

SOLVING THE NATIONAL CRISIS IN CONSTRUCTION





EXECUTIVE SUMMARY

The building and construction sector is in crisis, beset with a number of problems that have their foundations in deficient models of project delivery, flawed procurement methods and shoddy laws and regulation that do not protect consumers and workers.

AT THE apex of myriad problems in the construction sector is failing regulatory oversight, where outsourced building certification are the bedrock of a system which has seen staggering levels of non-compliant work approved.

These issues have underpinned a crisis in the nation's construction sector which has resulted in \$6.2 billion waste on residential apartment defects and around 170,000 apartments affected by flammable cladding.

National harmonisation of the application of the code could save an additional \$2.1 billion in defective building and administration fees.

The outsourcing of expertise does not stop in residential building. A lack of expertise has seen Australian governments waste \$10.8 billion in the last ten years, with warnings of a further \$5 billion set to be wasted in the next several years through appalling management of infrastructure projects.

The analysis by Equity Economics finds projects such as Sydney's Light Rail, Victoria's Regional Fast Rail and the new Royal Adelaide Hospital have run significantly over budget with substantial delays and quality issues as a direct result of State, Territory and Commonwealth Governments not retaining adequate expertise in the procurement of infrastructure projects.

Over the last 30 years state governments have divested themselves of the capacity to scope and manage major infrastructure delivery shifting the responsibility to the private sector. Their institutional knowledge and technical capacity dissipated and they now find themselves as 'uninformed purchasers' in major infrastructure projects. As a result they remain trapped in a 'cycle of waste' as poorly scoped work, leads to inferior construction, rectification, disputation, delay and cost overruns and ultimately to sub optimal outcomes for taxpayers.

The use of the Design and Contract model of delivery drives an adversarial culture which dilutes accountability and creates unsustainable downward pressure on costs between contractors in a manner that disadvantages workers and makes lifecycle costs of the project difficult to gauge.

This model also encourages the use of outsourced workers, which further divorces the project from the principal contractor, facilitating poor workmanship and compromising worker renumeration and entitlements.

Current legislation also failures to adequately protect whistle-blowers and their unions. As a result, substandard workmanship, non-complaint building materials or unsafe workplaces go unreported, fuelling an increase in building defects, remediation costs and litigation.

While these issues may appear entrenched and difficult to resolve, governments retain important levers, both in the form of a significant infrastructure spend and through legislation and regulation.

We want to work constructively with government on the solutions we have proposed. However, while the government seeks to silence us through the 'Ensuring Integrity' legislation, we stand with the community in wanting to address the real crisis in construction.

THE REAL CRISIS IN CONSTRUCTION

SHAKY FOUNDATIONS.

\$6.2 billion waste on apartment defects.

170,000 apartments affected by flammable cladding.

BAD CUSTOMERS.

Government waste of \$10.8 billion in the last ten years.

A further \$5 billion set to be wasted in the next several years through appalling management of infrastructure projects.

A GOLDEN OPPORTUNITY.

National harmonisation could save an additional \$2.1 billion in defective building and administration fees.

RECOMMENDATIONS

That the Federal government require jurisdictions to demonstrate informed purchaser capacity in delivery of projects they are funded to deliver.

That the Federal government require jurisdictions to deliver a harmonised system and establish an incentive scheme to achieve this.

That Federal funding be contingent on jurisdictions having an appropriate prequalification regime which accounts for past performance against safety, worker's entitlements and wages and the delivery of government projects on time, and on-budget.



INTRODUCTION

While the National Construction Code stands as an effective framework, the inconsistent and ad hoc manner it is applied in each state renders the concept of national regulation defunct.

NATIONAL harmonisation of the application of the code could save an additional \$2.1 billion in defective building and administration fees, as identified by independent economic research performed by Equity Economics.

The march towards increased private sector involvement in the construction industry has been characterised by an ideological pursuit of perceived increases in efficiency, productivity and savings. However, the cost of labour, capital and materials has remained steady over the past ten years.

GOVERNMENT AS AN UNINFORMED PURCHASER

Since the 1990s state governments have increasingly preferred to contract infrastructure delivery through the market. This has resulted in the dismantling of state government public works agencies. The intention has been to reduce public costs and risk. The result, however, has been the atrophy of state government institutional knowledge and expertise in delivering strategic oversight of major infrastructure projects.

In conjunction with the Australian Constructors Association, law firm Ashurst recently published Scope for Improvement, concluding that legal disputation is often driven by "poorly scoped projects, resulting in variations, rework and interface issues between trades, unclear contract drafting... poor contract administration (and) overly optimistic scheduling and cost estimates".1

Equity Economics argues that this dearth of adequate procurement and infrastructure proficiency has cost the Australian taxpayer \$10.8 billion over the last decade, and potentially another \$5 billion during the next three.2

THE CYCLE OF WASTE

This dynamic results in a cycle of waste, whereby governments commission work and lack the expertise necessary to ensure the scope and design is fit for purpose.

The result is inferior construction, requiring rectification, and disputation between the state and proponents when projects suffer delay and overruns, resulting in further delay and public money lost to legal proceedings. Projects then require re-work and revision.

The capital and energy wasted in this process results in more expertise leaving government for the private sector, which further entrenches the cycle.

FAILED DELIVERY MODELS

In the procurement of public works services, the Design and Construct (D&C) framework is the predominant delivery model. The tenderer prepares a design brief outlining what is required and then seeks tenders from proponents to design it, and separate tenders to deliver it.

A single proponent (head contractor) is contracted, who subsequently subcontracts to other entities to complete the works. There has therefore been a growth in the use of pyramid contracting, labour on-hire and subcontracting arrangements, which makes the enforcement of workers' rights difficult for the state authority responsible for the project. Furthermore, competition on cost has perpetuated adversarial relationships in the construction industry, with labour costs inevitably being reduced.

Ashurst, Scope for Improvement 2014, 2015, p.20 Equity Economics, Bad Customers - The billions going missing from infrastructure investment in Australia, 2019, p.2.

The shift to the private sector has also encouraged a flight of expertise from the state. In combination with complex sub-contractual arrangements, such a model makes life-cycle costs very difficult to determine. While responsibility of project oversight is shifted from the state to the proponent, liability for runaway costs and delays is not, however.



THE SHIFT TO THE PRIVATE SECTOR HAS ALSO ENCOURAGED A FLIGHT OF EXPERTISE FROM THE STATE.



OUTSOURCED WORKFORCE

It is not uncommon for a subcontractor to further engage another subcontractor to deliver elements of its respective contract. This further divorces the project from the principal contractor, who are often unaware of such arrangements.

It also prevents and encourages non-compliance with statutory employment requirements. Labour costs are the largest overhead and the easiest to reduce. In a competitive environment, where records of delivery, employment practices and business conduct are subordinate to cost, workers' rights inevitably suffer.

Additionally, the evolution of a hierarchical 'pyramid' of contractual relationships has been detrimental to workmanship. This is because subcontractors frequently do not have the capacity to complete the works, are subject to poorer oversight and may be forced to compromise labour costs and quality assurance in order to remain competitive or meet the requirements of the lead subcontractor.

FEDERAL GOVERNMENT FUNDING

The Federal Government distributes \$95 billion of Goods and Services Tax (GST) revenue to the states.³ Approximately 14 per cent of state infrastructure projects capital expenditure is funded by Federal Government allocation of GST revenue. In Victoria, half of all taxation revenues are derived from Federal Government grants, half of which are from Specific Purpose Payments - grants the Commonwealth makes to the states, usually subject to conditions as to how the money is spent.

The Federal Government could use funding to apply considerable leverage to achieve better compliance by proponents and outcomes for the public. Unfortunately, though, it has applied this leverage to advance an ideological agenda. Funding has previously been used to encourage reform. In particular, privatisation has been encouraged in the states' infrastructure development processes. However, the Federal Government has done little to ensure that state governments are equipped to effectively utilise the funding they receive or ensure the projects on which it is spent are appropriately delivered.

ONE RULE FOR EMPLOYERS, ANOTHER FOR WORKERS AND WHISTLE-BLOWERS

The Code for Tendering and Performance of Building Work is the Commonwealth procurement policy for building and construction. The Code is enforced by the Australian Building and Construction Commission (ABCC). The Code and the ABCC are intended to improve the performance of contractors and subcontractors.

However, instead of empowering the Union to protect workers by preventing and alleviating the consequences of poor delivery, the ABCC devotes considerable energy and resources to inhibiting the Union in its efforts to protect workers. It does not employ the same rigour in dealing with employers engaged in sham contracting, wage theft or poor health and safety practices. In addition, the Ensuring Integrity Bill may paradoxically effectively silence whistle-blowing union officials from holding the private sector to account.

Instead, in combination with a weak regulatory regime and the diffuse nature of government procurement and pyramid contracting, unscrupulous employers have been granted considerable latitude to undermine workers' rights and safe work place practices.

³ Australian Bureau of Statistics, Taxation Revenue Analysis, 29 April 2019, Retrieved from: www.abs.gov.au/ausstats/abs@.nsf/mf/5509.0







There has been a growth in labour on-hire and irregular subcontracting arrangements, which has subsequently eroded worker's rights, wages and entitlements. In some instances, pyramid contracting is deliberately pursued to circumvent the wages and conditions within an Enterprise Agreement and offset employment obligations of the primary contractor. This means employees of the second subcontractor are often receiving lesser entitlements in comparison to the workers employed by the first subcontractor.

At the same time, whistle-blowers who might bring misbehaviour to light are effectively hamstrung and Unions sidelined, the first casualty is often safety followed shortly by the worker. It is a demonstrable fact that unionised workers suffer less injuries than nonunionised workers. They are 70 percent more likely to be aware of OHS hazards and issues, than in a nonunionised workplace.4

FAILING COMPLIANCE REGIME

Local Governments used to perform the certification of building plans to ensure they were compliant with relevant building codes and standards. However, over the last two decades this function has increasingly been outsourced to external independent professionals. This was in part an effort to address perceived deficiencies of local government, including dilatory certification and corruption. In many instances however, allowing a contractor to select its own building surveyor has its own failings. Contractors are potentially future clients, for example, and may not be forthcoming with future custom if a surveyor fails to certify a plan.

Even in circumstances where plans are certified compliant, adjustments may be made during the build phase. The Victorian Building Authority found that 20 per cent of external cladding on high rise building differed from those specified in the original plans.⁵ With workers being restricted in their ability to blow the whistle on such failings, it falls entirely on building inspectors to pick up on post-build defects. However, some aspects of a building are not accessible upon completion, and again, there is potential for conflicts of interest between inspectors and contractors. The same is true for the supply chain regarding private certification of building materials.

As the CodeMark International Standard's recent suspension from the Joint Accreditation System of Australia and New Zealand demonstrates, some building material manufacturers may deliberately seek accreditation from substandard certifiers. It may therefore be the case that building materials meet standards, but that the standards themselves are deficient.

ACTU, What has the Union movement done for OHS?, https://www.actu.org.au/ohs/about-us/union-movement

Australian Building Codes Board, Non-Compliant use of external Cladding Products on Building. Retrieved from: www.acbc.gov.au/-/media/Files/Resources/Consultation/RIS-External-Cladding.pdf

Non-compliance is occurring across the construction cycle, and regulators are underfunded and weak. In the absence of effective enforcement, one can expect such issues to continue unabated. Furthermore, while the National Construction Code and National Standards is a Federal Government regulation, the state's regulatory authorities are responsible for enforcing it. The Federal Government, however, does very little to ensure that state authorities enforce these standards.

THE MATERIAL CONSEQUENCES OF THESE FAILINGS.

The issues outlined above are directly responsible for the dire consequences that fill our newspapers every week; flammable cladding, cracked buildings and leaks.

The cost of such defects are estimated to be \$6.2 billion for apartments alone, which constitute a mere 14 per cent of new residential dwelling construction.⁶ This is just the tip of the ice-berg. Apartment blocks attract a great deal of scrutiny because the risks such defects represent affect more people. However, because such oversight is not extended to individual dwellings, these defects are likely replicated there too.

Housing constitutes 61 per cent of household net worth in Australia. The damage to property value and liquidity is immense. Needless to say, however, the threat such issues pose are not merely financial. Australians buy property under the assumption that its construction meets basic standards of quality and safety. When these standards are not enforced and met, the lives of Australian families and construction workers at risk.

Most conspicuously, flammable cladding has been used in 3461 residential apartment blocks across Australia, affecting nearly 170,000 apartments.8 As London's Grenfell disaster so tragically highlighted, there is potential for significant loss of life in fires involving flammable cladding. Since 2014, the Victorian Government has committed an enormous \$600 million towards rectifying these buildings.

Fire safety concerns do not end with non-compliant cladding, however. A study conducted by Deakin and Griffith Universities found that 13.26 per cent of the defects they identified in multi-apartment building were fire protection defects, including compromised fire separation walls, missing fire collars on pipes, incorrectly installed smoke detection systems, inconsistent fire plans, poor exit signage and water damaged fire doors.

Regarding the latter, structural defects and poorly fitted cladding is often a precursor to water and mould damage. The New South Wales Government's report into the structural deficiencies of the 36-level, 392 apartment Opal Tower reached damning conclusions about the quality of materials and workmanship. Notably, there were substantial inconsistencies between the materials and specifications used during construction and those specified in the architectural designs and standards. This was the product of the D&C contract model resulting in a deficit of contractor oversight.



THE COST OF SUCH TO COST \$6.2 BILLION FOR APARTMENTS ALONE

Equity Economics, Shaky Foundations – The National Construction Crisis. 2019. p.2. Australian Bureau of Statistics (28 June 2019), 5232.0 – Australian National Accounts: Finance and Wealth, March 2019, Table 32.

Equity Economics, Shaky Foundations – The National Construction Crisis. 2019. p.2. Carter, J., Opal Tower Investigation Interim Report, Independent Advice to the MSW Minister for Planning and Housing., 2019, pp.4-6.



THE SOLUTIONS



A LITTLE GOES A LONG WAY BUILDING CAPABILITY.

A small investment in government capability would reap large dividends. A report drafted by Equity Economics demonstrated that during the roll-out of the Queensland Government's Building the Education Revolution (BER) infrastructure program, every \$5 million of funding infrastructure resulted in one construction employee. Conversely, in NSW every \$32 million of funding accounted for a single construction worker, while in Victoria this figure increased to \$181 million.

One might assume that over the project lifecycle, such a vast disparity world result in proportionally more expensive projects. However, in Queensland, BER project were in fact \$400-\$800 cheaper per m².

The Federal Government could exert considerable leverage through its Specific Purpose Payments or general grants by stipulating that funding calculations to other state governments, be predicated on recipients ensuring that they likewise have the capability or governance to deliver on their infrastructure commitments. This has precedent. For example, both the Abbott and Rudd Governments used this leverage to initiate regulatory reform processes. The former also established the Asset Recycling Fund (ARF) in 2014.

Initially made up entirely of uncommitted funds from the Building Australia Fund and the Education Investment Fund totalling \$5.9 million, subsequent funds were derived from the privatisation of Commonwealth assets, such as Medibank.

The ARF was primarily used fund the new Infrastructure Growth Package and specific projects of Infrastructure Investment Program, such as Black Spot Projects, road investment projects and the Roads to Recovery Programme. In parallel to this, the Asset Recycling Initiative was begun, whereby states and territories were provided with a financial incentive to sell assets and use the proceeds to fund infrastructure investment. Incentives are an attractive mechanism for the Federal Government – where it suits their ideological end. However, they could easily be used to drive national harmonisation in the regulation of the built form.

In some jurisdictions, an "Alliance" model has emerged as a favoured model in the delivery of complex, costly projects. Such a model establishes a joint team by bringing together the proponent and private sector partners for the delivery of a project. It would avoid the development of adversarial relationships, minimise the duplication of processes, streamline governance and ensure that Government remains involved in a key oversight capacity. This would minimise costs and delays, maximise innovation and improve skills sharing, and is underpinned by a 'no-fault, no-blame culture' and a commitment to avoid disputation. The savings such a model would produce by increasing efficiency and minimising waste would fund the extra costs such a model entail.

Such a model would go some way to restoring state capability in the sector and turning the state in to an informed purchaser. The Queensland Government has maintained an informed purchaser capacity with a significant standing workforce. 10 As has been discussed, this has resulted in reduced waste, a nimbler response to emergencies and a more diligent, considered approach to procurement thanks to the state maintaining a level of expertise and oversight in infrastructure projects.

While an alliance model appears preferential, naturally, some projects will better lend themselves to one delivery model over another. For example, "Construction Management" models allow for the project owner to maintain control and oversight, with design and trade contractors engaged in conjunction with a construction manager. A "Managing Contractor" model employs the lead contractor as the "managing contractor", with responsibility for the design of the project as well as the contracting of delivery partners to complete construction, all on behalf of the project owner.

States should maintain a strong internal procurement capacity fulfilled by a small project delivery team that could determine which model best applies to a project's requirements. Additionally, were states to maintain a public sector construction workforce such as in Queensland, threshold tests could be undertaken to determine whether the state requires external private contractors at all.

Recommendation: That the Federal government require jurisdictions to demonstrate informed purchaser capacity in delivery of projects they are funded to deliver.

REINFORCING THE FOUNDATIONS — HARMONISING REGULATION

Current enforcement of the National Construction Code does this world-class regulatory framework a disservice. The Building Confidence Report recommends a move to a harmonised approach to enforcement across the states. Research conducted by Equity Economics calculates that if undertaken by July 2020, a harmonised approach to enforcement across the states would result in \$2.1 billion over four years.

True, harmonising and strengthening building regulation will involve additional expenditure. Queensland is considered an exemplar of best practice in regulation and is the most advanced jurisdiction in terms of implementing the recommendation of the Building Confidence Report. It spends \$5.80 per \$1000 of residential construction on regulation. Comparatively, Victoria spent \$4.40. If states outside of Queensland were to increase their administrative expenditure by \$1.20 per \$1000 of construction expenditure, total expenditure would increase \$252 million.

A 2019 MOZO Survey of 1,000 people found that in Queensland 14.89 per cent more apartments were completed according to their building plan, resulting in increased compliance and reduced defects.¹¹ An ACIL Allen Consulting report on improved regulation in NSW has already estimated potential reduction in building defects of 13 per cent from the limited reforms currently being implemented by the NSW Government.¹² If Victoria and NSW were to adopt the proposed increase in regulatory expenditure, this increase would result in savings of up to \$295 and \$288 respectively from 2020-2021 and 2023-24, by avoiding defects in new houses and apartments.

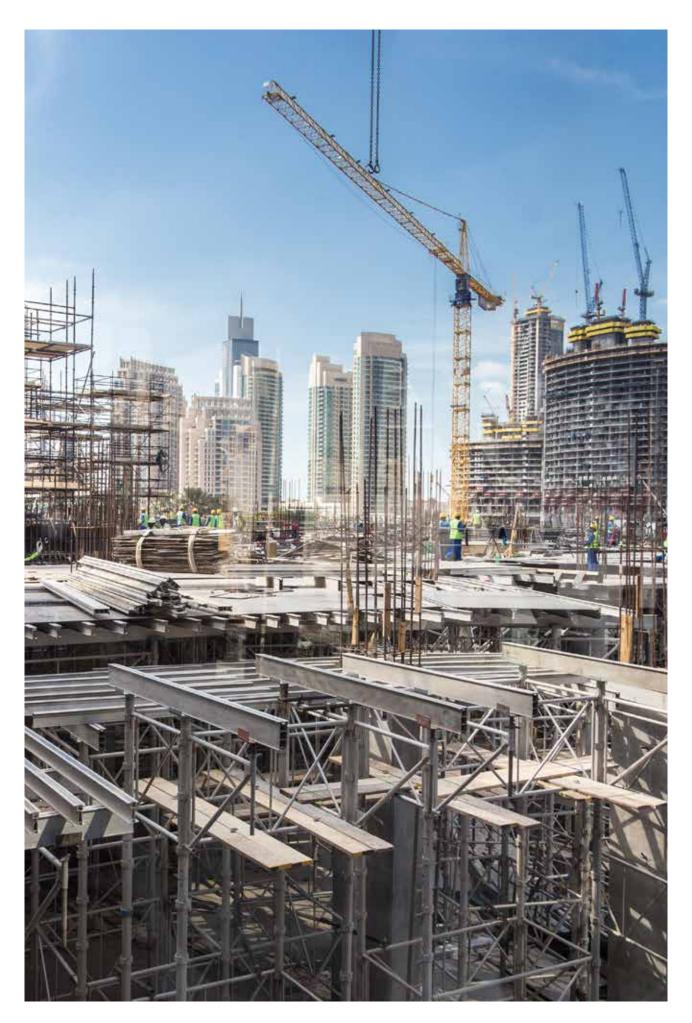
Recommendation: That the Federal government require jurisdictions to deliver a harmonised system and establish an incentive scheme to achieve this.



A HARMONISED APPROACH TO CROSS THE STATES WOULD ESULT IN \$2.1 BILLION

¹⁰ Orgill, B., Building the Education Revolution Implementation Taskforce, 2011, p.11.

MOZO, Property Pain: Building Defects Report 2019, 2019.
ACIL Allen Consulting, Independent Review of the Building Professionals Act 2005 – Cost Benefit Analysis of the Recommendations, 2015.



THREE STRIKES

The problems outlined in this document have created an environment where project delivery, workers' rights, safe working conditions, secure employment and meaningful training opportunities have been put on the altar of privatisation, and far removed from the oversight of regulatory bodies and state authorities.

While a new model of delivery, greater investment and regulatory harmonisation would go a long way in increasing the capacity of the state to ensure workers' rights are front and centre in infrastructure development, this is a field where the public sector already has considerable leverage.

As the Transport Workers' Union noted upon launch of the 2018 report Raising the Bar: How government can use its economic leverage to lift labour standards throughout the economy, "the reach of Government has now been revealed in monetary terms and it is massive, we should harness this power to benefit the entire community instead of rewarding employers which break the rules and game the system".13

There are several examples of how this influence could be effectively marshalled to guarantee better labour outcomes in three avenues of influence; direct public sector work and production, indirect influence over the activity of arms-length service providers, and government procurement from private firms.14

For example, in the absence of Federal direction and in the face of the Abbott Government's revocation of several minimum Commonwealth procurement standards, several state governments have also implemented procurement policies which require adherence by contractors to specified minimum labour standards, award conditions, and industrial relations practices.

Pyramid contracting and re-bidding for contracts have made it very difficult for workers to obtain meaningful improvements in wages and working conditions, because competition drives down labour costs. In NSW, however, under pressure from union and community advocates, municipal councils in Central Coast, Penrith and Randwick agreed to require all service bidders to protect the job security, wages, and conditions of existing waste collection workers.15

This conditional access to procurement bidding processes has been replicated at a Federal level where a new initiative requires prospective bidders on Federal procurement projects valued at over \$4 million to be compliant with ATO tax obligations. This could easily be transposed to stipulate adherence to compliance with labour standards.

Similarly, federal funding to state governments should be contingent on adherence to strict rules that hold employers to account for undermining labour standards and wages, including the termination of contracts with proponents who break the rules.

Similarly, infrastructure companies are repeatedly winning work despite late delivery, shoddy workmanship and massive cost over-runs. The same large companies which inflict enormous damage on the public purse and endanger workers and the community are awarded contracts again and again. The Federal government's response is to target unions who act to protect the community and their members.

A "three strikes and you're out" clause would encourage greater compliance by intransigent companies and ensure persistent offenders are not able to continue their malpractice at the taxpayers' expense.

Recommendation: That Federal funding be contingent on jurisdictions having an appropriate pre-qualification regime which accounts for past performance against safety, worker's entitlements and wages and the delivery of government projects on time, and on-budget.

 ¹⁰ John Sheldon, Indulonal Secretary, Iransport Workers Union, March 22 2018, available from: https://www.twu.com.au/press/twu-calls-for-three-strikes-law-for-employers-on-public-projects-as-report-shows-huge-600bn-government-spend/
The Australia Institute, Raising the Bar: How government can use its economic leverage to lift labour standards throughout the economy, 2011, available from: https://www.tai.org.au/sites/default/files/Raising_the_Bar_Formatted_Final_0.pdf
Ibid.

CONCLUSION

The seeds of the national crisis in construction have been sown over the last 30 years and it now that taxpayers, consumers and workers that face a bitter harvest.

DRIVEN partly by relentless pressure from the property development sector for decreased regulation and increased profit, and partly through government's failure to stand by adequate regulations that protect workers and consumers the construction sector has driven itself to near collapse.

State governments have been complicit in diminishing their own technical knowledge and capability in delivering large scale infrastructure projects and equally suffer with constant cost blow outs and humiliating delays for which they ultimately bear public responsibility.

Additionally, high profile construction failures such and the Opal and Mascot Towers will become par for the course as poorly constructed buildings age and their defects become more apparent.

Consumers rightly expect that government will uphold laws ensuring their homes are built in a safe and affordable manner where their rights to quality workmanship and contract transparency are protected.

Equally, workers expect and deserve workplaces that are safe, and jobs where their wages and entitlements and protected and not undermined by unscrupulous operators.

Through the crisis in residential apartment construction, which has seen the costs of defects soar to \$6.2 billion, to the use of flammable cladding which affects 170,000 apartments, consumers and workers has expressed their dismay and exasperation that successive governments have failed to adequately protect them.

While these issues may appear entrenched and difficult to resolve, both Federal and State governments retain important levers, both in the form of their own considerable infrastructure spend and through their control of legislation and regulation, to positively address the crisis.

Australian governments, the private sector and unions collectively owe it to the community to come together and resolve the national crisis in construction.

As always, the construction union stands ready to work with government and the private sector to tackle this vitally important task for the Australian people.





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