

ReBUILD Australia

Plumbers, Painters, Electricians, Insurers



ReBuild Australia is an industry led working group of trade associations leading the construction industry to make sure small businesses get paid for the work they do to protect livelihoods and create jobs.

20 August 2020

ReBUILD Australia proposals for October 2020 Federal Budget

Outcomes Sought

Ensure taxpayers funds are used for their intended purpose; to support & create jobs.

Innovative approaches and use of technology to ensure;

- Funding barriers to access government stimulus building grants are removed
- Ensure government building stimulus funds are used to pay SME tradies for work completed and not lost to builder insolvencies
- Guarantee that government building stimulus funds achieve the economic stimulus sought rather than destroy the livelihoods of small businesses in the sector

The industry requires a government guarantee to remove the uncertainty of payment for all.

Introduction

The building and construction industry has been placed front and centre by the Australian government in its plan to “Rebuild” its way out of the Covid-19 triggered economic crisis. However it is imperative for the economic benefits to be realised that small and medium businesses that make up over 98.5 percent of the sector and trade subcontractors that represent over 82 percent within the sector get their share of the spending bonanza in order to maintain and support employment levels and create jobs. The government’s plan should be to **protect**, support and create jobs.

It is vital that the government does everything it can to ensure the promised historic wave of investment will deliver the economic growth we so desperately need. That means we must prioritise innovation in the sector. Business as usual is not an option.

Many of the SMEs in the industry and in particular trade contractors are not represented by the Master Builders Association or the Housing Industry Association, but by speciality trade associations that struggle to be heard by government.

There is a perception in the sector that:

“As a trade contractor the government stimulus package have left us out in the cold. Grants are aimed at supporting the industry’s biggest players”. Andrew Murray, Tiler

“All top 10 building groups are now capping their monthly sales, some of them have nearly sold out their September allocation” Property Developer and rich lister Nigel Satterly told the Australian Financial Review.

“Builders win fewer jobs despite grant” AFR 20/8/20 discusses that small and micro builders are winning fewer jobs and that the qualifying criteria for the HomeBuilder Stimulus is too onerous.

Developers and large builders are requesting that the government homebuilder stimulus package is extended to give large land developers more time to title more lots of land to increase their profits and the profits of Australia’s largest builders. We agree it should be extended, but not in its current form. We propose the changes outlined below to ensure

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that the SMEs who make up the majority of the industry can also be guaranteed to benefit from taxpayer funded stimulus payments.

Both government stimulus for jobs and economic activity grants need to have broader application rather than just benefiting land developers and large builders. Demand by homeowners for off the plan homes is weak with many homeowners preferring to live inner city and complete a major renovation rather than a new home build in the outer suburbs. Homeowners should not be penalised by state-based grants such as in Western Australia that are only available on new homes or apartments. Such grants target large developers and builders and not tradies.

To proceed with any building work, particularly in the current economic conditions, confidence is an essential requirement. There is increasing uncertainty in the construction sector that building stimulus grants for developers and large builders will only serve to intensify this uncertainty unless payment problems in the industry are addressed. Building contracts must be entered into which are fair and include the requirement to use cascading trust accounts to protect and guarantee project funds. Standardised contracts and subcontracts should be provided on projects, with assistance provided for industry participants who are less sophisticated . The government should invest in innovation that will help small businesses access expertise in administering and adhering to contracts supported by the Security of Payment Acts so that homeowners and small business subcontractors are not left at the mercy of larger builders or contractors.

Of the 1,200,000 workers in the building and construction industry, 350,000 (29%) workers are supported by the government's Jobkeeper scheme. (MBA 2020 budget proposal). At 40%, construction has one of the largest share of workers on Jobkeeper out of all sectors. The government needs to focus on industry stimulus that helps SME businesses in the sector transition back into a situation where they can pay for their employee's wages out of their income. This means providing greater security for contractors and subcontractors to be paid for the work they do. This can be achieved by using cascading trusts to ensure government building stimulus and payments for building works completed by small business contractors are paid immediately against contracts for works at all levels of the supply chain. Overcoming most industry payment and cashflow issues. Cascading trusts will largely achieve the government's desired objective of protecting and creating jobs and delivering economic benefits.

Government should support this type of innovation that removes all the industry barriers to use with a government guarantee to remove uncertainty for all. This can be delivered by way of the existing SME loan guarantee the government has provided to large banks. Instead funds administered through cascading trust accounts, using technology that enforces existing statutory payment protections enables the immediate payment of approved invoices at all levels of the supply chain. Given the very low risk of these transactions due to the use of cascading trust accounts and the enforcement of existing legislative payment protections, providers of this type of service should be able to tap into the government's SME 50% loan guarantee scheme alongside major banks.

Proposed Budget Measures

- 1) Government Investment in building and construction
- 2) Expand Homebuilder stimulus grants so they directly benefit SMEs that make up 98.5% of the sector.
- 3) Attract private investment into the sector by reducing/removing the insolvency risks by supporting innovation

Residential

Homebuilder stimulus

- Instead of a Homebuilder grant that is only eligible to builders (who represent around 18% of industry) offer homeowners a 30% rebate on completed projects by a licensed trade
 - Reduce eligibility threshold from \$150k to \$50K
 - Increase salary and property valuation caps
 - Extend the program for 12 months
 - Request state governments mirror the homebuilder program to include renovations. (WA has excluded renovations to qualify for the \$20k grant)
- a) Incentivise residential investors to renovate by removing the HomeBuilder grant investor exception.
 - b) Allow homeowners to access a portion of their superannuation to renovate or build or to lend to their children to build or renovate property.
 - c) The First Home Super Saver Scheme should be extended to include both buying a new home and renovations.

Attract private investment in building and construction

Government needs to use the disruption of COVID19 as an opportunity to address the payment and cash flow issues in the industry.

For too long building and construction businesses have not been making money on projects. The high rates of insolvency have resulted in industry access to insurance becoming problematic and private investment in the sector declining.

To attract more private investment government must address the high rates of business insolvency and working capital shortage by supporting innovation in the sector.

Commercial construction

- a) Government funding for projects should be linked to the use of cascading trust accounts which manage payments and provide trade contractors the required safeguards for prompt payments

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- b) Grants should be available to commercial builders who agree to use cascading trusts to manage payments
- c) Focus on minor works contracts that generate more immediate work for SME contractors

Support for small businesses in the building and construction sector

- a) Support innovative financing and payment solutions that link directly to payments from homeowners for work completed and improve cash flow in the industry by providing platform providers and non-bank providers access to the government's 50% SME loan guarantee.
- b) The National Housing Infrastructure facility to support innovative finance offers that get the grant money out the door quickly and is paid against contracts for work completed by builders and tradies directly via cascading trusts.
- c) Government support for innovative approaches to help SME businesses transition back into a situation where they can pay employee's wages out of their income. Approaches that ensure government building stimulus payments are directly paid against works completed should be supported.
- d) Support digitisation of payment processes which will remove uncertainty, enable fast payments, foster collaboration and speed up the delivery of projects.
- e) Deliver on the promise made to Senators Nick Xenophon and Rex Patrick to protect payments for SME contractors in return for getting their vote to legislate the creation of the ABCC. The Murray review recommendations provide the road map for industry wide implementation of cascading statutory trusts.
- f) Deliver on commitments made in the Building Ministers forum meeting to standardise security of payment laws across the country and legislate the use of cascading statutory trusts across the sector to protect progress payments and retentions held for small businesses that have done the work
- g) Access to government building stimulus funds should be conditional on having in place the required safeguards and guarantees for payment through the use of cascading trust accounts.
- h) Enforce industry compliance to Security of Payment Laws.

Tradie shortage

Expect shortages in specialist trade subcontractors such as bricklayers, carpenters and plasterers. Many have left the industry because they can't make a fair income, receive reasonable profits on projects, suffer long payment delays or don't get paid at all if builders fail.

To retain and attract specialist trade contractors the government must offer payment protections .

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- Offer a kickstarter grant of \$12k to businesses for any new jobs created aimed at employing people aged 16 – 25.
- Offer start-up grants for tradies setting up new businesses.

Innovation

The opportunity to build a more financially robust construction supply chain.

- Support digital connectivity, collaboration and transparency.
- Innovation that increases the ability to leverage private capital, with government providing support.
- Innovation that can spend the money quickly and ensure benefits are realised.
- A fund that can provide renovation and development finance for private sector led projects that use cascading trusts to safeguard and guarantee payments
- Require project owners as a condition of funding, to use cascading trusts or technology that enables payments via cascading trusts and fast payment, ensuring appropriate allocation of risk.
- Support digitalisation of the sector for e-invoicing, and other digital cash flow management platforms that reduce time and cost and increase productivity.
- Support innovative funding models that remove the access to loan barriers for homeowners for new builds or renovations that use technology to deploy funds via cascading trusts against contracts for works and immediate payment of approved invoices to solve the cash flow issues for builders and the supply chain.

Industry factors that support our proposal

Where is the activity coming from?

Given the drop in immigration from overseas , reduced interstate movements, increased dwelling supply, a big increase in unemployment resulting in lower confidence and the high level of debt; we are passing to the younger generations massive financial problems.

ReBUILD Australia proposes another way to generate activity in the sector. We should be encouraging every Australian to improve their home via a renovation or upgrade by building a new home. Now is the time for government housing stimulus to support young people to build or renovate a home. Government and the industry should be encouraging parents to lend money to their children to get them into the property sector, whether that is to build a home or to renovate one. Many millennials do not wish to live in the outer suburbs and government needs to be mindful of not funding further urban sprawl, in an already over supplied market with homes that are likely to be worth less then resale price once built. This only serves to disadvantage homeowners and benefit land developers and large builders.

Homeowners should be able to access their superannuation to help fund their children into new homes or a renovation.

Older Aussie's should help their young adult children shoulder the COVID19 debt burden as they are in a better position and more comfortable financially to help secure their children's future via a new home build or renovation. The wealth gap between older and younger Australians has hit its highest level this century with fears that home ownership is out of reach for many young people (Australian Institute of Actuaries). Young people are becoming increasingly disadvantaged across a range of financial and life quality measures. Home ownership rates for young Australians have fallen from 50% in 2000 to about 36%. High house prices and low interest rates has made it difficult for younger people to save for a home, especially with the BNPL generation having an aversion to traditional bank finance or paying interest at all.

There is the opportunity to better target the Jobkeeper program so instead of jobkeeper payments being paid to retailers by millennials for shoes and handbags, government should encourage young people to invest in what will be their biggest asset - their home. This is achieved by supporting access to new innovative funding models that appeal to this generation and provide government incentives to build or complete a major renovation. This will ensure that the jobkeeper debt the nation is accruing is used to support future generations who will need to live with the debt. Housing has a big role to play in lifting Australia out of recession and will make Jobkeeper a jobcreator rather than a retail dividend keeper.

This is a once in a lifetime opportunity to support young people in Australia to invest in their financial future through real estate. Given we will be leaving an extraordinary level of public debt for future generations, it is only fair that Australian young adults benefit from government stimulus to help secure their futures and standard of living.

Stimulus should not be targeted to just new builds that result in long term negative impacts. The established residential property market should not be excluded from benefiting from government stimulus grants. It is not the role of government to maintain the market share of large builders. Government stimulus needs to stop focusing on builders and land developers and focus on benefiting homeowners and tradies. Otherwise the government risks a severe skills shortage in the industry, as builders can not deliver projects without the tradies to do the work.

Protect, support and create jobs

Protecting payments by cascading trust accounts to safeguard against construction insolvencies will strengthen the Australian economy, reduce risk to attract private investment and enhance job security.

The industry now operates in an environment where non-payment for work carried out is commonplace. Uncertain cashflows leave businesses lower down the subcontracting chain with little power relative to the larger businesses at the top.

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Typically, it is difficult for SMEs to break into public sector or government works projects that benefit large builders. The government should focus on fast tracking minor works projects that benefit SMEs in the sector.

A large majority of building projects are small, and it is these projects that should now flow from government's stimulus and facilitate recovery. We need more immediate activity that comes from small-scale building works by business and homeowners that includes the renovation of a business premises, home or investment property. The government should be focusing on renovations rather than using taxpayer funds to support large developers and builders.

The building and construction industry is built on a house of cards. When a builder collapses, trade subcontractors also fail. Given the payment problems in the industry, these small businesses don't want loans. They want to be guaranteed to be paid fast. Given the low uptake of the government SME loan scheme, funds should be deployed to innovative homeowner funding models for new builds and renovations that use technology to manage the payment of those funds directly against works contracts. This will provide the cash flow support that SMEs need in the supply chain.

Without the required payment protections government stimulus grants could result in the accelerated collapse of subcontractors businesses as builders and larger contractors focus on maintaining their own cash flows and profit margins at the expense of tradies that have done the work.

Over 82% of the industry (the tradie) does not think it acceptable for government to rely and 'hope for the best' that the trickle down effect of the HomeBuilder stimulus grants will benefit them. They are at the end of the trickle effect and need to know government stimulus will benefit them in creating jobs and rebuilding the Australian economy.

Land developers and large builders have already increased the cost to buy land and build a new home meaning that taxpayer funded building grants have already been gobbled up by land developers and builders. The price rises are in excess of the benefit of the grant. This means HomeBuilder grants are not offering any additional financial assistance for Homeowners.

Inexperienced homeowners are likely to pay over \$100,000 more for a home and land package than what it would cost to buy an established home next door. Many of the new homes will be worth less than the total cost the moment the keys are handed over, especially those on the urban fringes who are at risk of oversupply as tracts of land are opened up. Land developers quickly cashing in on government stimulus packages will exacerbate this situation. Should there be a Coronavirus housing bust, the homebuyers that have purchased a home and land package in the outer suburbs are most vulnerable to be left with homes that will be worth significantly less than mortgages taken out. The government needs to focus away from stimulus that supports large builders and property developers and focus on supporting the existing property market through major renovations or inner-city new builds.

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The UK government has stipulated that Project Trust Accounts be used on all projects and have shown that the use of them improves the performance of the supply chain, streamlining the overall payment process. Government department HS2 has further strengthened fair payment to SMEs in the supply chain by requiring businesses at all levels to use trust accounts for payment to make sure that all contractors, big or small, working for HS2 feel confident and supported as they work together to build Britain's new low-carbon high speed rail. We expect the same level of payment support from the Australian government.

Given the amount of taxpayers funds entering the industry, government face unlimited liability and risk of class actions. The precedence was set during the GFC when many state based ex-gratia payments intended to stimulate small businesses were lost when builders collapsed before paying contractors and subcontractors for the work done on government stimulus projects.

Taxpayers do not want to see their money squandered on builders who fail, or misappropriate their money leaving any remaining assets to pay administrators/insolvency experts and banks. Without cascading trusts the small businesses that paid the employee wages, created the jobs and paid the suppliers are left high and dry to fend for themselves.

The government can no longer continue to turn a blind eye to the illegal and inverted pay-when-paid arrangements that continue to be the basis of operation of payments in the industry due to builders being not sufficiently capitalised to pay the small businesses in their supply chain.

It is unrealistic and unreasonable for government to expect that the small businesses should take out cash flow loans to cover the delayed payment from the builder or larger contractor. It is unreasonable for small business to continue providing what is effectively interest free loans to those further up the payment chain.

This can be seen by the very low uptake by SMEs in the construction sector of government guaranteed loans. This is not what the industry wants or needs, they just want to be paid for the work they do. These loan offers serve to further disadvantage the small businesses in the sector and benefit only the banks providing them.

Governments' attempts to stamp out the practice of developers and contractors delaying payment to subcontractors and suppliers by ignoring progress claims, raising spurious reasons for not paying or simply delaying payment (lemma 2002) by legislating across Australia nationally inconsistent laws is insufficient to alleviate the insolvency problems. The inability to secure prompt payment remains the biggest on-going problem within the industry.

Government needs to be concerned and should be taking action to deal with the continuing fragile nature of many large tier 1 contractors and builders which have weak balance sheets. The additional pressures imposed by COVID19 should be the catalyst to finally require cascading trust accounts to protect and guarantee payment for the small businesses that

make up 98.5% of the sector. The industry is sitting on a cash flow timebomb that current government stimulus or government lending guarantees is not alleviating. The industry needs funds paid immediately against contracts for works with the payment protection of cascading trust accounts to ensure the immediate payment of funds reach the SME businesses at the bottom of the supply chain.

“Large insolvencies are inevitable”. Phillip Lowe, Reserve Bank governor (AFR 15/8/20).

It has been seen with projects like Opal Towers that poor payment practices lead to poor behaviours which, in turn, lead to poor quality of work. This issue impacts the entire way the industry operates. With government stimulus for residential construction that only builders can access, homeowners are exposed to the risk of loss of project funds due to builder collapse and poor quality work.

Government must support and invest in new innovative payment and finance offers that protect payments and encourage prompt payment.

The industry must adapt to wide scale use of e-invoicing and digital technologies that fully digitise the overall payment process linked to deemed cascading trust accounts overlaid with industry regulatory compliance that removes the barriers to use at every level of the supply chain. This will deliver monumental benefit to the industry and turbocharge broader economic recovery.

Any technology or bank account solution must include tools for tracking and reporting claims for payment and variations. A fundamental role of holding the funds in trust is also ensuring that they get to the right people once certain criteria are met. Allowing users to exchange information about payment claims and variations and manage the tracking of approvals, holding funds and releasing them or withholding them based on particular triggers (e.g. a dispute) whilst ensuring compliance to industry regulation and the contracts for work.

Government must remove the distraction of payment insecurity. More importantly, government must act now to be seen to provide the solution that enables cash-strapped firms to survive the current crisis. There is no more effective way than cascading trusts to protect against insolvency and provide shorter payment times. The government must invest in innovative solutions that provide this level of payment protection and guarantee.

In a sector already renowned for the highest number of business failures and collapses, the government can save the Australian economy over \$5 billion every year by using innovative technology to guarantee payments via cascading trusts. The government would be negligent in their duty of care to taxpayers and the 395,000 predominately small and medium businesses in the sector to not prepare and protect against the avalanche of insolvencies heading our way and the snowball effect this will cause in the sector due to the hierarchical contractual arrangements and deep supply chains of the sector.

‘As money passes down the chain from owner at the top, through the head contractor (builder) to subcontractors, sub-subcontractors and suppliers. Businesses at the bottom of the chain face significant risk of payment delay and default. Payments may be delayed due to the action of either a direct contractual counterpart, or any party operating at a higher tier. This hierarchical contractual chain leaves subcontractors not only vulnerable to the consequences of late payment (having to find their own source of finance to survive, pay their employees and suppliers) but also to the risk of insolvency by a business at the top of the pyramid’ (Commonwealth government commissioned review by Murray 2017)

And this from SERC 2015,

“Owing to the pyramidal structure of the construction industry in Australia, the failure of businesses up the contractual chain can affect contractor and subcontractors further down the chain, as well as suppliers, developers. Homeowners and other participants that are part of the building project. The failure of one business can push others over the fiscal cliff, ultimately resulting in significant financial cost to individuals through-out the industry”.

Additionally, the industry behaviours of phoenix activity whereby businesses are sucked dry of assets and funds unpaid to subcontractors for work completed and diverted into a new business entity free from subcontractor creditors, before placing the initial entity into liquidation.

Trade subcontractors at the base of the pyramid lack the bargaining power to negotiate more favourable contractual provisions, such as better payment terms or interest on late payments (Murray 2017).

The government needs to acknowledge the shortfall and limitations of state-based security of payment laws, that this legislation by itself has failed to solve these problems. Government should be supporting innovative technology driven solutions that take a different approach in line with government commissioned recommendations to address these issues.

The financial and economic benefit of using cascading trusts in the building and construction industry will create financially better off small to medium sized construction businesses that make up 98.5% of the sector (Houston Kemp Economists 2019). Including lower financing costs, reduced insolvencies and with the use of technology innovation, there will be no additional administrative or compliance cost burden. Houston Kemp highlights the key benefit for industry and the economy being the reduction in costs resulting from insolvencies, which are over \$5 billion every year, expected to triple as a result of COVID19. This does not include the health cost as a result of high rates of suicide and family destruction in the sector from business failure.

Payment Times Reporting Bill

We recognise that late payment is not confined to the building and construction industry alone. We applaud the government in following the UK lead in implementing a payment times reporting bill. Unfortunately, this bill will have very little impact on the Building and Construction industry in Australia given the \$100m turnover threshold. 98.5% of businesses in the Building and construction industry are small businesses and would be well below the turnover threshold for the bill to apply.

The unique pyramid structure of the industry continues to require and justify government intervention whereby hierarchical contractual arrangements that aggravate the issue of late payment, and non-payment. This structure results in a chain of payments, from top being the homeowner/client to the bottom being the tradie.

“As money passes down the chain from the owner at the top, through head contractors to subcontractors, sub-subcontractors and suppliers. Businesses at the bottom of the chain can face significant risk of payment delay and default. Payments may be delayed due to the action of either a direct contractual counterpart, or any party operating at a higher tier. (Fiocco 2018)

Conclusion

It is not too late to legislate statutory cascading trusts to assist with this COVID 19 crisis. In the immediate term, government should still support industry innovations that remove all barriers for the use of cascading trusts to manage payments via commercial arrangements.

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