or more of the authorised investments set out in the NSW Trustee Act 1925 and if the trustee elects to do so it must ensure that the account to which the funds are transferred continues to be described as a trust account for payment to subcontractors and suppliers in respect of the particular project name.*⁵³

This proposal was endorsed following extensive industry consultation and an exhaustive analysis of similar schemes which have operated in other jurisdictions for many years, most notably Canada and the U.S. The Australian Defence Force, which has used a form of trust for its projects for some years, was also considered as a working model.⁵⁴ The report comprehensively disposes of the various arguments put up by the naysayers, including the usual points about the supposed administrative burden inherent in such a scheme.

Unfortunately at this point, the NSW Government has chosen not to implement this key proposal.

The CFMEU supports the adoption of the Collins trust recommendation at a national level. We believe it offers a simple, cost efficient and fair means of dealing with the insolvency problem and the peculiar circumstances of the industry. Coupled with tighter rapid adjudication processes akin to those already provided for in various security of payment legislation [also part of the Collins recommendations], we are of the view that the introduction of such a scheme is long overdue and would go some considerable way to overcoming the types of problems that have plagued the industry for years.

Conclusion

The health of the construction industry, which makes such a vital contribution to the Australian economy overall, is a matter of national interest. The construction industry is the third largest employing industry in the Australian economy accounting for 8.9% of total employment. It generates in the order of 7.7% of the nation's GDP. When systems failures occur here, it damages the industry and the effects reverberate across the economy.

In the first instance though, it is those who work in the industry who are most directly and seriously affected. It is the workers and smaller contractors who are erect our buildings and infrastructure who are most at risk and who are least able to deal with the losses when they occur.

The existing legal machinery and enforcement processes for dealing with this problem have manifestly failed. Whilst some account must be taken of the inherent risks in running any business, the industry's track record and the continuing trail of economic and social devastation left behind by many of these corporate insolvencies reflect a real and serious structural problem that requires urgent attention.

We urge the Committee to adopt the measures set out in this submission – and for Parliament to act on them – as a matter of priority.

⁵³ At page 158.

⁵⁴ It is understood the Western Australian Government is trialing a project bank account scheme on a number of State Government projects at the present time.

CFMEU