

## DEVELOPER REVIEW PANEL – DISCUSSION PAPER

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### 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 the options listed in Appendix A of the *Developer Review Panel – Discussion Paper* (the discussion paper), which was released for public consultation in November 2022. The submission focusses on those options in the discussion paper likely to impact builders and trade contractors.

### Licensing and associated regulatory options (options 1 and 2)

The licensing of developers is not supported, including associated regulatory options in the discussion paper that rely on licensing.

The introduction of a licensing regime necessarily results in a major restraint on trade for developers in Queensland. Risks associated with the initiative include a disincentive for development activity and investment in the State, as well as the potential for increases in the cost of residential and commercial development.

Master Builders generally supports licensing in those circumstances where there is verifiable evidence of a widespread market failure that can only be effectively remedied by a licensing system. However, very limited evidence has been provided in the discussion paper of a market failure of this kind.

For example, the discussion paper notes that the licensing of developers would allow minimum financial requirements to be imposed on developers, thereby ensuring they have a "financially sustainable business" and an "appropriate level of working capital". However, Master Builders does not agree that Queensland's minimum financial requirements laws achieve either of these outcomes. In addition, there is a lack of supporting evidence of the precise problem.

Based on information provided by our members, non-payment of building contractors by developers is not widespread in the industry. Further, while late payment of payment claims has been identified, in many cases this appears to be linked to the timeframes for payment used in the banking and finance sector being misaligned with legislation requirements for building contracts. Similarly, where Government is the developer, government processing

timeframes commonly exceed those allowed for in the legislation. Neither of these issues are likely to be resolved through licensing.

The extent of behaviour by developers to deliberately non-comply with building contract requirements is also unclear. The QBCC is empowered under its governing legislation to prosecute and take a range of regulatory actions where this type of behaviour by developers is identified and there is a resulting significant financial loss (see section 42E of the QBCC Act). However, Master Builders is not aware of any regulatory action ever being taken by the QBCC in this regard.

Other regulatory options exist in relation to unfair contract terms that do not require licensing. Should Queensland introduce any prohibited or mandatory contract terms those offences should extend to principals under the contract.

There is also no empirical evidence or data to support that licensing of developers will reduce defective work. Of relevance, the QBCC is the regulatory agency responsible for issuing directions to rectify defective building work, including defective work caused by developers. The QBCC Act also provides for a publicly available developer register to record directions of this kind. To date there have been no directions against developers published on the register.

While Master Builders does not support the introduction of a licensing regime for developers it does support government exploring voluntary accreditation of developers with a professional body, along with a code of conduct and continuing professional development.

If the Government ultimately decides that licensing, registration or increased regulatory oversight (project specific or otherwise) is warranted, Master Builders submits that it should be aligned with developers who undertake projects where a project trust account is required.

Master Builders also supports increased QBCC intervention to ensure enhanced regulatory accountability of those developers who behave contrary to existing legislative requirements. In this regard, Master Builders recommends QBCC review its operational policies to ensure they appropriately hold developers accountable in the event:

- a developer is responsible for the carrying out defective or incomplete work.
- a developer causes another party to a building contract to suffer a significant financial loss because of the person's deliberate non-compliance with the contract.

### **Developer ranking system (option 3)**

Master Builders does not believe there is sufficient evidence to support the introduction of a developer ranking system Queensland akin to that in NSW (ICIRT).

Prior to Queensland embarking on such a path, it is recommended that the Government undertake a detailed assessment of the costs, benefits and measurable outcomes achieved by the ICIRT system as it applies in NSW.

Unfortunately, the ICRT system is still relatively new, and it is not possible to do such a review at this early stage. However, Master Builders understands that the ICIRT system has so far proven to be a lengthy and expensive process for affected developers in New South Wales and that the commensurate benefit to the community at this stage is unclear.

It is also important to bear in mind that historically in NSW commercial builders, trade contractors and engineers were not required to be licensed or registered.

### **Disclosure arrangements (option 4)**

Master Builders supports legislative initiatives to improve the level of disclosure from a principal to a head contractor.

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 and capability of paying progress payments by their due dates. Inquiries to establish overall fitness and propriety of the developer's directors, secretary, and other influential persons would also be prudent.

There are a variety of reasons why a head contractor may resolve not to undertake due diligence inquiries. 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 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).

Master Builders also proposes that the principal under a building contract should have a legislative obligation to inform potential head contractors, prior to acceptance of tender, whether or not a project trust account will be required to be established for the project.

### **Expand project trust accounts (option 5)**

Master Builders supports the important principle that those who carry out building work should be promptly paid for their work when it is contractually due and owing. However, there is currently no evidence whether the Queensland project trust regime can achieve this outcome.

Of further concern is that the complexity, financial cost, audit requirements and restrictions on cashflow associated with the Queensland project trust system are likely to be financially unsustainable for smaller and medium size builders. This is particularly significant when the requirements expand to include \$3M projects on 1 April 2023 and \$1M projects 1 October 2023.

There are also ongoing implementation issues with the project trust system in Queensland that continue to be unresolved. These include:

- The Queensland Government and QBCC have been unable to identify any IT providers providing software that complies with the complex record keeping and system requirements prescribed in the legislation.
- Industry understanding and awareness of the project trust requirements remains low, including knowledge of the costs, impact on cashflow, and complexities associated with administering a building project through a project trust.
- Many builders are likely to be unable to absorb the additional administration, IT and other costs associated with project trusts in the existing economic climate. Relevant in this regard is that the industry is currently experiencing business sustainability challenges arising from subcontractor and materials shortages and delays.
- The legislation governing project trusts is overly complex and, in many cases, ambiguous as to the obligations and requirements imposed on trustees.

By way of general comment, Master Builders supports Government undertaking further work to review the existing project trust framework to resolve the above issues. In the context of developers, Master Builders supports the introduction of an obligation on developers to advise builders of whether a project trust is required prior to contract.

The prospects for success of the project trust initiative are also 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).

A much simpler project trust account regime such as that recommended by Murray could be considered to replace the existing Queensland framework.

The benefits of applying a project trust obligation to developers include:

- Progress payments owed by the developer to the head contractor are held in trust for the head contractor and not used for other purposes or projects.
- It will assist in addressing late payment practices routinely adopted by many developers, as they will be subject to the “top-up” and other legislative obligations of trustees.
- It will assist in addressing the builder/head contractor being the ‘meat in the sandwich’ in relation to payment obligations.

These benefits are further articulated below.

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

For cashflow to appropriately move through the contractual chain, it is critical to have a certainty of cash flow from the originating source. 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 places head contractors in an unenviable position of having obligations to ‘top up’ the project trust account if insufficient funds exist at the time of occurrence of a ‘liability’ to pay, but no obligations on the client/developer to hold money owing to the head contractor in a trust account. 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.

Some of the key drivers of late payment practices include:

- Arrangements with financiers that make it impossible for developers to meeting progress payment due dates.
- Where Government is the principal, standard approval process times in some departments and entities routinely exceed maximum due dates for payment prescribed in legislation.
- Inadequate financial management practices by some developers.
- The impracticality for many head contractors (particularly smaller builders) to enforce their contractual rights through adjudication and the courts system.

- The lack of regulatory activity by the QBCC in relation to obligations of developers (for example, developers are bound by legislative obligations to pay within a certain timeframe, yet do not appear to be subject to regulatory action such as random audits).

The application of the project trust regime to developers would assist in improving payment practices as it would provide a further incentive for developers to put in place appropriate payment and finance arrangements. However, this would require a commitment from the QBCC to enforce such obligations on developers.

### **Benefit (3): Builders as the ‘meat in the sandwich’**

Members have identified that the exclusion of developers from the project trust regime results in an imbalance of obligations.

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. This issue tends to typically occur where there is a dispute at the final progress payment stage.

For the head contractor to have this ‘top up’ obligation where the developer has no obligation to pay into a trust account puts the head contractor in a difficult position.

The head contractor must consider their financial ability to comply with the top up provisions when negotiating the dispute. Some head contractors 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.

## **Education and CPD (options 6, 22, and 25)**

As stated above, Master Builders members have advised that late payment of progress claims by developers is a common issue, particularly for smaller and some medium size builders. This in turn leads to the building contractor experiencing financial stress and increases the risk for non-payment of subcontractors, financial collapse, and regulatory and licensing intervention by QBCC.

Master Builders supports the introduction of compulsory professional development for developers and building contractors to assist in addressing the above issue and associated risks. The focus of the education should include 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.

Option 22 canvasses the possibility of third party quality assurance assessments being introduced as part of CPD for the sector and run by professional bodies post completion.

While Master Builders generally supports the introduction of CPD in Queensland, endorsement of specific proposals of this kind requires more detailed information as to content of the proposal, including an assessment of feasibility and associated costs to deliver.

Master Builders supports the policy position canvassed in option 25 that CPD programs should be “modern and fit-for-purpose”.

### **Tendering and contracts (options 7-15, 20-21)**

The discussion paper contains a range of options intended to amend the tendering and contractual arrangements for development projects through legislative and government policy reform.

The introduction of legislation that seeks to hinder the freedom of commercial entities to tender and contract is not something that should be taken lightly. Aside from the need to establish that there is a market breakdown that can only be resolved through legislation, there is also a need for careful consideration of the contractual complexities underpinning the issues that are being sought to resolve, including the potential for unintended consequences.

Such detailed analysis and consideration have not been included in the discussion paper.

Master Builders submits that the options under consideration would be best assessed by a specialist Ministerial Construction Council (MCC) subcommittee. It is also noted that the MCC Subcommittee on Fairness in Contracting has recently considered many of the options canvassed in the discussion paper. The subcommittee delivered its report to the Ministerial Construction Council in December 2022. Master Builders provided a letter setting out its views, annexed to that report.

### **Mediation and alternate dispute resolution (options 27-32)**

Master Builders supports initiatives to broaden, review, and improve the range of alternate dispute resolution and mediation options available to parties to resolve payment disputes fairly and promptly.

Master Builders also supports expanding the adjudication system to encompass consumers of domestic building work, including consumers who are engaging in residential property development activities.

### **Increasing reporting obligations (option 16)**

Master Builders does not support the introduction of legislation to compel quantity surveyors, project trust administrators, superintendents, and other participants in the construction process to report to the QBCC their beliefs and suspicions about incidents of non-payment of debts by developers and building contractors.

Legislation that seeks to introduce mandatory “thought reporting” and “thought policing” is understandably controversial by its very nature and polarising. The introduction of the



necessary offence provisions to support such a policy initiative would also be impracticable to enforce, unlikely to be ever used, and create an environment that encourages the reporting of frivolous matters to the QBCC.

This policy initiative, if introduced, is also likely to complicate and negatively impact the effectiveness of alternate dispute options, including mediation to resolve contractual and building disputes (which inevitably involve payment issues).

## **NCBP Legislation (options 17 and 19)**

Options 17 and 19 propose to extend the “chain of responsibility” in Queensland NCBP legislation to include developers and building certifiers.

It remains unclear from the commentary in the discussion paper why it is believed that developers are not already adequately captured by the existing legislation.

Specifically, section 74E states who is a person in the chain of responsibility for a building product. The provision is expressed to include a person who “installs” the product in a building in connection with relevant work. The term “install” is given a very wide definition in section 74AA of the QBCC Act. It includes a person who engages a person to “carry out” the relevant building work in relation to which the product is installed in a building (in addition to the person who carried out the building work). This broad definition would appear to encompass a developer who contracts with the builder to carry out the building work for the project.

It is unclear whether building certifiers are within the chain of responsibility for NCBP as defined in section 74E. It depends on whether the term “carry out” (as defined in schedule 2 of the QBCC Act in relation to building work) extends to the certification functions performed by a building certifier under the Building Act.

Further, the broader policy issue as to whether building certifiers should be captured under the chain of responsibility also requires substantively more research and investigation than is provided in the discussion paper. Key policy matters that need to be considered include the existing obligations on certifiers, the impact on the availability and cost of insurance for building certifiers and whether it is fair and reasonable to expect that a building certifier could identify a non-conforming building product as part of the certification process.

Arguably it is manufacturers, importers and suppliers who should bear responsibility for non-conforming products and product information. A product assurance framework strengthening product information and traceability requirements would be a better regulatory framework. Should a professional architect or engineer specify an incorrect product, that would presumably be covered by existing regulation and professional bodies. If a builder or trade contractor incorrectly uses a building product, that would presumably be defective building work and covered by other requirements.



## **Building certifiers (options 23 and 24)**

Master Builder generally supports the regular review of legislation by Government to ensure it continues to be fit for purpose and does not impose unnecessary regulatory burden and cost on industry and the community. Accordingly, Master Builders does not have concerns about proposals to review legislation and regulatory practices suggested in various parts of the discussion paper, including the proposed review stated in option 23.

Consistent with the above, Master Builders supports the Government reviewing guidelines published under section 258 of the *Building Act* to help achieve compliance with the Building Act, including the guidelines currently published for inspection of class 2 to 9 buildings. For example, there is scope to provide more detail and examples in the current inspection of class 2 to 9 buildings guideline which in turn may better assist building certifiers in their functions.

Before deciding whether the current risk-based approach to inspections should be replaced or enhanced by requiring mandatory inspections (as envisaged in option 24), it is recommended that a detailed policy analysis be undertaken that includes reference to the costs, benefits, and practical implications of any changes under consideration. Such analysis is not included in the discussion paper.

## **Additional insurance (option 26)**

This option is currently under consideration by the Ministerial Construction Council (MCC). It is a complex issue that requires actuarial analysis to identify its cost feasibility, reasonable availability of reinsurance, and overall achievability.

This work is currently being undertaken by a subcommittee of the MCC. Master Builders would prefer not to indicate its support for the proposal until the work of the subcommittee is completed.

## **QBCC Audits (option 27)**

Under this option, legislation would be amended to give QBCC the power to conduct audits of buildings before a certificate of occupancy is given.

Unfortunately, there is insufficient detail in the discussion paper as to basis for the belief that QBCC needs further investigative powers to enable it to audit a building for defective work prior to the issuing of a certificate of competency.

Master Builders' understanding is that the QBCC already has broad powers to allow it to enter building sites during construction to investigate whether defective work has been or is being carried out. See for example section 105 of the QBCC Act.

By way of general comment, Master Builders supports the collaborative work currently being undertaken by the Technical Services Unit of the QBCC. The Unit proactively works with building contractors during construction to provide education and guidance regarding compliance with building standards and regulatory requirements.

### **Line of sight to contractors (option 33)**

The paper states this option 'would ensure owners are provided with, or have access to, information about the head contractor and subcontractors who worked on the building before sale or as part of the sale contract'.

If this is information such as name and licence number, Master Builders does not object.

However, if additional information is proposed, requiring head contractors to collate information from all subcontractors to provide to the developer, Master Builders would not support this on the basis it is additional administrative burden for builders with no proven benefit.

### **Documentation at handover and digital tools (options 34 and 35)**

Master Builders supports efficient methods of collecting useful data. Industry participants must be adequately compensated if additional scope is required. Provided the scope of any additional work expected to be performed by head contractors is included in the building contract, it can be priced accordingly.

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