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ABOUT THE HOUSING INDUSTRY ASSOCIATION

The Housing Industry Association (HIA) is Australia’s only national industry association representing the interests of the residential building industry, including new home builders, renovators, trade contractors, land developers, related building professionals, and suppliers and manufacturers of building products.

As the voice of the residential building industry, HIA represents a membership of 60,000 across Australia. HIA members are involved in land development, detached home building, home renovations, low & medium-density housing, high-rise apartment buildings and building product manufacturing.

HIA members comprise a diverse mix of companies including residential volume builders, small to medium builders and renovators, residential developers, trade contractors, building product manufacturers and suppliers and allied building professionals that support the industry.

HIA members construct over 85 per cent of the nation’s new building stock.

The residential building industry is one of Australia’s most dynamic, innovative and efficient service industries and is a key driver of the Australian economy. The residential building industry has a wide reach into manufacturing, supply, and retail sectors.

Contributing over $100 billion per annum and accounting for 5.8 per cent of Gross Domestic Product, the residential building industry employs over one million people, representing tens of thousands of small businesses and over 200,000 sub-contractors reliant on the industry for their livelihood.

HIA exists to service the businesses it represents, lobby for the best possible business environment for the building industry and to encourage a responsible and quality driven, affordable residential building development industry. HIA’s mission is to:

“promote policies and provide services which enhance our members’ business practices, products and profitability, consistent with the highest standards of professional and commercial conduct.”

HIA develops and advocates policy on behalf of members to further advance new home building and renovating, enabling members to provide affordable and appropriate housing to the growing Australian population. New policy is generated through a grassroots process that starts with local and regional committees before progressing to the National Policy Congress by which time it has passed through almost 1,000 sets of hands.

Policy development is supported by an ongoing process of collecting and analysing data, forecasting, and providing industry data and insights for members, the general public and on a contract basis.

The Association operates offices in 22 centres around the nation providing a wide range of advocacy, business support services and products for members, including legal, technical, planning, workplace health and safety and business compliance advice, along with training services, contracts and stationary, industry awards for excellence, and member only discounts on goods and services.
1. INTRODUCTION

In February 2020, the Australian Small Business and Family Enterprise Ombudsman (ASBFEO) released a position paper inquiring into supply chain finance (Position Paper). The Position Paper follows a previous inquiry by the ASBFEO examining payment terms, times and practices (Payment Times Inquiry), media articles late last year that highlighted examples of the use of supply chain finance arrangements and comes just prior to the release of the exposure draft Payment Times Reporting Bill 2020 (Payment Times Reporting Bill) for consultation.

HIA understands that the Position Paper seeks to examine the use of Supply Chain Financing (SCF) by larger businesses and its impact on small business. The Position Paper would also seem to traverse areas previously raised by the ASBFEO during the Payment Times Inquiry that has been the subject of further consultation by the Department of Jobs and Small Business and are addressed by the Payment Times Reporting Bill. This overlapping consultation is undesirable.

HIA does not support conduct that involves adopting deliberate and calculated business practices which seek to avoid paying any business, not just small businesses, on time. However, legitimate and legal avenues available to businesses to respond to risks should not be stifled. As outlined in the Position Paper SCF can act as a positive tool for all parties to commercial arrangements.

To that end, some of the findings and recommendations outlined in the Position Paper are concerning. For example, the finding that the definition of small business is manipulated for nefarious purposes is largely unsubstantiated. Equally, recommending that the minimum standard for all supplier payments (regardless of size) should be 30 days fails to acknowledge that there will be legitimate reasons for both longer and shorter payment times which will be influenced by a range of internal business and external regulatory factors, some of which the business may have very little control over.

The Position Paper also omits not only a range of matters relevant to payment arrangements including security of payments and unfair contracts laws but also a range of industry specific circumstances. Regarding the latter, HIA’s submission is made within the context of the unique circumstances faced by the residential building industry.

The residential building industry is heavily regulated when compared to other building sectors and other sectors of the economy, for example home builders must manage a complex web of national, state and local laws, regulations and codes. These range from planning, design, environment, health and safety, to local authority inspection and certification and a multitude of building, electrical, mechanical and plumbing processes.

Residential building businesses must also comply with a legislative framework that spans licencing of individuals and companies, ATO contractor reporting requirements, dispute resolution oversight, builders warranty obligations and contractual requirements.

These regulatory arrangements largely determine payment arrangements in the industry. HIA would caution against any moves that would further restrict a residential building business’ ability to manage their risk or set payment arrangements with subcontractors.

HIA appreciates this opportunity to respond to the Position Paper and is open to working with the ASBFEO on these matters in the future.
2. THE RESIDENTIAL BUILDING INDUSTRY

The residential building industry, including the home improvements and alterations market, is a key component of the Australian economy. The residential building industry is also the dominant sector in the building and construction industry.

The Position Paper does not seek views on the impact of SCF, the consequences of a consistent definition of small business or the imposition of mandatory payment terms on specific industries. HIA considers that an investigation of that nature is necessary and critical.

The practice and paradigm in the residential building industry differs significantly not only from businesses operating in different sectors but also when compared to those businesses operating in commercial and civil construction. These differences have implications for the matters raised in the Position Paper.

The terms and conditions for commercial builders and those engaging in government contracts are significantly different from the terms and conditions for a builder working on a residential building project.

Commercial projects and government works are generally characterised by:

- a tendering process that often forces negative margins with the hope that future variations will cover the shortfall;
- the use of retentions;
- longer payments terms (up to between 45 and 60 days compared to 5 to 21 days in residential);
- limitations on a builder’s ability to select subcontractors;
- contract administration by a superintendent/architect;
- significant amounts for liquidated damages; and
- long defects liability periods.

Such elements are not present in the residential building environment, which faces equally as challenging, yet different, factors with respect to payments such as:

- the homeowner, whose significant emotional and financial investment places additional pressures on the builder and trade contractors;
- prescriptive statutory contractual arrangements;
- quasi regulation of payment terms through the involvement of financial institutions;
- ineffective, time consuming and often litigious methods of recouping late payments;
- demanding terms of trade from suppliers; and
- significant exposure to uncontrollable events such as inclement weather and fluctuations in the supply and hence price of building materials.

2.1 RISK ALLOCATION

HIA supports the Abrahamson Principle, namely that ‘a party to a contract should bear the risk where that risk is within that party’s control’.

However the statutory consumer protection frameworks established around the country distort the usual allocation of risk in favour of home owners, influencing the payment arrangements that home builders enter into with their subcontractors. Proposals within the Position Paper also seek to affect the risk allocation of parties to commercial arrangements.
While residential home building laws differ around the country residential builders are generally required to incorporate a number of mandatory terms and conditions into their contracts for the benefit of home owners. For example a contract with a home owner must include:

- mandatory terms and conditions such as the name of the parties, a description of the building works, the contract price and any plans and specifications;
- variations must be in writing. If these requirements are not strictly complied with a builder may not be paid for the variation;
- implied warranties of materials and workmanship;
- limits on deposits and bans on up front progress payment;
- limits on the estimated amounts of prime costs and provisional sums;
- requirements that builders take out warranty insurance; and
- outlawing and/or voiding unconscionable contractual provisions.

It is generally accepted practice in the residential building industry for the builder to claim payment from the client upon defined progress stages being completed. With the exception of the deposit, it is uncommon for builders to claim in advance of work being undertaken. In fact, draw downs on project finance is normally only available upon lenders being satisfied with completion of certain recognised building stages.

There are significant cost implications on the residential builder associated with these regulations.

The cyclical nature of the residential building industry is relevant to the relationships between contracting parties.

The high cost and highly regulated nature of the industry together with the small business profile of firms also means that they are especially susceptible to economic cycles and changes in government policies and regulation.

There are also inherent uncertainties in contract prices which arise from the fact that works are required to be priced before construction commences and are based on technical, financial and workforce assumptions, together with material costs/availability, access to site, timeframes, weather and statutory approvals/delays.

Finally, a consistent challenge for builders is maintaining cashflow under a negative cash flow model. Whilst a trade contractor is typically paid for work in arrears and must finance this cost, the same holds true for builders who must ‘finance’ an owner’s costs.

Subcontractors and suppliers will naturally not wait for the substantial client to builder payment late in the duration of the job and often builders must source other financing arrangements to keep cash ‘flowing’.

Builders in the residential building industry ordinarily fund their works by way of debt financing. Revenue on the other hand is derived from client payments which are highly regulated and paid after completion of work and after the building costs are incurred.

The builder’s reliance on cashflow to manage operations and cyclical conditions exposes them to an even greater extent in the event of non-payment by a client.

The failure to take account of these factors, or even acknowledge that there may be industry specific circumstances that may impact, for example, SCF arrangements is a significant omission from the Position Paper.

SCF may offer a tailored and unique solution to the financial challenges and regulated risk allocation in the residential building industry. To that end while HIA sees value in the suggestion made in the Position Paper to review SCF arrangements from a competition and financial product perspective, more information is needed regarding the use and impact of SCF in the economy and across specific industry sectors.
3. EXISTING REGULATORY ARRANGEMENTS

3.1 THE ACCC

Unfair Contracts Laws

On 16 November 2016, the unfair contract term protections in the Australian Consumer Law (ACL) were extended to small business. Of note, these laws are currently under review.

These provisions are aimed at remedying an imbalance between parties, based on the perceived strength of the bargaining power between large and small businesses. Under the ACL an unfair term is defined as one that causes an imbalance in the parties’ rights and obligations that goes beyond what is reasonably necessary to protect the legitimate interests of the party relying on the clause.

In the Government’s response to the ASBFEO Inquiry into Small Business Payment Times and Practices it was noted that:

‘…the ACCC is monitoring complaints about payment terms and unfair commercial practices that delay payment times for suppliers. This includes terms allowing large businesses to unilaterally alter their payment terms and unfairly delay payment times for their suppliers.’

HIA sees actions by the ACCC through existing unfair contracts laws as serving more utility than the proposed recommendations in the Position Paper. To that end the review of unfair contracts laws currently on foot should take precedence over the measures outlined in the Position Paper.

The role of the ACCC in relation to SCF

Questions in the Position Paper that seek views regarding the role of the ACCC in taking steps against third line forcing or unconscionable conduct in relation to SCF arrangements are inappropriate. Both are serious breaches of the ACL and require significant evidence in order to substantiate an allegation.

Third line forcing occurs when a business will only supply goods or services, or give a particular price or discount on the condition that the purchaser buys goods or services from a particular third party. If the buyer refuses to comply with this condition, the business will refuse to supply them with goods or services. Notably exclusive dealing will only break the law when the conduct has the effect of substantially lessening the competition in the relevant market.

Unconscionable conduct does not have a precise legal definition. Conduct may be unconscionable if it is particularly harsh or oppressive. To be considered unconscionable conduct it must be more than simply unfair—it must be against conscience as judged against the norms of society. According to the ACCC business behaviour may be deemed unconscionable if it is particularly harsh or oppressive and is beyond hard commercial bargaining.

As per the normal course, the role of the ACCC is to respond to information they receive about arrangements that may involve anti-competitive behaviour. This would apply to SCF arrangements or any other arrangement the ACCC believes may require investigation on the basis that it may be anti-competitive.
3.2 SECURITY OF PAYMENT LAWS

Since 1999, security of payment (SOP) legislation for the construction industry has been progressively introduced into all Australian jurisdictions.

The common objective of this legislation has been to improve cashflow down the contractual chain. It effectively establishes a default entitlement to payment.

Under these laws:

- the subcontractor has a statutory right to a progress payment;
- the builder/principal is liable for claimed amounts irrespective of what the contract provides;
- the subcontractor may suspend work or supply without liability, and, if the principal removes any part of the work or supply from the contract as a result of the suspension, the principal is liable for any loss or expense the contractor suffers;
- the subcontractor can exercise a lien in relation to the unpaid amount over any unfixed plant or materials supplied;
- there is an expedited dispute resolution procedure (adjudication) by which disputes concerning payment are resolved, usually by way of written submission, within a very short period of time;
- if a principal becomes liable for an amount under SOP laws, then, in addition to recovering the amount as a debt due to the contractor, the adjudication determination may be enforced as if it were a court judgment; and
- there are very limited appeal rights or rights of judicial review in respect of an adjudication decision materials supplied by the contractor for use in connection with carrying out construction work.

The remedy of rapid adjudication is not available for a residential builder in dispute with a client. This has potentially undesirable implications for payment arrangements throughout a residential builders contacting chain.

Clauses in building contracts that offend the SOP legislation are void – contracting out of the laws is prohibited.

There are time limits for payments to subcontractors and a principal contractor/builder cannot require that payment to a subcontractor be withheld or delayed due to payment from the client not yet being received. This has codified the common law position that ‘pay when paid’ and ‘pay if paid’ clauses are void in respect of contracts for construction works performed or related goods and services supplied in Australia.

In HIA’s experience SOP legislation has provided an effective mechanism for payment for those subcontractors who have availed themselves of the laws. However and notwithstanding the existence of SOP laws some subcontractors continue to work for builders and principals when they have not been paid for a number of outstanding progress claims. This choice to continue to work even when substantial sums are already outstanding and when there is therefore an increased exposure to greater losses in the event of insolvency, is often based on a balanced assessment of risk and essentially is a commercial decision of these firms.

There also are a number of building firms who continue to undertake work for a consumer or home owner notwithstanding a failure to pay current or previous progress claims by that owner. As noted above, unlike subcontractors they do not have access to SOP or rapid adjudication to remedy cashflow issues in this regard.

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3 Except in Tasmania
Below is a table setting out the security of payment protections:

<table>
<thead>
<tr>
<th>State</th>
<th>Legislation</th>
<th>Maximum time period for payment of progress claims</th>
<th>Paid when paid clauses</th>
</tr>
</thead>
<tbody>
<tr>
<td>ACT</td>
<td>Building and Construction Industry (Security of Payment) Act 2009 (ACT)</td>
<td>10 days after a payment claim</td>
<td>Void</td>
</tr>
<tr>
<td>NSW</td>
<td>Building and Construction Industry Security of Payment Act 1999 (NSW) (NSW SOPA)</td>
<td>20 days to a subcontractor, 15 days by a principal to a head contractor.</td>
<td>Void</td>
</tr>
<tr>
<td>SA</td>
<td>Building and Construction Industry Security of Payment Act 2009 (SA)</td>
<td>15 days after a payment claim</td>
<td>Void</td>
</tr>
<tr>
<td>NT</td>
<td>Construction Contracts (Security of Payments) Act 2004 (NT)</td>
<td>20 days</td>
<td>Void</td>
</tr>
<tr>
<td>Qld</td>
<td>Building Industry Fairness (Security of Payment) Act 2017 Queensland Building and Construction Commission Act 1991 (QLD)</td>
<td>25 business days after submission of a payment claim for construction management trade contract or subcontracts. For commercial building contracts, 15 business days after submission of a payment claim.</td>
<td>Void</td>
</tr>
<tr>
<td>Tas</td>
<td>Building and Construction Industry Security of Payment Act 2009 (Tas)</td>
<td>10 days</td>
<td>Void</td>
</tr>
<tr>
<td>Vic</td>
<td>Building and Construction Industry Security of Payment Act 2002 (Vic)</td>
<td>20 days</td>
<td>Void</td>
</tr>
<tr>
<td>WA</td>
<td>Constructions Contracts Act 2004</td>
<td>42 days</td>
<td>Void</td>
</tr>
</tbody>
</table>

Recent changes in Queensland also mean that a failure to respond to a claim for payment can result in the imposition of penalties and/or disciplinary action and may have consequences for a contractor’s license. Further, compliance with minimum financial requirements in Queensland are a license condition and require that:

‘a Licensee must at all times pay all undisputed debts as and when the debts fall due and within industry trading terms’.

In NSW under the Contractors Debts Act 1997 subcontractors (or supplier of building materials) who have not been paid by a contractor can, in some cases, obtain payment directly from the principal. The rights under this legislation are expansive. For instance, the subcontractor is able to freeze monies in the hands of the principal (client) so that the principal does not pay the money to the contractor (builder) until the subcontractor has had the opportunity to obtain judgment of the amount owed by the contractor to the subcontractor.

The laws in NSW also enable subcontractors to earmark money which may become payable by the principal contractor to the subcontractor through rapid adjudication under the security of payment legislation and require a head contractor to submit a supporting statement with a payment claim to a principal. A supporting statement requires that a head contractor declare that all payments due and owing to subcontractors have been paid and identifies any disputed amounts that have not been paid. Penalties apply for failing to provide a supporting statement and making a false declaration.

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4 The Draft Building and Construction Industry Security of Payment (Review Recommendations) Amendment Bill 2020 proposed to reduce this to 10 days.
5 See Division 2A NSW SOPA
6 See section 13(7) NSW SOPA and Schedule 1 Building and Construction Industry Security of Payment Regulation 2008. This is also proposed to be adopted in SA and Qld.
7 See sections 13(7) and (8) NSW SOPA
4. RESPONSE TO QUESTIONS

4.1 DEFINITION OF SMALL BUSINESS

a) For consistency, should there be a single definition of small business for payment terms?

b) If so, what should that definition be? (For example, $10m turnover?)

In HIA’s experience, businesses do not attempt to ‘manipulate the definition of small business’ to suit their own ends. It may be appropriate, and indeed preferred, to allow larger businesses the flexibility to determine who is a small business in their particular industry or for a particular purpose. For example for many businesses in the residential building industry, it is not unusual for a relatively large building company to have relatively few employees as the majority of on-site construction activity is performed by independent trade subcontractors.

These businesses are not and should not be considered ‘small businesses’. On this basis HIA does not support a definition of small business based on a headcount approach.

Further it is clearly difficult, if not impracticable, for any business to know whether or not the business they are contracting with is a ‘small business’ for the purpose of a definition.

HIA prefers a multi-factor test be applied in order to determine a small business. Similar to the current approach adopted under the unfair contracts provisions of the ACL a small business would be defined by:

- The upfront price payable under the contract; and
- The turnover of the small business.

As such, HIA takes issue with the characterisation in the Position Paper of applying both a head count and turnover requirement as ‘not in the spirit of paying small businesses within 30 days’ and as an example of an ‘extreme case’ of large businesses trying to avoid the classification of a business as a small business. There are legitimate, reasonable and sensible reasons why a multi-factor test may be the most appropriate way of identifying a small business. This approach seeks to balance the needs of all businesses in the interest of the broader economy.

The consideration of one factor (such as turnover) for such an important classification does not allow any flexibility to account for:

- Changes in economic conditions that will impact the expansion or contraction of a business.
- The way a business may structure themselves in order to either be (or not be) considered a ‘small business’.
- Incentives (or disincentives) for business growth.

4.2 ENFORCEABLE PAYMENT TIMES

a) Is there a need for a mandatory Supplier Payment Code?

HIA does not see that there is a need for a mandatory Supplier Payment Code.

HIA supports the needs of parties to residential building contracts to be paid for the work that they perform in a timely manner and in accordance with the contract. However, HIA does not support mandatory payment terms.

Such an approach prevents the efficient operation of the market for all businesses operating in the residential construction industry, HIA supports the general principle that parties should be free to contract and agree upon their own terms and conditions, including the terms and conditions of payment.
b) What role does the proposed Commonwealth Government’s Payment Times Reporting Framework have in:

i. Assessing payment terms performance when SCF is utilised; and

ii. Auditing and issuing fines or other sanctions for non-compliance?

According to the February 2019 Payment Times Reporting Framework discussion paper (Framework), the purpose of the Framework is four-fold:

1. To introduce a new national large business reporting framework for businesses with an annual turnover of over $100 million to publish payment information.
2. Improve the collection of information about the payment practices of large businesses and government agencies towards small business.
3. Make information about payment practices visible and easily accessible to small businesses and other interested stakeholders.
4. Minimise the compliance and administrative burden associated with the reporting framework for government agencies, large and small businesses.

On this basis, the Framework should play no role in inquiring into SCF or issuing sanctions. This would equate to a significant and unjustifiable overreach of the Federal Government’s 2018 November announcement.

More generally, HIA sees that the remit of the Framework should be a narrow one to deal with discrete and clear matters. At this stage SCF must undergo further investigation and consideration prior to any intervention or oversight by the Framework or any other mechanism.

4.3 30 DAY PAYMENT TERM STANDARD

a) For consistency, should there be an economy wide 30 day payment term mandated?

As outlined earlier, HIA supports the needs of parties to residential building contracts to be paid for the work that they perform in a timely manner and in accordance with the contract. However, HIA does not support mandatory payment terms. HIA supports the general principle that parties should be free to contract and agree upon their own terms and conditions, including the terms and conditions of payment.

An economy wide mandated payment term will have a plethora of undesirable consequences.

The approach ignores one of the bases on which a competitive market can operate. In commercial relationships, payment terms are a valid and often successful negotiating tool. To remove this option could not only lead to anti-competitive outcomes but could also stifle the efficient operation of various markets within the economy, particularly where other government interventions already exist to regulate.

For example, and as outlined above, SOP laws around the country impose limits on payment times and terms. Also noted above is that the residential building industry is heavily influenced by the state based consumer protection frameworks particularly in relation to the ways a builder can invoice a home owner. Imposing standardised payment terms could severely squeeze the cash flow of the builder, the consequence of which are not good for the builder, subcontractor, homeowner and the economy more broadly.

As outlined above in the building and construction industry payment terms varying considerably between sectors within the industry and there may also be reasons for differing payment terms between industries.

A blunt regulatory approach is ill advised given the clear complexities associated with payment arrangements.
4.4 SCF AS A REAL CHOICE

a) Should SCF be available to small business to reduce payment times from 30 days to better?

b) What forms of SCF are of the greatest benefit to small business?

Yes. As outlined in the Position Paper there are a number of advantages for small business if they wish to utilise SCF in cases where it is offered. As such any SCF that offers a subcontractor favourable terms in exchange for a discount should be seen as advantageous.

4.5 REGULATORY INTERVENTIONS

A number of questions raised at under items 5 and 6 (Appropriate coverage by accounting standards and further questions from competition & regulated financial product perspectives) seek to raise matters of oversight, intervention and/or regulation of SCF. HIA sees value in addressing these matters together.

Accounting Standards and other Regulators

As indicated throughout this submission, further investigation and information on the operation of SCF is required before ‘who has a role to play’ can be determined. The implications in the Position Paper is that the treatment of SCF arrangements for accounting and financial purposes is incredibly complex, requiring detailed consideration prior to any action being taken.

While clarity and certainty is preferred, this should not come at the expense of a fulsome investigation of the issues, complexities and parties involved.

Use of data

Data collected by businesses by way of SCF arrangements should be used responsibly. If information is to be collected and disclosed to third parties, the small business supplier should be advised of this when using the SCF arrangement.

Arrangements with the SCF company

The arrangement between a buyer of SCF and the finance company is a matter for those parties. Any contractual arrangements should be treated as confidential.

Further, there is no evidence to support the need for the contractual arrangement between a business and the SCF provider to be regulated in any way nor is there any evidence to support the need for the public disclosure of an interest rate or discount rate. These rates may have been determined and negotiated to reflect the specific circumstances of the individual companies based on, for example, the financial standing of that company. There is no legitimate basis on which these confidential business negotiations should be disclosed and may in fact jeopardise any beneficial terms secured.