

10 June 2022

# SUBMISSION TO BUILDING AND CONSTRUCTION DEVELOPER REVIEW PANEL

## BACKGROUND

Master Builders is Queensland's peak industry body for building and construction in Queensland and represents the interests of over 9,500 building and construction related members. Most members are licensed builders or trade contractors regulated under the *Queensland Building and Construction Commission Act 1991* (QBCC Act).

This submission outlines Master Builders policy positions on a range of matters relevant to the review of developers currently being conducted by the Building and Construction Developer Review Panel.

## **(1) Payment protections for head contractors**

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### **Master Builders position**

**As a general proposition, head contractors are given equivalent payment and fair contract protections when dealing with developers as those currently afforded between builder and subcontractor.**

Security of payment and fair contracting legislation in Queensland principally targets the contractual relationship and payment practices between head contractors and subcontractors. By comparison, the level of legislative assistance to promote appropriate and proper contractual and payment practices by developers in their dealings with head contractors is minimal.

Examples of the disparity in the legislative treatment of developers and head contractors in Queensland include:

- The *Building Industry Fairness (Security of Payment) Act 2017* (BIF Act) imposes project trust obligations on head contractors for the benefit of subcontractors. Developers, despite being at the head of the contract chain, are not subject to similar requirements to protect monies owed to head contractors.
- Unlike licensed head contractors, developers are not subject to a licensing or akin regulatory regime that requires them to be financially viable, pay their debts when they fall due, and comply with fitness and propriety obligations.

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- Section 67GB was recently introduced into the *Queensland Building and Construction Commission Act 1991* (QBCC Act) to prohibit unfair contract terms in building contracts. However, the provision expressly excludes principals from the application of the relevant offence provision.

Appropriate payment and fair contractual practices by all parties in the contractual chain, including those at the top of the chain, is critical for the ongoing financial viability of the construction industry.

To achieve this, Master Builders believes security of payment and fair contract legislation should be amended to ensure head contractors are given equivalent protections, when dealing with developers, as those afforded between builder and subcontractor. Specific initiatives to achieve this equivalency are provided in the remainder of this submission.

## **(2) SECURITY OF PAYMENT**

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### **2.1 – Project trusts**

#### **Master Builders position**

**Where a project trust obligation is imposed on a head contractor, the developer is also required to operate through a project trust arrangement for the protection of the head contractor.**

The project trust regime is at this stage untested as to its ability to reduce insolvencies or otherwise improve security of payment outcomes, including payment of progress payments when they fall due. However, the prospects of its success are substantially reduced by the fact that the project trust obligation does not apply to the top level of the contractual chain (i.e., the developer).

The benefits of applying the project trust obligation to head contracts include:

- 1) It will ensure progress payments owed by the developer to the head contractor are held in trust for the head contractor. This in turn supports the ongoing financial viability of the head contractor, including their capability to pay subcontractors and other creditors.
- 2) It will assist in addressing late payment practices routinely adopted by many developers, as they will be subject to the “top-up” and other obligations of trustees stated in the BIF Act.
- 3) It will assist in addressing power imbalances in the contractual relationship between the developer and head contractor.

These benefits are further articulated below.

#### **Benefit 1: Ongoing financial viability of contractor**

For cashflow to appropriately flow throughout the contractual chain, it is critical that the originating source of the cash flow be protected. Put simply, imposing project trusts obligations to protect progress payments between the head contractor and the subcontractor is of limited utility if there is no legislative mechanism to also secure payments flow from the developer to the head contractor.

The current legislation provides no protection of this kind for head contractors. Its failure to do so prejudices the financial viability and cashflow of all down-stream contractors, including subcontractors and suppliers. In view of this, Master Builders believes that project trusts should apply from the top of the contractual chain.

### **Benefit (2): Late payment**

Members have identified that late payment (as opposed to non-payment) is a common issue when contracting with developers. Some members estimate that two-thirds of progress payments are paid after the due date for payment, including those envisaged in legislation.<sup>1</sup>

Some of the key drivers of late payment practices include:

- Inadequate financial management practices by some developers,
- Arrangements with financiers that make it impossible for developers to meeting progress payment due dates.
- The impracticality for many head contractors (particularly smaller builders) to enforce their contractual rights through adjudication and the courts system.

The application of the project trust regime to developers would assist in improving late payment practices as it would provide a further incentive for developers to put in place appropriate payment and finance arrangements. These incentives include the avoidance of an adverse audit finding by the QBCC and the application of relevant offence provisions in the BIF Act.

### **Benefit (3): Power imbalance**

Members have identified that the exclusion of developers from the project trust regime in some instances results in a contractual power imbalance between the developer and builder.

The imbalance arises because of the statutory obligation for the head contractor to “top up” shortfalls in the project trust account when monies held in the trust are insufficient to pay amounts owed to subcontractors.<sup>2</sup> This issue tends to typically occur where there is a dispute at the final progress payment stage.

The source of the imbalance is that the head contractor must consider their financial ability to comply with the top-up provisions in the BIF Act when negotiating the dispute. Those head contractors unable to top up shortfalls in the project trust account may be inclined to “cut their losses” in the dispute and accept a lesser payment amount from the developer to that which they believe they are entitled.

Having project trust requirements also apply to the developer would assist in addressing this issue.

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<sup>1</sup> See section 67W (*Void payment provision in Commercial Contract*) of the QBCC Act.

<sup>2</sup> See section 51 (*Trustee to cover shortfalls*) of the BIF Act.

## 2.2 – Compulsory professional development

### Master Builders position

**Compulsory continuing professional development (CCPD) is introduced for contractors in Queensland as allowed for under the QBCC Act. The CCPD program should include learning outcomes relating to administering head contracts with developers and associated financial management practices.**

As stated in section 2.1, Master Builders members have advised that late payment of progress claims by developers is a common issue, particularly for smaller builders.

One of the contributing factors to this issue (in addition to those mentioned in section 2.1) is that less experienced head contractors may have insufficient understanding of one or more of the following:

- Best practice administration of commercial contracts between head contractors and developers.
- Managing cashflows and legislative requirements in a project trust environment.
- Financial and risk management practices for a successful business.
- Minimum financial requirements for licensing.

Section 116 (d) of the QBCC Act allows a regulation to be made that provides for continuing professional development to be undertaken by a licensed building contractor. Master Builders supports the making of an appropriate regulation under this provision to give licensed head contractors appropriate training in the above listed topic areas.

## 2.3 – Mandatory Disclosure

### Master Builders position

**Legislation is introduced to impose mandatory disclosure obligations on developers prior to entering a head contract. The mandatory disclosure obligations should include requiring the developer to provide relevant information to a prospective head contractor about:**

- **Financial arrangements for the project.**
- **Other development projects undertaken, or being undertaken, by the developer or its directors.**
- **History of proven regulatory actions taken against the development company, directors, the company secretary, and influential persons.**

To address and properly assess business risk prior to entering a contract, head contractors should ideally undertake a due diligence assessment of the developer's financial position, capability of paying

progress payments by their due dates, and the overall fitness and propriety of the developer's directors, secretary, and other influential persons.

There are a variety of reasons why a head contractor may not make due diligence inquiries about a developer prior to entering a head contract. These include:

- Contractors may be unwilling to ask for due diligence related information due to the power imbalance in their relationship with the developer, including risk of losing the tender/job.
- Contractors may not have the resources or knowledge to independently undertake the inquiries about the financial position of the developer or the fitness and propriety of its directors.
- Some information relevant to a due diligence assessment may not be publicly accessible information.

Master Builders supports the making of legislation to require a developer to disclose relevant due diligence related information to the head contractor, prior to entering a head contract for a development project. The disclosure obligations should include providing relevant information regarding:

- financial arrangements for the project.
- other development projects undertaken or being undertaken by the developer, including its company secretary and directors.
- any history of proven regulatory actions taken against the company's directors or influential persons (e.g., exclusions, bans or disqualifications from holding a QBCC contractor's licence).

See also discussion at paragraph 3.1 (QBCC approval of substantive development projects).

### **(3) DEVELOPER ACCOUNTABILITY**

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#### **3.1 – QBCC approval of substantive development projects**

##### **Master Builders position**

**Legislation is introduced for developers who do not hold a QBCC contractor's licence to be approved by QBCC to undertake a building development requiring a project trust arrangement. The pre-requisites for approval should include:**

- **The developer has the financial capacity to undertake the development and the necessary financial arrangements in place to ensure the head contractor is paid amounts owed under the contract within prescribed maximum legislative timeframes.**
- **An obligation for directors, secretary, and influential persons of the developer to meet fit and proper requirements akin to those applied to licensed head contractors.**

To mitigate the financial risk associated with building developments for head contractors, subcontractors, and consumers (e.g., those buying off the plan), it would seem appropriate there be some regulatory oversight of developers by the industry regulator.

At very least, QBCC should have independent oversight of substantive development projects to safeguard that a developer has the financial capacity to undertake the project and the necessary financial arrangements in place to pay progress payments within a maximum of 15 business days from submission of a payment claim (as envisaged in section 67W of the QBCC Act).<sup>3</sup> It would also seem reasonable that the regulator makes inquiries to satisfy itself that directors, secretary and other influential persons of the development company are fit and proper.

There are various regulatory options that could be used to achieve the above, including the implementation of a registration system for major developments.

However, if developers were made subject to project trust obligations (as recommended in section 2.1 of this submission), it may be possible to build in the oversight into the project trust process. For example, developers could be restricted from opening a project trust account for the head contract unless they hold a QBCC contractor's licence or otherwise hold an endorsement from the QBCC. The endorsement for the unlicensed developer would be subject to the QBCC being satisfied that the developer has demonstrated the requisite financial capacity and capability, and that all fit and proper obligations have been met.

Under the above model, a QBCC licensed contractor would not need a QBCC endorsement as they already must meet minimum financial requirements (including payment of debt obligations) and fit and proper requirements, as part of holding their contractor's licence.

## **3.2 – Unfair contract terms**

### **Master Builders position**

#### **Legislation is introduced prohibiting unfair contract terms in head contracts.**

Master Builders supports in principle the introduction of legislation that prohibits unfair contract terms in developer head contracts.

Generally, an unfair contract term includes a term that meets all the following:

- It causes a significant imbalance in the parties' rights and obligations.
- It is not reasonably necessary to protect the legitimate interests of the party advantaged by the term.
- It causes financial or other detriment to a party if it were relied on.

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<sup>3</sup> Section 67W(1) of the QBCC Act states "A provision in a commercial building contract is void to the extent it provides for payment of a progress payment by a contracting party to a contracted party later than 15 business days after submission of a payment claim."

However, it is also possible for a contract term to be unfair for other reasons including, for example, unfairness associated with intentional ambiguity and lack of transparency.

Examples of terms in a head contract that Master Builders has identified as being potentially unfair include the following.

No.	Term/Condition	Additional Comment
1	Clauses conferring power to assign and/or novate a contract to the detriment of the other party without that other party's consent.	
2	Indemnity clauses that excessively extend liability to the subcontractor	
3	Defects rectification by third parties' clauses	Excluding clauses relating to urgent rectification due to WHS reasons.
4	Collusion clauses prohibiting head contractors to consult with their industry association	
5	Clauses requiring the head contractor to pay a deposit before the head contractor can sue for breach of contract.	
6	Release upon claim made for progress payment clauses	Excluding clauses relating to final payment.
7	Warranties for design and document accuracy clauses	
8	Limited Liability-clauses that exclude or disproportionately limit the liability of the principal even if they are partially at fault.	
9	Clauses that prevent a supplier from offering a bank guarantee or similar surety as an alternative to cash retention.	
10	Obligation to accelerate work without compensation clauses.	

Also of particular concern to Master Builders is section 67GB (*Particular conditions void in building contracts*) of the QBCC Act. Under this provision, a building contractor must not enter a building contract that includes a prohibited condition prescribed by regulation. Failure to comply with the provision is an offence attracting a maximum penalty of 80 penalty units. However, the offence provision expressly excludes principals (and subcontractors) from its application.

At present, the Queensland Government is still in the policy development process to identify prohibited conditions that should be prescribed by regulation for section 67GB. If the section is not amended prior to the prescribing of a regulation to include principals within its ambit, head contractors will once again be disadvantaged and unreasonably excluded from protective legislation intended to promote best practice in the building industry.

### 3.3 - Ongoing accountability post project completion

#### **Master Builders position**

The QBCC's processes for issuing directions to developers to rectify or remedy building work are reviewed to ensure that developers are being held accountable where appropriate.

Section 72 of the QBCC Act allows the QBCC to issue a direction to a person who carried out defective or incomplete building work to rectify the work. The section also allows the QBCC to issue a direction to remedy to a person who has carried out building work causing consequential damage. A direction may generally be given with 6.5 years after the building work was completed or left in an incomplete state, unless QCAT approves for it to be extended.

There is no doubt that a direction can be given to rectify or remedy work to a developer. This is because they fall into the class of persons who are taken to carry out building work under sections 71I(i) and/or(l) of the QBCC Act. The QBCC Act also provides for a publicly available developer register to record directions.<sup>4</sup>

Master Builders supports these provisions continue.

However, we have concerns that the QBCC may not be taking regulatory action to apply them. The basis for this concern is that the Master Builders is not aware of a direction to rectify or remedy ever being given to a developer. This view is supported by the fact that, despite the legislative requirements in sections 103B and section 103E of the QBCC Act for the QBCC to keep and publish a developer register recording such directions, the register does not appear to exist.

A review of the QBCC's policies regarding the issuing and enforcing of directions to developers is accordingly recommended. The purpose of the review would be to identify:

- Potential improvements in QBCC's policies to ensure that developers are held accountable for defective work, incomplete work, and consequential damage for which have caused (in whole or part).
- Any legislative or "practical roadblocks" that may be impacting on the effectiveness of the policies.

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<sup>4</sup> See section 103B, QBCC Act.