

Master Builders Hot Topic Survey increasing the 5% deposit

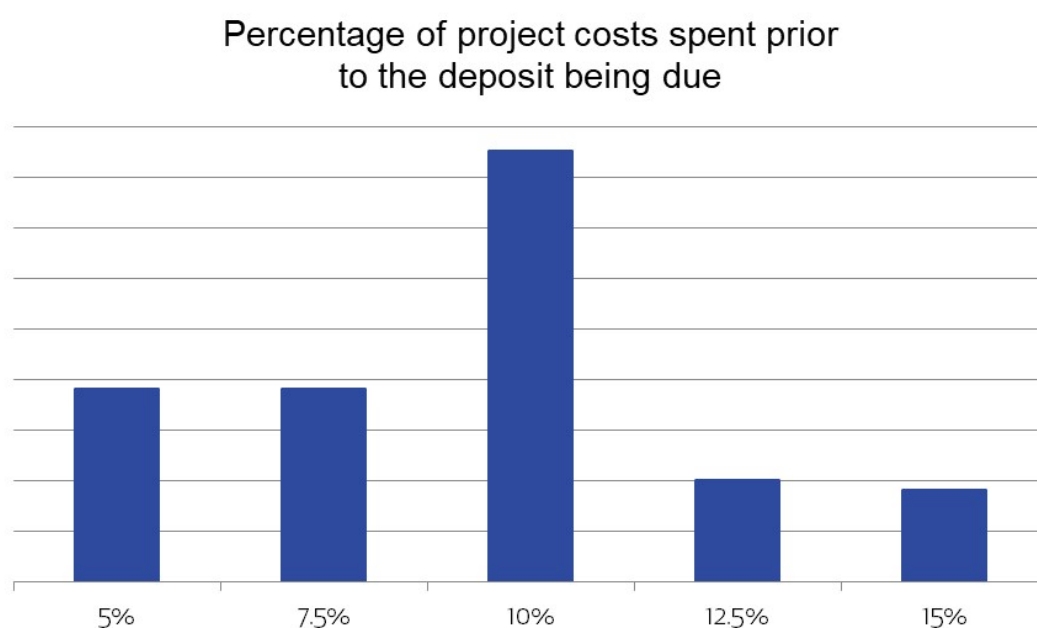
Master Builders surveyed members to understand whether there is a case for increasing the 5% deposit allowed on domestic building contracts¹.

The deposit payment that can be taken under a domestic building contract for projects \$20,000 and more has been capped at 5% since 2000.

The survey results confirm that in the 20 years since the rule was introduced there has been a substantial increase in both the scale and the cost of tasks performed at the pre-construction stage. And that the 5% cap is creating significant challenges for businesses.

Current Situation

Four out of five respondents spent more than 5% of the project cost prior to the deposit being due, with nearly half agreeing that 10% was the expected spend prior to the first payment.



The costs that are payable prior to receiving the initial deposit or on contract signing include:

¹ Domestic Building Contracts Act 2000

- quotation costs (site visits, client meetings, printing plans, consultation meetings, estimation)
- overheads (staffing, office, equipment, QBCC licensing costs, advertising & sales commission)
- contract documentation
- surveyor (boundaries & contours) / survey plan
- Underground Services Survey
- preliminary Council check
- soil report
- engineering
- building plans
- plumbing & drainage plans
- energy efficiency report
- product specification
- building approval
- material and sub-contractor deposits
- QLeave Levy
- Home Warranty Scheme premium.

Depending on the site and the project there may also be a number of other early expenses necessary for a successful build. These include:

- site specific design (bushfire, flood, acoustics, slope, coastal area etc)
- Council siting variations (relaxations)
- water/sewer connection fee
- effluent disposal report
- percolation reports/septic design if non-sewered site
- demolition approval
- environmental requirements
- construction insurance (when requested by client's bank prior to start of construction)
- public liability insurance.

"On some projects we can spend at least 3 to 5 times the deposit value to get to the first progress payment stage."

"The majority of supplies need to be ordered as soon as possible once the contract is signed. This amount can add up way above the 5% threshold." "Windows and joinery are asking up to 50% deposit."

The situation can be exacerbated by the lending policies of banks. Banks are also unwilling to be flexible with progress payments and will not accept a varied payment schedule.

"Buyers do not part with deposit until the lender gives them approval which can take weeks."

The time taken to get a project to contract signing and the deposit being payable has increased in recent years further exacerbating the situation. For a third of respondents the increase in time has been significant.

"Our staff spend a significant amount of time with clients prior to contract signing - often months of site visits, client meetings, selections, liaison with third-parties and council to obtain approvals, etc. and there is no guarantee that the client will proceed to contract signing."

A preliminary agreement is one strategy that builders can use to cover the initial costs but this increases time, paperwork and cost for each project.

Impact

The impact the 5% deposit cap at this is having on construction businesses is significant.

The challenges to the cashflow and the resulting financial stress was the most common theme. Cashflow problems can also lead to project delays, impacting when material and sub-contracting orders can be placed.

"It can be a challenge to fund the work until you get to the first progress payment, particularly when there is large amounts of materials to purchase etc and labour costs."

"It's impacting a lot on the cash flow, where again you can run in to trouble with QBCC."

"If its a bigger job, the 5% deposit rule can negatively impact business proceedings for months. This is also assuming that the client doesn't delay on future payments."

This exposes the business to greater risk which may have knock effects for security of payment.

"On a couple of occasions when the client has not gone ahead with the contract prior to the slab progress payment, we have lost money on the project."

And adds financial costs to running the business.

"It means that the business is now carrying the build, in essence we have become the bank."

And the impacts are felt more keenly by small business.

"Running a small business is all about cash flow and the 5% has never been enough. It puts us behind the eight ball from the start."

"Stretches the liquid funds of the business, as I'm only a small family business, basically pushes small guys out of the market and the already established businesses gain a monopoly by default. It is a bit of a tilted system."

“Being a small business and a sole trader it has a huge impact. For example on our last job the 5% deposit was roughly \$18,450. Our window company wanted \$32,000 deposit upfront to order windows/doors as being a sole trader (who has never been late on an account payment). Our timber company wanted \$12,000 to order the timber which needed to be paid on placing the order. These orders need to be placed immediately due to processing times and when those products are required onsite. We carry these costs until the draw can be made as the stage payments rarely will cover these amounts before their stage. With windows/doors being enclosed stage this was over six months on this job. Add to that administration for contracts, Q Leave levy, home warranty insurance, certifiers fees etc we are expected to carry a huge amount of expense and essentially act as the bank for the works for large amounts of money.”

“We are forever chasing, stressing about the works being completed.”

It can stifle business growth.

“It has an impact on capital and staff resourcing investment decisions.”

If businesses are pushed to cutting corners on any of the early expenses it may have ramifications of the quality of the product.

“It diminishes our capacity to do more extensive pre works - such as administrative and WHS works etc.”

“It’s frustrating to rush to a slab stage to get to break-even point.”

Conclusion

“I understand we are supposed to do the work prior to getting paid but we should not be doing works on a project with no money down to start the actual digging. If the government are forcing security of payment on builders, why are we having to float a build from inception. There needs to be a bit more money down to ensure that we can cover costs especially ones that can't be floated on an account such as wages and subbie costs.”

“We should not have to carry upwards of 35% of project for the first quarter of the project when we have only received 5% ourselves.”