

## Chapter 11

### Licensing arrangements

11.1 As the previous chapters noted, the exclusive regulation of building and construction is not within Commonwealth power, as unincorporated businesses operating intrastate will not be covered. Licensing arrangements and standards are therefore governed by each state and territory. Naturally, differences have emerged in the respective schemes. Many submissions indicated their frustration with discrepancies between jurisdictions. The Electrical Trades Union of Australia explained how the state-based licensing regime affects electrical contractors:

Another inconsistency is that electrical contractors in New South Wales and the Australian Capital Territory do not require any business training for licensing purposes, whereas other jurisdictions require between one and four units of competency. Only Queensland and South Australia jurisdictions have provisions of seeking financial statements or evidence of financial status whereas the other jurisdictions do not make it a requirement to assess for eligibility.<sup>1</sup>

11.2 Nevertheless, despite a push for national harmonisation of licensing requirements for participants within the construction industry, the Council of Australian Governments disbanded the National Occupational Licensing Authority (NOLA) in 2013. The NOLA aimed to cover licensing requirements for selected occupations, removing inconsistencies across state and territory borders to allow for a more mobile workforce. In its place, the Council for the Australian Federation is consulting with state and territory regulators and industry to enable 'external equivalence' for selected licences across jurisdictional boundaries.<sup>2</sup> That is, a licence to operate in State X may be accepted by State Y.

11.3 This section does not examine the licensing standards of every state. Instead, it focuses on what submissions considered the three most important elements of a licensing regime in reducing insolvency within the industry: evidence of adequate capital backing; financial skills training; and a fit and proper test. It will do so by close reference to the licensing regime in Queensland, which was a particular focus of submissions and witnesses before the inquiry, and a cause of concern in the Walton collapse.

11.4 In an industry characterised by low barriers to entry, small profit margins and inequitable allocation of risk, an effective licensing regime is necessary to protect participants from both unscrupulous and hapless operators. However, as important as an effective licensing regime is, its inherent limitations must be understood—an effective licensing regime is not a silver bullet for the problems of the industry. Mr Michael Chesterman, Queensland Building and Construction Commission, made

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1 ETUA, *Submission 4*, p. 15.

2 Council for the Australian Federation, 'Occupational Licensing Reform' <<http://www.caf.gov.au/OccupationalLicensing.aspx>> (accessed 1 December 2015).

this point to the committee in explaining the operation of capital backing tests. Mr Chesterman noted that capital backing requirements may 'operate in different ways at different times, but they are always reflective of a position, essentially back in time'.<sup>3</sup> That is, a contractor who satisfies a capital backing test and thus receives a licence to operate at a certain level, has only proven they have capital backing at that 'snapshot in time';<sup>4</sup> it 'is not a guarantee that the company is solvent at every single point of time'.<sup>5</sup>

11.5 It is also important to bear in mind that there are trade-offs when introducing a licensing regime. As Mr. John Price, ASIC and Mr Warren Day, ASIC, stated that Australia consistently rates highly on international surveys measuring the ease of doing business.<sup>6</sup> A key component of this measure is the difficulty or ease in setting up a company. Therefore, increasing licensing requirements in order to protect participants from unqualified individuals may reduce the ease of doing business in Australia. Conversely, excluding unqualified individuals from operating—and collapsing—may increase business confidence.

11.6 A further consideration is the effect licensing regimes have on the public purse. Mr Day noted that there are about 2.25 million companies registered in Australia. Approximately 99 per cent of those are small, proprietary limited companies. Mr Day considered that the process of assessing each person's qualifications and level of experience would be:

...a huge undertaking when you are talking about 2.25 million companies and I think about 1.8 million distinct, different directors. Would all of those have to be grandfathered straight through or would they have to be checked? It is a huge undertaking. There is a huge cost to government in running that out.<sup>7</sup>

### ***Capital Backing***

11.7 A number of submissions, including the Australian Institute of Building, the Electrical Trades Union of Australia and Cbus Super,<sup>8</sup> suggested that an appropriate licensing regime should provide evidence that a contractor has adequate capital backing for a proposed project and require business or financial skills training. For example, Cbus Super indicated its support for measures designed to 'ensure that contractors or sub-contractors were able to demonstrate a financial capacity and wherewithal to meet the level of contract they are seeking through an appropriate licensing regime' with the aim of reducing insolvency in the building and construction

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3 *Official Committee Hansard*, 31 August 2015, p. 35.

4 *Official Committee Hansard*, 31 August 2015, p. 41.

5 *Official Committee Hansard*, 31 August 2015, p. 35.

6 *Proof Committee Hansard*, 28 September 2015, pp. 37, 38–39.

7 *Proof Committee Hansard*, 28 September 2015, pp. 38–39.

8 Australian Institute of Building, *Submission 12*, p. 4, ETUA, *Submission 4*, p. 2 and Cbus Super, *Submission 13*, p. 11.

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industry.<sup>9</sup> As noted in chapter 2, this position mirrors the recommendation of the 2012 Collins Inquiry.

11.8 Cbus Super argued in favour of requiring evidence of capital backing at the licensing stage. In its view, such a measure would 'ensure companies bidding for work are in appropriate financial circumstances to undertake such work' and therefore provide 'greater assurance' for subcontractors.<sup>10</sup>

11.9 The Collins Inquiry appreciated the limitations of licensing regimes. It acknowledged that licensing 'in and of itself, can offer little more than gentle reassurance that a builder has paid a yearly or other fee to maintain a current occupational licence'. As such, it is imperative that licensing 'work alongside other reforms such as capital backing and net tangible asset thresholds, as mandatory requirements to work in the industry'.<sup>11</sup>

11.10 With that in mind, the final report of the Collins Inquiry recommended the introduction of:

...a licensing system which requires all builders and construction contractors operating in the commercial building sector to qualify within a particular graduated licence category according to the net financial backing they are able to demonstrate, in respect of proposed projects. The result will be that the work of builders and construction contractors will be restricted to the category of project value for which they have demonstrated financial backing and licenced accreditation.<sup>12</sup>

11.11 This licensing system would operate in a similar fashion to that in Queensland. The Queensland Building and Construction Commission informed the committee of the licensing framework for building and trade contractors in that state. The Commission explained that the financial requirements for licensing have recently been replaced but set out the policy that was in place at the time of the collapse of the suspected illegal phoenix operation known as Walton Construction (Qld) Pty Ltd. The Commission noted that under the previous policy (the Financial Requirements for Licensing Policy—FRL):

Licensed contractors were required to maintain a minimum level of liquidity and hold a minimum value of net tangible assets to support their Allowable Annual Turnover (AATO). The FRL Policy established financial categories which set the AATO for licensees based on the level of net tangible assets held by the licensees of each financial category. Licensees were not permitted to exceed their AATO amount. If a higher turnover was required, the licensee needed to apply for a higher AATO with evidence

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9 Cbus Super, *Submission 13*, p. 11.

10 Cbus Super, *Submission 13*, p. 2.

11 *Final Report of the Independent Inquiry into Construction Industry Insolvency in NSW* (2012), p. 353.

12 *Final Report of the Independent Inquiry into Construction Industry Insolvency in NSW* (2012), p. 353, Recommendation 3.

that the licensee held the required level of net tangible assets for the higher AATO.<sup>13</sup>

#### 11.12 The Commission continued:

Depending on a contractor's financial category, a declaration, independent review report or audit report was required to be provided on licence application and renewal as evidence that the contractor satisfied the financial requirements set out in the FRL Policy. Independent review reports and audit reports were required to be prepared by an 'Appropriately Qualified Person' or 'AQP' as defined by the FRL Policy.

The complexity of the report and the qualification of the person preparing the report increased with the financial category. Licensees with an AATO of \$300,000 or less could provide a declaration as to their compliance with the financial requirements. Contractors with an AATO of more than \$300,000 were required to provide an Independent Review Report or if the company was required to be audited under the *Corporations Act 2001*, an Audit Report prepared by a registered company auditor was required to be provided.<sup>14</sup>

11.13 It appears that the FRL policy has proven effective in ensuring that contractors without adequate financial backing are not allowed to engage in high value projects. The FRL Policy became effective on 1 October 2014. Between that date and 30 June 2015, Mr. Chesterman informed the committee that the QBCC undertook '286 non-payment of debt investigations resulting in the suspension of 75 licences and the cancellation of 54 licences'.<sup>15</sup> These statistics are important because licensing standards are only as effective as their enforcement.

11.14 The QBCC acknowledged that this licensing system did not prevent the collapse of Walton Constructions (Qld).<sup>16</sup> It should be remembered, however, that licensing systems are merely gateposts to the industry, not the primary detection or enforcement mechanism.

#### ***Financial and business acumen***

11.15 Chapter 2 demonstrated poor financial and business acumen was a principal cause for insolvencies in the industry. Many witnesses and submissions recognised this and indicated support for strategies designed to improve participants' financial management skills. The ETUA considered this approach 'worthwhile' suggesting that it 'should be introduced at the point of licensing and in qualifications'.<sup>17</sup>

11.16 Master Builders Australia provided a series of quotes arising from consultations with its members. The overwhelming message from these consultations was improving business and financial skills of new entrants:

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13 QBCC, *Submission 19*, p. 1.

14 QBCC, *Submission 19*, p. 2.

15 *Official Committee Hansard*, 31 August 2015, p. 33.

16 QBCC, *Submission 19*, pp. 3–7. See also Subcontractors Alliance, *Submission 18*, p. 5.

17 ETUA, *Submission 4*, p. 15.

If the young blokes don't have business or entrepreneurial skills then they won't last very long in the industry...

The industry needs more business skills training. As an industry we do a poor job of teaching apprentices about business management.

We should add one or two modules on business management to Cert 4.<sup>18</sup>

11.17 They continued:

We need to train young builders much better in running a business...

Building licences are too easy to get. We need to have a tiered licencing system. HWI (home warranty insurance) at the moment in (State name here) really is the de facto licencing system.

HWI is really the framework for licencing—what you can do, the value of the work you can do.

(Regulators and the industry) should look at a bronze/silver/gold tiered licencing system, which applies as the business scales up.

We need tiering (of licences). Younger builders should have to get at least two years post ticket experience. They should also have a diversity of experience across a range of projects before they can get an unrestricted licence.<sup>19</sup>

11.18 Mr Wilhelm Harnisch, CEO MBA, informed the committee that the Master Builders are 'actively promoting and encouraging' apprentices to upskill through their own training programs. Mr Harnisch explained:

What we are doing actively, in terms of upskilling through our own training programs, is encouraging particularly apprentices at year 3 or year 4 to take on business courses, preparing themselves to be able to understand contracts.<sup>20</sup>

11.19 Although not mandatory requirements, Mr Harnisch considered that these programs would better position participants in the industry and provide them with critical business and financial literacy capabilities. Mr Harnisch did acknowledge that not all individuals would appreciate financial skills training during their apprenticeship, and in some cases, it may be more appropriate for the training to be conducted at registration level.<sup>21</sup>

11.20 The HIA agreed that levels of financial and business acumen across the industry are a concern, though were somewhat philosophical about this. Mr Glenn Simpson, General Counsel HIA, noted that 'it is difficult to be entirely knowledgeable about the full range of legal and financial issues when essentially you are a builder, not a lawyer'.<sup>22</sup> Further, Mr Graham Wolfe, Chief Executive, Industry Policy and

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18 MBA, *Submission 3*, p. 20.

19 MBA, *Submission 3*, Appendix B, p. 29.

20 *Proof Committee Hansard*, 4 November 2015, p. 5.

21 *Proof Committee Hansard*, 4 November 2015, pp. 5–6.

22 *Proof Committee Hansard*, 4 November 2015, p. 49.

Media, HIA, considered that he was not 'entirely qualified' to speculate on the connection between insolvencies and inadequate financial and business skills.<sup>23</sup> Mr Wolfe suggested that builders should engage and rely on appropriate specialists if they are concerned about their financial acumen.

11.21 Nevertheless, Mr Simpson informed the committee that the HIA provides certificate IV courses, and believes that 'a greater emphasis' should be placed on commercial issues at the certificate III and certificate IV levels.<sup>24</sup>

11.22 Consistent with their position on financial skills training and in contrast to the MBA, the HIA contended that requiring additional financial and business acumen courses at registration level would not be appropriate. The HIA warned that doing so may damage productivity throughout the industry and cause individuals to seek other opportunities. They noted:

The average small business builder/principal contractor spends significant hours each week attending to paperwork and compliance obligations arising from regulatory requirements including business, income and payroll tax compliance, training regulations that apply to apprentice employees, workplace health and safety management, occupational licensing and state-based home building laws and requirements.

Regulations impose cost, barriers and administrative burdens on firms that distract them from their principal objective of growing and running a profitable business.<sup>25</sup>

11.23 Of course, a revamped licensing regime will not ameliorate all issues. As Mr O'Sullivan, Masonry Contractors Association, noted, in most cases on-the-job training and investment in the workforces offers the best prospect for enhancing business acumen within the sector, though the structure of the industry and accompanying regulatory framework must prove conducive to long-term planning for this to eventuate:

You have to start cross-pollinating that as well, between a tradesman and a businessman, to talk about how they work out efficiencies and processes. You can have someone who has gone to university who does not have the skill, and you can have a person who has the skill but does not have the mind to process how the systems and efficiencies work. That is what we found. Our tech company got involved with people who had nothing to do with the construction industry, because they could understand processes. We had a guy who had done computer science and robotics and, within three months, he could run a job better than Lend Lease, because it was all automated and we showed him how to do it.<sup>26</sup>

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23 *Proof Committee Hansard*, 4 November 2015, p. 51.

24 *Proof Committee Hansard*, 4 November 2015, p. 49.

25 HIA, *Submission 7*, p. 3.

26 *Official Committee Hansard*, 12 June 2015, p. 50.

### *Fit and Proper Person Test*

11.24 Submissions and witnesses noted that an effective licensing regime requires a third criterion: a 'fit and proper person' test. The QBCC noted that under the *Queensland Building and Construction Commission Act 1991* (QBCC Act) applicants seeking a contractor's licence must meet certain additional requirements. In addition to technical and managerial qualifications, a minimum level of experience and the financial requirements examined above, the applicant 'must be fit and proper' to hold a licence.<sup>27</sup> The HIA pointed out that in relation to the housing industry; similar arrangements exist in South Australia, Victoria, Western Australia and New South Wales.<sup>28</sup>

11.25 The Commission explained further that the QBCC Act provides the Commission with the power to exclude individuals from holding a contractor's licence for a period of 3 years. The exclusion provisions apply to any individual who in the previous 5 years:

- has taken advantage of the laws of bankruptcy or become bankrupt; or
- was the director, secretary or influential person of a company at, or within 1 year immediately before, the company has had a provisional liquidator, liquidator, administrator or controller appointed or has been wound up or ordered to [be] wound up.<sup>29</sup>

11.26 An individual who is excluded twice is then permanently excluded from holding a contractor's or nominee supervisor's licence and cannot be the director, secretary or influential person of a QBCC licensee. Failure to do so results in the company's licence being cancelled. Mr Chesterman informed the committee that as of 28 August 2015:

...a total of 1,921 individuals and 534 companies are currently subject to an exclusion period under the QBCC Act. In addition, 674 individuals, comprising 461 former licensees and 213 individuals who have never held a licence, have been permanently excluded from holding a contractor's licence or a nominee supervisor's licence since exclusion provisions commenced in 2007. The 674 individuals permanently excluded include the 461 former licensees and 213 individuals who have never held a licence but were directors, secretaries or influential persons for a failed building company.<sup>30</sup>

11.27 Mr Chesterman, QBCC, described these exclusionary provisions as 'the commission's anti-phoenix licensing provisions'.<sup>31</sup>

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27 QBCC, *Submission 19*, p. 1 and *Queensland Building and Construction Commission Act 1991* (Qld), s 31(1)(a).

28 HIA, *Submission 7*, pp. 10–11.

29 QBCC, *Submission 19*, p. 2.

30 *Official Committee Hansard*, 31 August 2015, p. 33.

31 *Official Committee Hansard*, 31 August 2015, p. 33.

11.28 The QBCC noted that there is a 'limited opportunity' under the QBCC Act for an individual to apply to have a relevant event excluded. The individual must establish that she or he took 'all reasonable steps' to avoid the relevant event from occurring.<sup>32</sup>

11.29 Cbus Super supported the existence of a fit and proper person test as part of a national licensing system. However, whether or not a national licensing system is eventually developed, Cbus Super considered that a fit and proper person test could include:

- whether or not company directors had been associated with previous insolvencies and the circumstances of such insolvencies; and
- the extent of financial management skill retained in the company—including an audit of financial records and record keeping.<sup>33</sup>

11.30 The Electrical Trades Union of Australia supported this proposal, recommending 'increased financial probity checks on an individual's bankruptcy/insolvency history within the context of licensing'.<sup>34</sup>

11.31 Veda also supported the intention behind this proposal but suggested the introduction of a beneficial owners register might be more appropriate. This proposal will be examined in the following chapter.

## **Conclusion**

11.32 The committee notes that the Council of Australian Governments disbanded the National Occupational Licensing Authority in 2013. In its place, the Council for the Australian Federation is working with state and territory regulators and industry, toward external equivalence for selected licences across jurisdictional boundaries. As such, it appears that national harmonisation is unlikely to be a viable option into the future. The committee therefore stresses that states and territories should develop their construction licensing regimes in a manner that protects industry participants and clients from the damaging effects of insolvencies.

11.33 Notwithstanding the failure of the then QBSA (now QBCC) to prevent the collapse of Walton Constructions, the committee believes that a graduated licensing scheme, similar to that currently operating in Queensland and recommended by the Collins Inquiry, which requires all builders to demonstrate they hold adequate financial backing for the scale of intended project is a necessary first step.

11.34 The committee believes further that, in light of the low barriers to entry and incidence of insolvencies in the construction industry, some form of financial and business skills training should be a pre-requisite for the registration of a builder's or contractor's licence. In many states and territories this is already the case. The committee therefore encourages the states and territories to engage with industry and develop appropriate and consistent standards. Advanced training in business,

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32 QBCC, *Submission 19*, p. 2.

33 Cbus Super, *Submission 13*, p. 13.

34 ETUA, *Submission 4*, p. 3.



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including principles of construction contract law, should be undertaken at post-trade level.

11.35 The committee believes that a fit and proper person test would improve the rigor and integrity of the licensing regime. Consideration should be given by each state and territory to either: (a) introduce such a test where no test exists; and (b) extend it across the entire construction industry. The committee notes further that a critical element of any fit and proper person test is the regularity and responsiveness of the test to a change in circumstance. Automated cross-agency data sharing could trigger an alert on matters such as bankruptcy, fraud conviction, director disqualification, and/or liquidation, leading the regulator to satisfy itself that the licence-holder remains a fit and proper person.

11.36 It is important to recall that any licensing standard is only effective if it is enforced. The committee believes that greater resources need to be directed to appropriate regulators in order to ensure that all participants within the industry maintain conditions appropriate to their registration level.

#### **Recommendation 32**

**11.37 The committee recommends that the Council for the Australian Federation and state and territory regulators continue to develop external equivalence for licences in the building and construction industry.**

#### **Recommendation 33**

**11.38 The committee recommends that each state and territory licensing regime contain three key requirements:**

- **that licence holders demonstrate that they hold adequate financial backing for the scale of their intended project. This capital backing requirement should be graduated, with increased levels of proof required for more significant projects;**
- **that on registration, licence holders provide evidence they have completed an agreed level of financial and business training program(s), including principles of commercial contract law, developed in consultation with industry bodies; and**
- **that licence holders demonstrate that they are a fit and proper person to hold a licence.**

#### **Recommendation 34**

**11.39 The committee recommends that automated cross-agency data sharing should trigger an alert when an individual: declares bankruptcy; is convicted of fraud; is disqualified as a director; or liquidates a company. This alert should require the relevant state or territory regulator to satisfy itself that the licence-holder remains a fit and proper person.**

