Master Builders Australia

Submission to the Treasury

on

Improving Bankruptcy and Insolvency Laws Proposals Paper

10 June 2016

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1 Introduction

1.1 This submission is made on behalf of Master Builders Australia Ltd.

1.2 Master Builders Australia ('Master Builders') is the nation's peak building and construction industry association which was federated on a national basis in 1890. Master Builders Australia's members are the Master Builder State and Territory Associations. Over 126 years the movement has grown to over 32,000 businesses nationwide, including the top 100 construction companies. Master Builders is the only industry association that represents all three sectors, residential, commercial and engineering construction.

1.3 The building and construction industry is an extremely important part of, and contributor to, the Australian economy and community. It accounts for close to 8 per cent of gross domestic product, and around 9 per cent of employment in Australia. The cumulative building and construction task over the next decade will require work done to the value of $2.6 trillion and for the number of people employed in the industry to rise by 300,000 to 1.3 million.

2 Background

2.1 On 29 April 2016, the Treasury released a proposals paper 'Improving bankruptcy and insolvency laws' ('the Paper') containing a series of proposals to improve Australia's bankruptcy and insolvency laws.

2.2 Master Builders welcomes the opportunity to provide a submission in response to the Paper.

2.3 This submission seeks to highlight matters relevant to bankruptcy and insolvency in the building and construction industry. Except where specifically identified, comments regarding the three categories of proposed change and implementation options are expressed broadly.

2.4 Master Builders would seek further opportunities to engage with Treasury and the Government about the proposals in the Paper, and options for their implementation, at all future stages as they are developed into a legislative form.

3 The Building and Construction Industry

3.1 The building and construction industry is a key driver of the Australian economy and makes a major contribution to the generation of wealth and the welfare of the community, particularly through the provision of shelter. The building and construction industry is at the forefront of building Australia's economic and social infrastructure.

3.2 Master Builders estimates that the cumulative construction task over the next decade will require work done to the value of $2.6 trillion. The residential and non-residential building sectors combined will require work to the value of $1.25 trillion and in the engineering construction sector $1.15 trillion worth of work will be required. The construction workforce currently represents over 9 per cent of the total Australian workforce with the number of jobs expected to increase by 300,000 to around 1.3 million employees by 2021.

3.3 According to the Australian Bureau of Statistics (ABS), the value of work undertaken by the building and construction industry was $41 billion in the December quarter 2015. Residential building work done was $16 billion, non-residential building $7.3 billion and engineering construction $17.7 billion. At February 2016 the construction industry employed 1.05 million people.

3.4 Building and construction is one of the most important small business sectors. Small businesses account for nearly 99 per cent of firms in the building and construction industry, totalling almost 350,000 small firms. Ninety-five percent of all businesses in the building and construction industry employ fewer than five people, while less than one per cent employ 20 or more.

3.5 In broad terms, small business accounts for around half of national employment and over one-third of domestic product. Small building and construction businesses produce more than half the industry's output and create almost a third of the jobs - well ahead of other industries.

4 Bankruptcy and Insolvency

4.1 Bankruptcy and insolvency are subjects from which the building and construction industry is not immune.

4.2 Master Builders acknowledges that the level of entry and exits to the industry is higher than the average for other industries. A detailed analysis of relevant latest available data is at **Attachment A**.

4.3 As a result, Master Builders has a history of active engagement with government, regulators, relevant agencies and other stakeholders in this area and this remains ongoing. For relevant background, we would draw attention to the following Master Builders submissions made earlier elsewhere being:

- MBA Submission to the *Productivity Commission on the Draft Report – Inquiry into Business Set-up, Transfer and Closure* dated 6 July 2015 (**Attachment B**)

- MBA Submission *Business Entry and Exit in the Building and Construction Industry* dated 12 March 2015 (**Attachment C**)

- MBA Submission to the *Senate Economic References Committee on Insolvency in the Australian Construction Industry* dated 17 April 2015 (**Attachment D**).

4.4 We would also draw the attention of Treasury to the Report of the Senate Economic References Committee *Insolvency in the Australian Construction Industry December 2015*.

4.5 In terms of the data set out at **Attachment A**, care should be taken to avoid assumptions or draw inferences from the relevant entry/exist levels.

4.6 While it is acknowledged that the rate of insolvency in the industry remains high, there are other factors that contribute to, or have the capacity to contribute to, the entry/exit levels. These relate to the unique structure of the industry and the nature of work that is performed.

4.7 Building and construction work conventionally involves a client engaging a building contractor that will act as a 'project manager'. The building contractor uses sub-contractor companies to perform particular tasks at different stages of construction. Sub-contractors are generally small and specialise in particular types of construction work.

4.8 As a consequence of this approach entities are more likely to be established in order to obtain work and it is not uncommon for entities to cease existing once work is no longer available. In this regard, the level of entrants and exits are partly indicative of the way work is done in the industry.

4.9 The level of industry activity, as a consequence of the above structure, has capacity to influence entrants and exits more so than other industries.

4.10 The above factors should also be considered in conjunction with the trade based nature of the work performed in the industry. In short, it is not uncommon for building industry participants to transition between different entity relationships over their lifetimes. A tradesperson may therefore work in a traditional employment relationship (as an employee) at some point and work as a contractual relationship (for themselves and/or employing others as either a sole-trader or incorporated entity) at other points.

4.11 Therefore, any analysis of the data below should be careful to avoid concluding that building industry participants are more susceptible to failure. It is more likely that these higher levels arise due to unique structural elements of the industry, the way the work is done and the trade based nature of the work.

5 General View of Proposals

5.1 Master Builders' general policy view is to support measures that will increase the number of entrants to the industry while concurrently reducing the number of exits. To this end, Master Builders views the proposals in the Paper in a positive light.

5.2 Notwithstanding this, Master Builders would recommend that the Government take care to ensure that a regulatory balance is maintained so as to maintain a system of safeguards and disincentives to those who seek to do the wrong thing, or use the law in a way that deliberately avoids legal or commercial obligations.

5.3 We would also caution against any regulatory change taking a 'one size fits all' approach, particularly given the specific nuances unique to the building and construction industry. As noted below in section 8, the proposals have the capacity to deliver positive outcomes as well as unintended consequences.

5.4 The extent to which small business feature in the sector is also relevant to our favourable view of the proposals. As noted above, the nature of the industry and its work means that small contractors are particularly susceptible to the actions and conduct of larger contractors that impact cash flow.

5.5 For example, a small sub-contractor engaged on a project may be required to expend significant cash resources to purchase materials before work starts. Work may be performed and materials installed weeks ahead of the small sub-contractor receiving payment thereby creating circumstances where they are particularly susceptible to an insolvency event.

5.6 If the small sub-contractor is not paid, or if they receive a demand for payment from another party, this may cause financial difficulties. Concurrently, if the small contractor suffers an insolvency event, it may impact on the principal contractor via its management of the project. This can be experienced in terms of project delays and their management of other subcontractors so engaged on the same project.

5.7 The situation described above demonstrates how entities in the industry are co-dependent upon each other and how the success or failure, and conduct of one party, has capacity to influence the other. This co-dependency exists in the industry to a greater extent than for other sectors and creates a degree of cyclical vulnerability. This creates potential to put smaller entities at risk of insolvency events particularly during parts of the cycle where they are financially vulnerable.

6 Reducing the Default Bankruptcy Period

6.1 Master Builders supports the proposal in this section. Reductions in default bankruptcy periods, travel restrictions and credit restrictions are measures that we envisage will reduce the number of exits from the industry. It will also assist in addressing the cultural stigma associated with bankruptcy.

6.2 At the same time, Master Builders would support increased flexibility within, and greater accessibility to, consequential regulatory arrangements to achieve regulatory balance. To this end, we would support relaxations in the criteria for trustees to lodge objections and evidence in support to balance the reduction in default periods.

6.3 In terms of the general avenue of appeal for an act, omission or decision of a trustee, we would caution against any role being given to registered industrial employee organisations. This is because of the unique nature of the building and construction industry and the capacity for organisations of employees to impact on the financial status of an entity. An expanded discussion of this point can be found at Sections 8 and 9 of **Attachment D**.

6.4 Master Builders would not oppose a reduction to the retention period for personal insolvency information in credit reports and note that this could be an incentive to ensure greater levels of compliance with obligations after discharge.

6.5 Master Builders strongly supports proposal 1.3.3. It is noted that in the building and construction industry, the capacity for industry participation and income generation is frequently dependent upon the holding of a particular licence in order to perform work.

6.6 To this end, the capacity for a person to discharge bankruptcy obligations may be jeopardised if a licence is removed, cancelled or suspended. We submit that throughout relevant consultation with industry and licensing associations there should also be a detailed discussion of this issue.

7 Safe Harbour

7.1 Master Builders supports the safe harbour concept and submits that Safe Harbour Model B ought to be preferred.

7.2 Model B is simpler and less cumbersome than Model A. It reflects Master Builders' general preference towards a carve-out from particular legislative provisions as an alternative to the creation of a new defence. This reduces the need for litigation and reduces cost to the industry.

7.3 The factors to be considered by a director when appointing a restructuring adviser should be set out in regulator guidance provided by ASIC rather than in regulation. This enables changes or variations to those factors to occur in a nimbler and effective manner. Noting this, ASIC should be required to consult with stakeholders prior to the alteration of those factors were it to be given this role.

7.4 Were it to become a requirement that organisations are approved to accredit restructuring advisers, Master Builders would observe that such approval be conditional upon criteria that are transparent and accessible.

7.5 Master Builders would not oppose the proposed method for determining viability. We would, however, recommend that the restructuring adviser take into account two particular factors when determining viability. These are:

- any particular features of the industry in which the entity and directors exist that have particular capacity to impact viability; and
- the causes of, or event giving rise to, the necessity for the appointment of the restructuring adviser.

7.6 Master Builders express no preference about whether these factors ought to be set out in regulation or left to adviser discretion. We do note, however, that were they to be set out in regulation, the factors be expressly noted as being non-exhaustive.

8 Ipso Facto Clauses

8.1 Master Builders notes the proposal to void ipso facto clauses.

8.2 It is very common for contracts in the building and construction sector to contain clauses allowing termination due to insolvency. The proposal has the capacity to reduce the rate of exits from the industry, particularly for small business sub-contractors, and should be viewed favourably from this perspective.

8.3 Concurrently, the proposal could also increase the risk to principal contractors. It may lead to circumstances where they are forced to continue a relationship with a subcontractor which may in turn jeopardise the capacity for a project to be completed on time or limit recourse options in circumstances involving construction defects. This is likely to see principal contractors to prefer subcontractors who are substantial or require greater performance security. This would be an unintended consequence causing an adverse impact on small business, a reduction in the level of entrants to the industry, and cause the cost of construction to increase.

8.4 To this end, Master Builders would submit that the Government consider a flexible approach to the adoption of its proposal as applicable to commercial contracts in the building and construction industry. While we are not inclined to support a carve-out per se, there are other options to balance the competing potential consequences noted above.

8.5 One such option may be the inclusion of a mechanism that allows ipso facto clauses in industry related contracts to be considered void, subject to a simple and interim safeguard mechanism. Such mechanism may give the party who experiences an insolvency event a short timeframe (not more than five business days) in which it (or restructuring advisers acting on its behalf) could contest the termination of the contract if so initiated by the other party. This may involve invoking any dispute resolution process in the contract and the capacity for agreement to be reached whereby the contract is preserved without the principal suffering adverse consequences.

8.6 <u>To this end, we would invite the Government to consult further with Master Builders as it considers the implementation options set out in the paper</u>.

8.7 Master Builders would oppose any move to make the proposal to void ipso facto clauses retrospective. This has significant potential to increase risk to principal contractors and cause a spike in construction costs to clients.

9 Conclusion

9.1 Master Builders appreciates the opportunity to comment on the Paper.

9.2 As noted earlier herein, <u>we invite Treasury and Government to continue consultations with Master Builders to ensure relevant proposals within the Paper, if so implemented, occur without difficulty or disruption to the building and construction industry and accounts for its unique circumstances.</u>

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ATTACHMENT A

Master Builders Australia

Entry and Exit of Businesses in the Building and Construction Industry

June 2016

MASTER BUILDERS AUSTRALIA

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1 Overview

1.1 The building and construction industry (BCI) in Australia is confronting a number of challenges which are likely to frame its longer term future.

1.2 Key amongst these challenges is the seeming trend decline in the number of firms in the industry, reflecting a greater number of exits of existing firms over entry of new firms into the industry.

1.2.1 For example, some 15.3 per cent of firms in the BCI left the industry annually, on average, over the four years to 2014/15, while 13.9 per cent similarly entered the industry over the same period.

1.2.2 Looked at another way, these figures suggest a ‘churn’ (or turnover) rate of almost 3 in 10 firms in the BCI, on average, each year.

1.3 At the same time, the survival rate for BCI firms must be a matter for concern for the future of the industry, with just over half of new firms entering the industry failing within just three years.

1.4 This situation is made even more challenging when one realises firms in the BCI have a greater likelihood of failure (and exit from the industry) than the All Industry average – that is, firms in other industries, on average.

1.5 Taken as a whole, this paints a picture of a substantial loss of entrepreneurial initiative, and human (skills and training) and other (financial) capital to the industry. It also speaks to the longer term capacity of the industry both per se, and in its ability to contribute to the wider Australian economy.

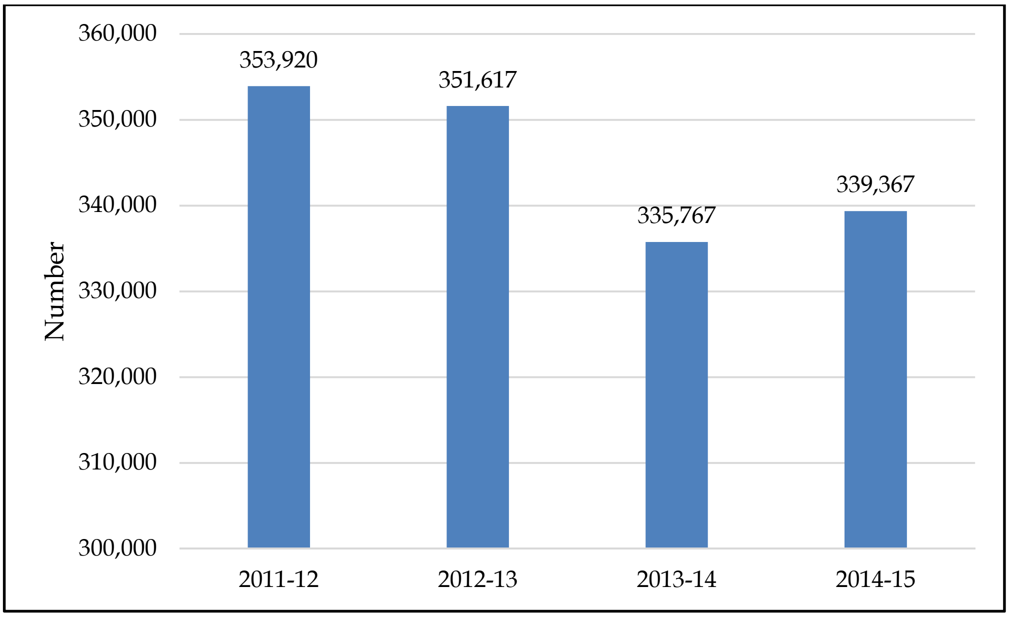
1.6 All data used in this report were taken from the Australian Bureau of Statistics’ data series on business entry and exit (ABS, 2016). The data series covers the four financial years from 2011/12 to 2014/15 (the latest available), unless otherwise indicated.

1.7 Caveat: while Master Builders acknowledges the ABS as the source of the data, the analysis, and the interpretations and inferences drawn therefrom are ours alone.

2 Construction – Entries, Exits and Churn

2.1 The number of firms in the BCI has fallen noticeably over the past four years, as can be seen in Graph 1.

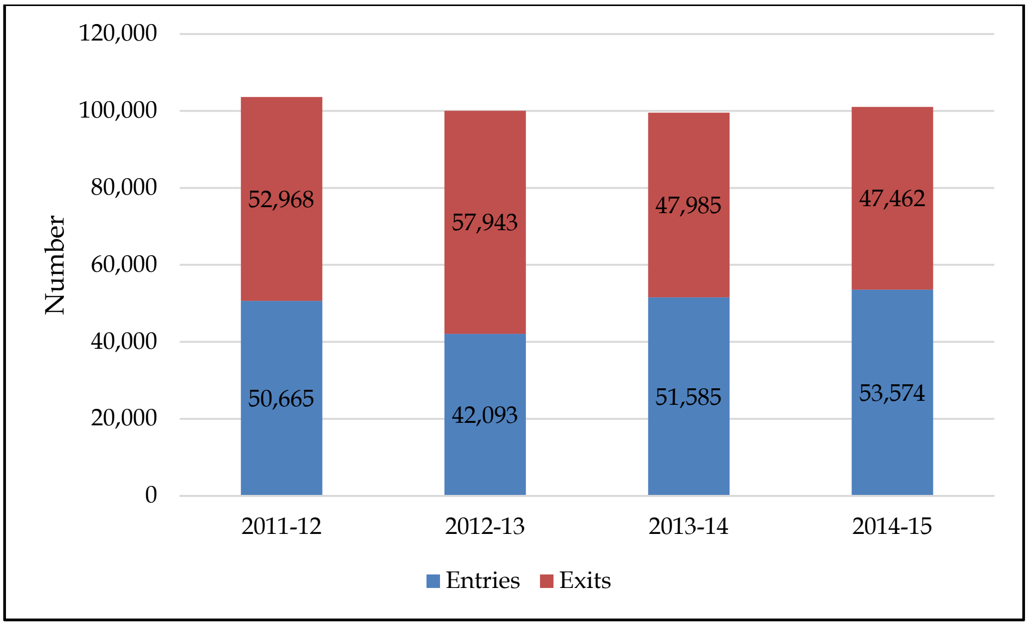
Graph 1: BCI Firms



2.2 The number of firms in the BCI declined from 353,920 in 2011/12 to a low of 335,767 in 2013/14, a drop of 5 per cent in two years, before recovering slightly to 339,367 firms in 2014/15 – an overall fall of 4 per cent over the four years under review.

2.3 The decline in the number of BCI firms reflects the excess of exits of firms from, over entries of firms into, the industry. In short, more firms left the BCI than entered it over the four years to 2014/15, as can be seen in Graph 2.

Graph 2: BCI Entries and Exits



2.4 The number of exits from the BCI averaged just under 53,000 firms, and the number of entries into the BCI averaged slightly more than 48,100 firms, per annum over the four years under review.

2.5 However, this general picture masked two sub-periods – the first two years when exits exceeded entries (that is, the total number of firms in the BCI declined); and, in the second two years when exits were exceeded by entries (that is, the total number of firms in the BCI rose).

2.5.1 In the two years to 2012/13, the number of exits averaged 55,456 firms per annum while the number of entries averaged 46,379 firms per annum, an average difference of 9,077 firms – or, to look at it another way, a total of net exit of 18,153 firms over the two years.

2.5.2 By comparison, in the second two year period (to 2014/15), the number of exits averaged 47,724 firms per annum while the number of entries averaged 52,580 firms per annum, giving an average difference of 4,856 firms – or, an increase of 9,712 firms over the two year period.

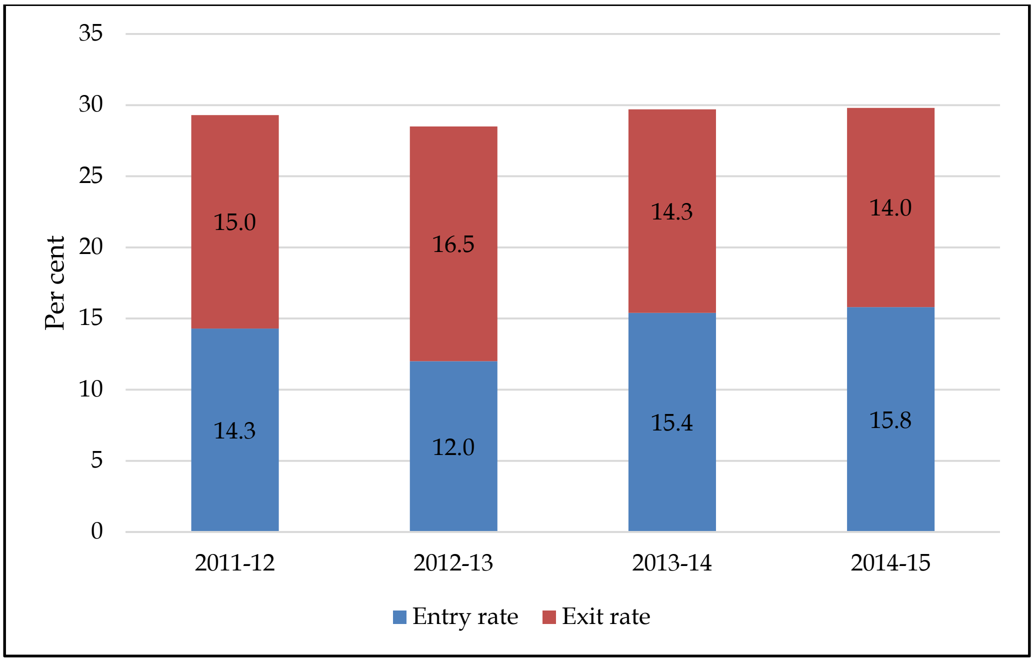
2.6 This pattern of net exits then net entries of firms in the BCI is broadly consistent with the broader cyclical nature of the industry as a whole.

2.7 A clearer picture of the movements in entry into and exits from the BCI can be gleaned from an examination of entry and exit rates – that is, movements in the number of firms as a proportion of total firms in the industry:

- the entry rate is the number of firms entering the industry as a proportion of the total number of firms in the industry;
- the exit rate is the number of firms leaving the industry as a proportion of the total number of firms in the industry; and,
- the churn rate, which is an aggregation of the entry and the exit rates, and is a measure of the turnover of firms in the industry.

2.8 Graph 3 reports the entry and exit rates, and by inference the overall churn rates, for BCI firms over the four years to 2014/15.

Graph 3: BCI 'Churn' Rates



2.9 In broad terms, the exit rate averaged 15.3 per cent and the entry rate averaged 13.9 per cent over the four years under review.

2.9.1 That is, on average, 15.3 per cent of firms left the industry each year, and 13.9 per cent of firms came into the industry each year.

2.10 The largest net exit rate (exit rate less the entry rate) at 4.5 percentage points occurred in 2012/13 (exit rate = 16.5 per cent; entry rate = 12.0 per cent).

2.10.1 By comparison, the largest net entry rate (entry rate less exit rate) at 1.8 percentage points occurred in 2014/15 (exit rate = 14.0 per cent; entry rate = 15.8 per cent).

2.11 Taken together – that is, summing the entry and exit rates – the figures point to an average churn rate of just over 29 per cent per annum over the four years to 2014/15.

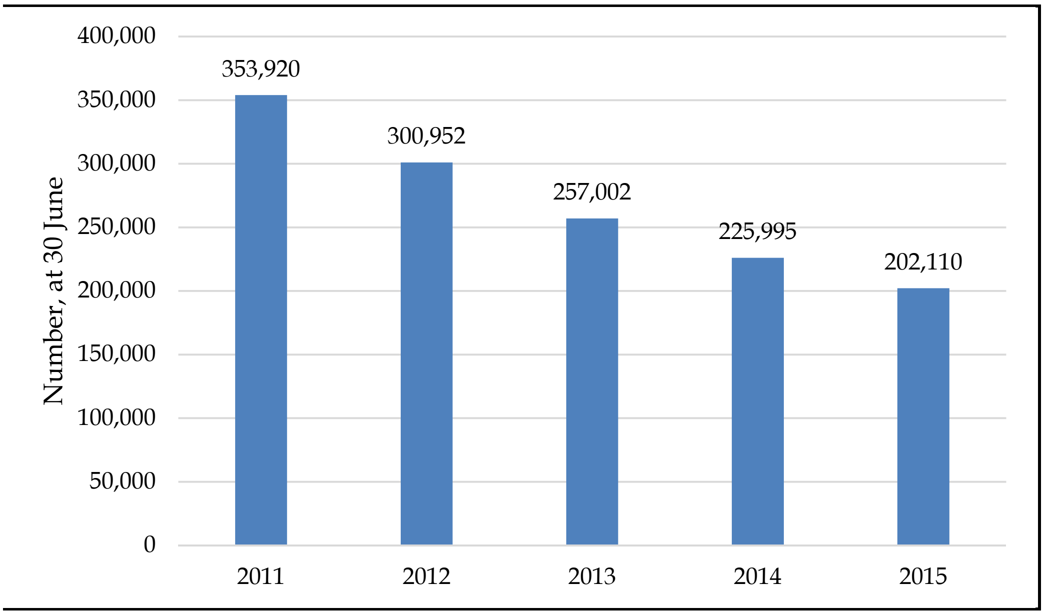
2.11.1 That is, nearly 3 in every 10 firms in the BCI will arrive into, or leave (or both) in the industry in any given year, suggesting a substantial loss of entrepreneurial initiative, and human (skills and training) and other (financial) capital to, and the longer term capacity of, the industry.

3 Construction – Survival Rates

3.1 Another perspective can be gleaned from a review of survival rates for firms in the BCI – that is, what is the likelihood a firm in the industry will continue in business in the industry in coming years.

3.2 Graph 4 reports the outcomes for all firms operating in the BCI at 30 June 2011.

Graph 4: BCI Firms – Survival



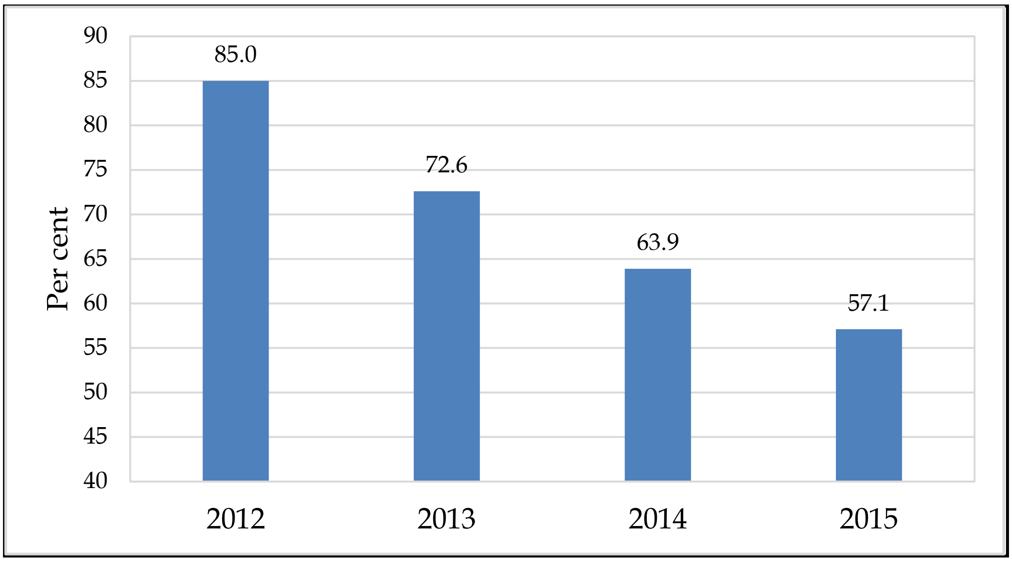
3.3 Of the some 353,920 firms operating in the BCI at 30 June 2011, just 202,110 of those firms (or some 57 per cent) were still operating in the industry four years later.

3.3.1 That is, more than four-out-of-ten firms in the BCI in 2011 departed the industry by 2015.

3.4 Graph 5 reports the survival rate for firms operating in the BCI in 2011 over each of the subsequent four years.

3.4.1 (Readers interested in attrition rates can simply calculate '100 per cent less the survival rate'.)

Graph 5: BCI Firms – Survival Rates



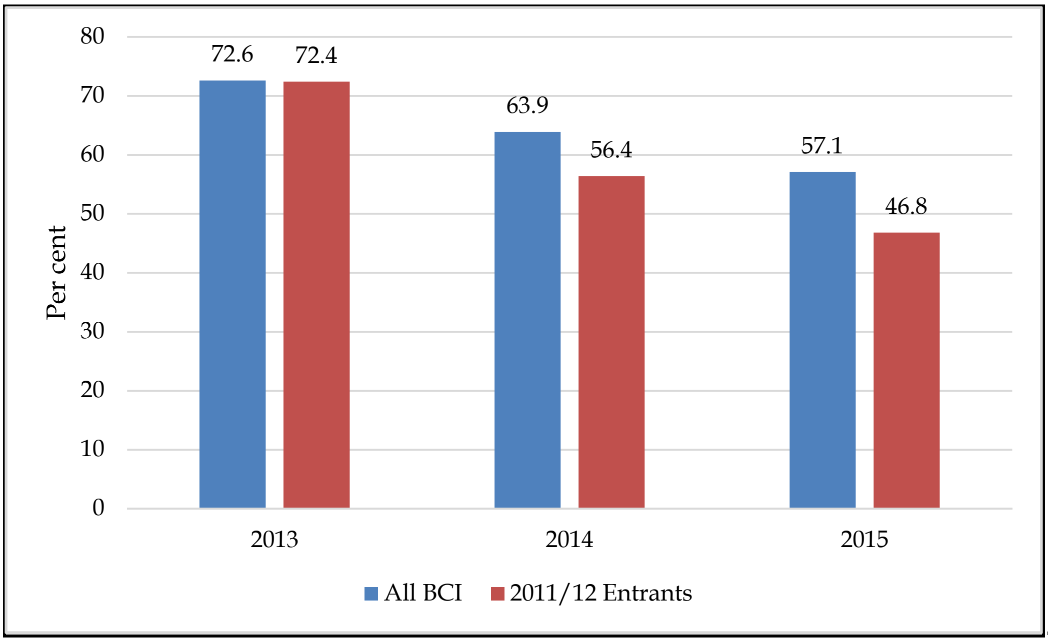
3.5 Several messages stand out from Graph 5, namely:

- 15 per cent of firms in the BCI in 2011 exited the industry within 1 year;
- 27 per cent exited within 2 years,
- 36 per cent exited within 3 years; and,
- 43 per cent exited within just 4 years.

3.6 As disheartening as these figures may be – 2 in every 5 firms in the BCI exits the industry within just 4 years – it should be realised these numbers cover all firms in the industry. That is, both long- and newly-established firms.

3.7 Not surprisingly, the survival rates for new entrants to the BCI appears to be much lower than those for BCI firms as a whole (that is, including longer established firms), as can be seen in Graph 6.

Graph 6: BCI Firms – Survival Rates by Firm Age



3.8 The survival rate profile for all BCI firms and newly established BCI firms is fairly similar for the first year of reported activity (that is, 2012/13).

3.9 However, the survival rate for newly established firms in the BCI deteriorates at a greater rate for the second and third years:

- whereas 64 per cent of all BCI firms are operating after 2 years, just 56 per cent of newly established firms are doing so;
- while the 'still operating after three years' figures are 57 per cent and 47 per cent respectively.

3.10 Clearly, newly established businesses in the BCI have a lower survival/ higher failure rate than longer established businesses.

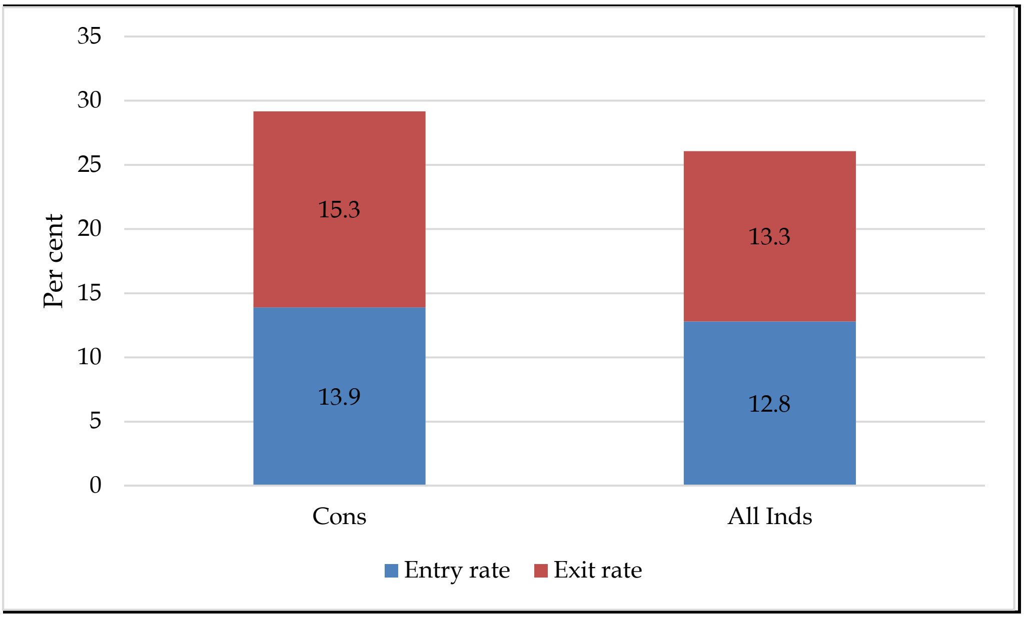
3.10.1 But, a failure rate of more than 53 per cent – or more than one-in-two firms in just three years for newly established firms - must be a cause for concern.

4 Construction vs All Industries

4.1 Another perspective on the entry/exit/churn and the survival/failure rates for firms in the BCI can be obtained by comparing them to those for other industries, a good indicator of which is the All Industries average.

4.2 Graph 7 reports the entry and exit (and by summation, the churn) rates for firms in the BCI and in All Industries on average across the four years to 2014/15.

Graph 7: Construction vs All Industries – Entry, Exit and Churn Rates



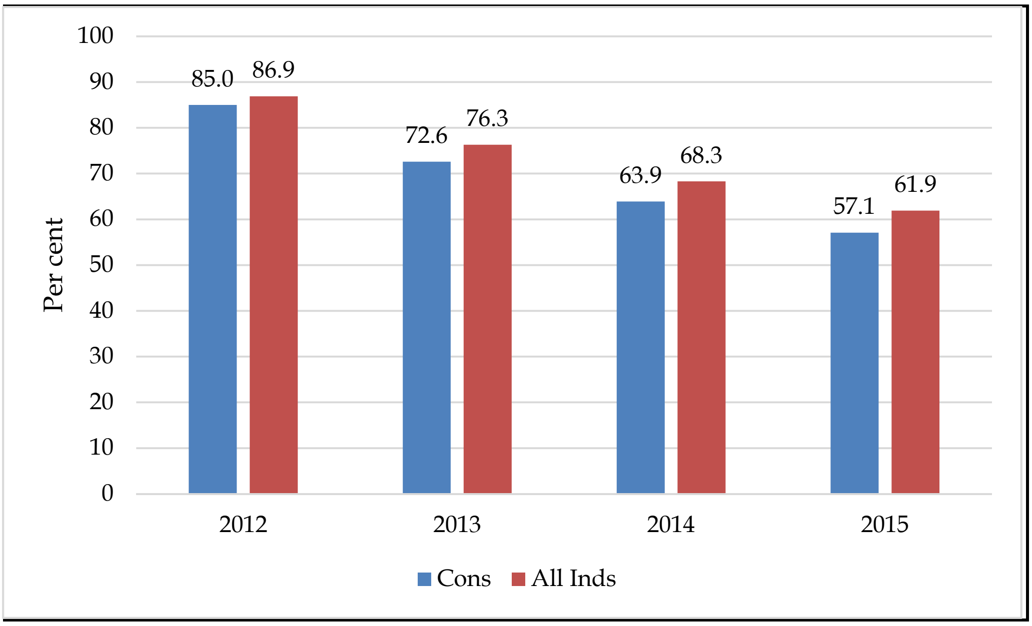
4.3 Several messages emerge from Graph 7, notably the average:

- entry rate for the BCI (13.9 per cent) was slightly higher than that for All Industries (12.8 per cent);
- exit rate for the BCI (15.3 per cent) was noticeably higher than that for All Industries (13.3 per cent); with,
- churn rate for the BCI (29.2 per cent) well clear of that of All Industries (at 26.1 per cent).

4.4 Looked at another way, two-thirds of the differences in the churn rate can be attributable to the higher exit rate in the BCI relative to All Industries, with the remaining one-third attributable to a higher entry rate.

4.5 This general pattern of higher exit rates for all BCI firms relative to all firms in All Industries is echoed in their survival rates, as can be seen in Graph 8.

Graph 8: Construction vs All Industries – Survival Rates



4.6 In general terms, the survival rates for all firms in All Industries exceeded that for all firms in the BCI across the four years to 2014/15.

4.7 However, of particular note must be the tendency for the gap between the All Industries and the BCI firms survival rate to widen over time:

- from 1.9 percentage points in 2011/12, to 3.7 percentage points in 2012/13; and,
- then to 4.4 percentage points in 2013/14, and to 4.8 percentage points +in 2014/15.

4.8 Looked at another way, firms in the BCI have a greater likelihood of failing than do those in All Industries.

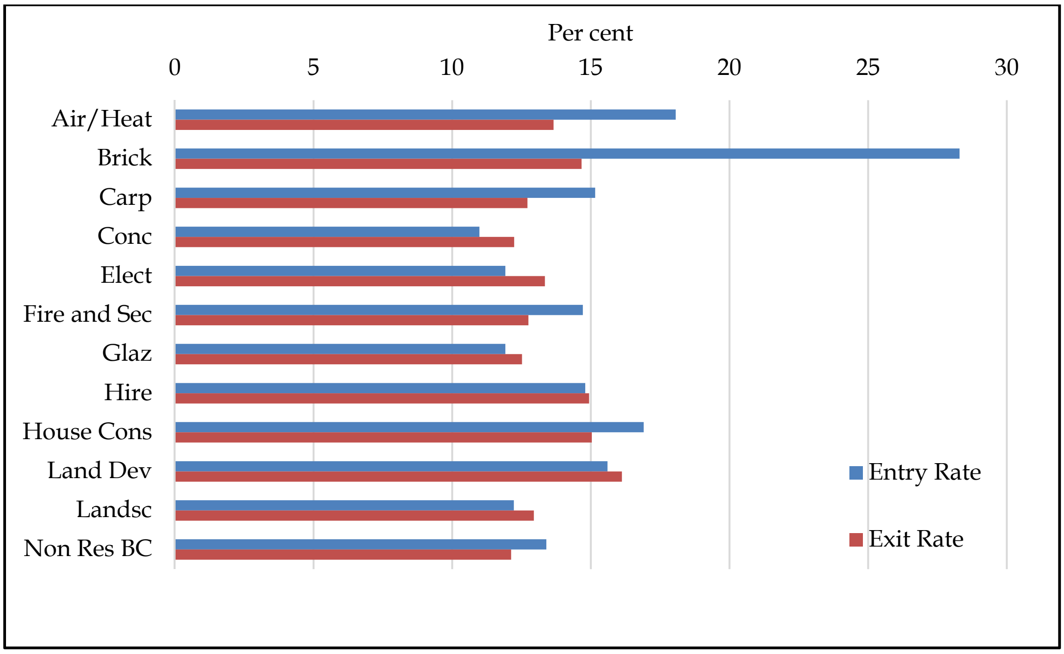
5 BCI Entry and Exit – By Sector

5.1 The ABS (ABS, 2016) usefully reports business entry and exit rates for 24 sub-sectors within the BCI for the 2014/15 financial year, visual summaries of which for All Firms are reported in Graphs 9 and 10.

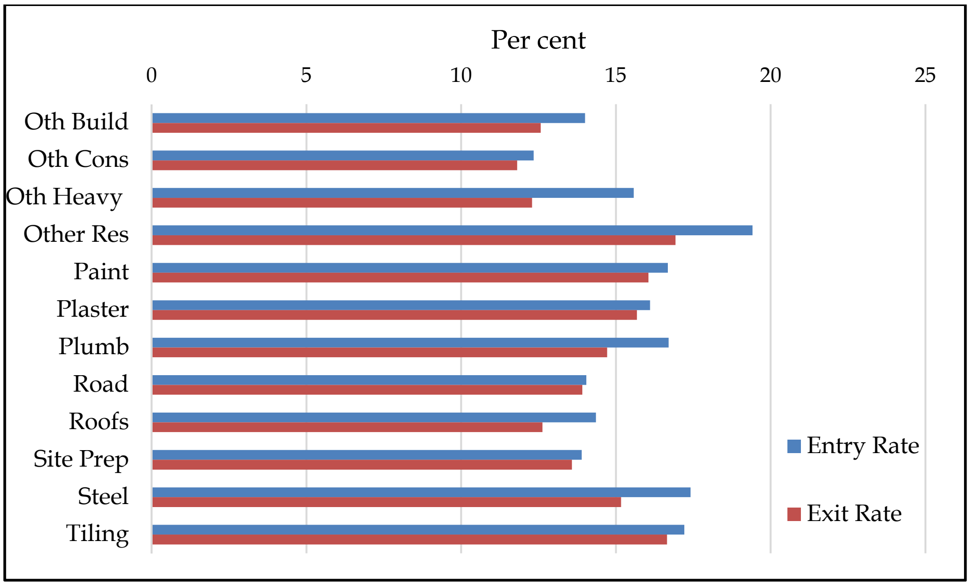
5.1.1 Graph 9 reports the results for the first 12 sub-sectors, by alphabetic order, and Graph 10 reports the results for the second 12 sub-sectors on the same basis.

5.1.2 The primary data for Graphs 9 and 10, and the mnemonics (codes) for the sub-sectors can be found in Appendix 1.

Graph 9: BCI Entry and Exit by Sub-Sector I – All Firms



Graph 10: BCI Entry and Exit by Sub-Sector II – All Firms



5.2 Looking first at entry rates for all firms in the BCI by sub-sector in 2014/15:

- the highest entry rates were experienced in bricklaying (Brick: 28.3 per cent), other residential building construction (Other Res: 19.4 per cent), air-conditioning and heating services (Air/Heat: 18.1 per cent) and structural steel erection services (Steel: 17.4 per cent); while,

- the lowest entry rates were experienced in concreting services (Conc: 11.0 per cent), electrical services (Elect: 11.9 per cent), glazing services (Glaz: also 11.9 per cent), and landscape construction services (Landsc: 12.2 per cent).

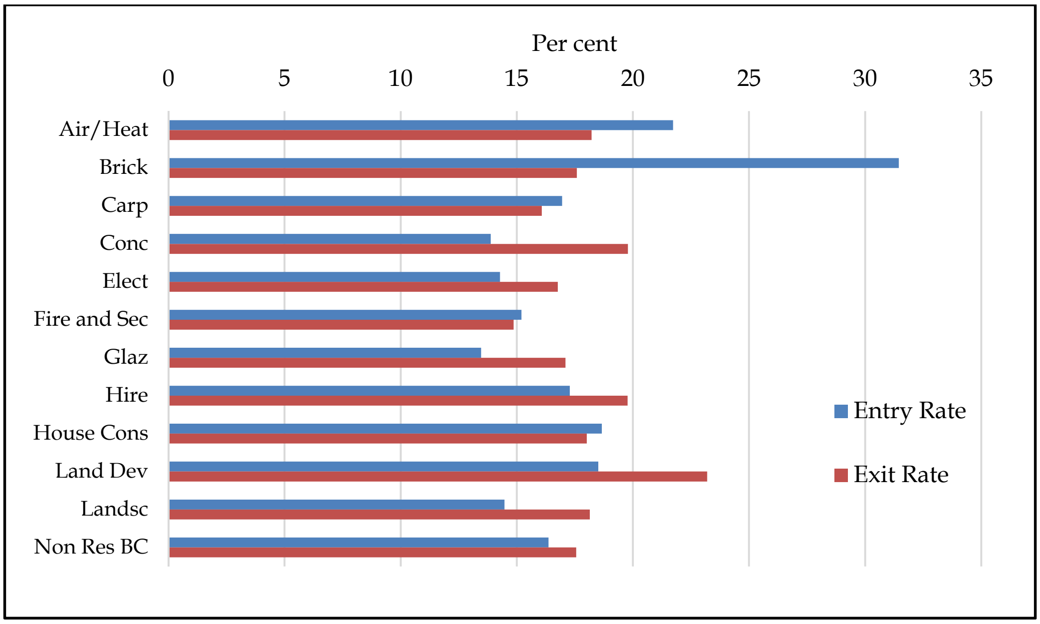
5.3 Not surprisingly, the sub-sectors with the highest entry rates also saw the greatest increases in net entries (that is, entries less exits) – Brick = 13.6 per cent; Other Res = 2.5 per cent; Air/Heat = 4.4 per cent; and, Steel = 2.2 per cent.

5.3.1 Similarly, the sub-sectors with the lowest entry rates also saw the greatest increases in net exits - Conc = -1.3 per cent; Elect = -1.4 per cent; Glaz = -0.6 per cent; and, Landsc = -0.7 per cent.

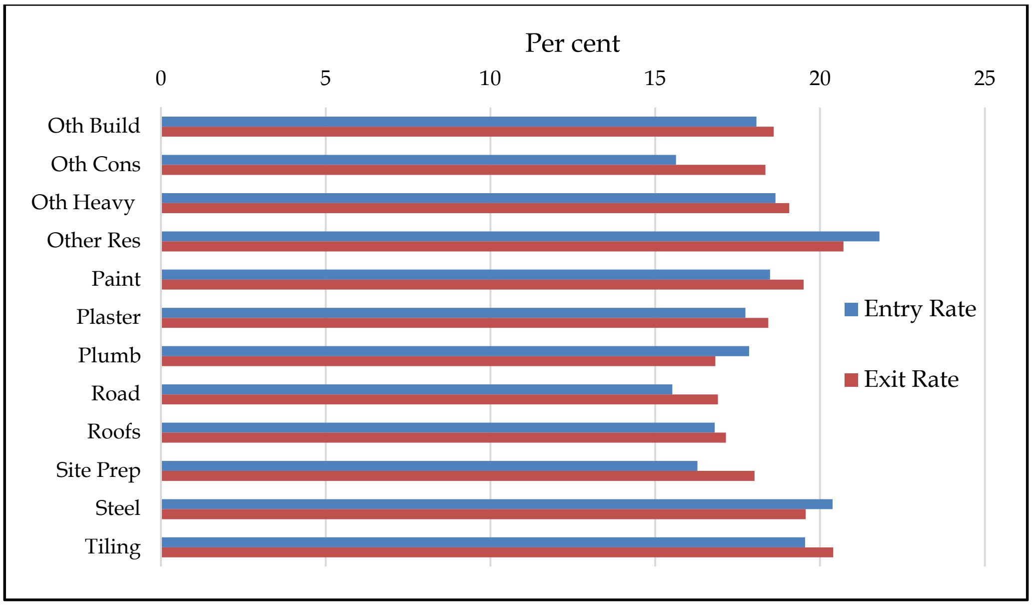
5.4 Similar information can be extracted for Non-Employing Firms, which can be seen as indicative of the survival/ failure rates of both new entrants to the BCI and/or those who have deliberately chosen, for whatever reasons, to operate as sole traders.

5.5 Graphs 11 and 12 essentially replicate the data for Non-Employing firms in the BCI reported in Graphs 9 and 10 for All Firms in the BCI. The primary data are reported in Appendix 2.

Graph 11: BCI Entry and Exit by Sub-Sector I – Non-Employing Firms



Graph 12: BCI Entry and Exit by Sub-Sector II – Non-Employing Firms



5.6 The entry and exit profile for non-employing firms in the BCI is fairly similar to that for all firms in the BCI in the 2014/15 financial year:

- the highest entry rates for non-employing firms were seen in bricklaying (31.5 per cent), other residential building construction (21.8 per cent), air conditioning and heating (21.7 per cent) and structural steel erection (20.4 per cent); while,

- the highest exit rates were seen in land development and sub-division (23.2 per cent), other residential building construction (20.7 per cent), tiling and carpeting (20.4 per cent), and concreting, and machinery hire (both 19.8 per cent).

6 Bibliography

Australian Bureau of Statistics (2016) “Counts of Australian Businesses, including Entries and Exits, June 2011 to June 2015”, Australian Bureau of Statistics, Cat No 8165.0, Canberra

7 Appendix 1: All Firms

BCI –Subsector (All Firms)	Mnemonic	Entry Rate (%)	Exit Rate (%)
Air Conditioning and Heating Services	Air/Heat	18.1	13.7
Bricklaying Services	Brick	28.3	14.7
Carpentry Services	Carp	15.2	12.7
Concreting Services	Conc	11.0	12.2
Electrical Services	Elect	11.9	13.3
Fire and Security Alarm Installation Services	Fire and Sec	14.7	12.8
Glazing Services	Glaz	11.9	12.5
Hire of Construction Machinery with Operator	Hire	14.8	14.9
House Construction	House Cons	16.9	15.0
Land Development and Subdivision	Land Dev	15.6	16.1
Landscape Construction Services	Landsc	12.2	12.9
Non-Residential Building Construction	Non Res BC	13.4	12.1
Other Building Installation Services	Oth Build	14.0	12.6
Other Construction Services n.e.c.	Oth Cons	12.3	11.8
Other Heavy and Civil Eng. Construction	Oth Heavy	15.6	12.3
Other Residential Building Construction	Other Res	19.4	16.9
Painting and Decorating Services	Paint	16.7	16.1
Plastering and Ceiling Services	Plaster	16.1	15.7
Plumbing Services	Plumb	16.7	14.7
Road and Bridge Construction	Road	14.0	13.9
Roofing Services	Roofs	14.4	12.6
Site Preparation Services	Site Prep	13.9	13.6
Structural Steel Erection Services	Steel	17.4	15.2
Tiling and Carpeting Services	Tiling	17.2	16.7

8 Appendix 2: Non – Employing Firms

BCI -Subsector	Mnemonic	Entry Rate (%)	Exit Rate (%)
		No Emp	No Emp
Air Conditioning and Heating Services	Air/Heat	21.7	18.2
Bricklaying Services	Brick	31.5	17.6
Carpentry Services	Carp	17.0	16.1
Concreting Services	Conc	13.9	19.8
Electrical Services	Elect	14.3	16.8
Fire and Security Alarm Installation Services	Fire and Sec	15.2	14.9
Glazing Services	Glaz	13.5	17.1
Hire of Construction Machinery with Operator	Hire	17.3	19.8
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Other Construction Services n.e.c.	Oth Cons	15.6	18.3
Other Heavy and Civil Eng. Construction	Oth Heavy	18.7	19.1
Other Residential Building Construction	Other Res	21.8	20.7
Painting and Decorating Services	Paint	18.5	19.5
Plastering and Ceiling Services	Plaster	17.7	18.4
Plumbing Services	Plumb	17.8	16.8
Road and Bridge Construction	Road	15.5	16.9
Roofing Services	Roofs	16.8	17.1
Site Preparation Services	Site Prep	16.3	18.0
Structural Steel Erection Services	Steel	20.4	19.6
Tiling and Carpeting Services	Tiling	19.5	20.4

ATTACHMENT B

Master Builders Australia

Submission to Productivity Commission on the Draft Report –

Inquiry into Business Set-up, Transfer and Closure

6 July 2015

MASTER BUILDERS AUSTRALIA

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CONTENTS

1 Introduction

1.1 Master Builders Australia is the nation's peak building and construction industry association which was federated on a national basis in 1890. Master Builders Australia's members are the Master Builder state and territory Associations. Over 125 years the movement has grown to over 33,000 businesses nationwide, including the top 100 construction companies. Master Builders is the only industry association that represents all three sectors, residential, commercial and engineering construction.

1.2 The building and construction industry is a major driver of the Australian economy and makes a major contribution to the generation of wealth and the welfare of the community, particularly through the provision of shelter. At the same time, the wellbeing of the building and construction industry is closely linked to the general state of the domestic economy.

2 Purpose of Submission

2.1 Master Builders welcomes the opportunity to provide a response to a number of the key issues raised in the draft report of the Productivity Commission's Inquiry into Business Set-up, Transfer and Closure. We commend the Productivity Commission for the depth and quality of its work.

2.2 This response builds on our original submission to the inquiry and emanates from our review of a number of the key elements of the draft report.

2.3 Attachment A to this submission is our submission to the Senate Economic References Committee on Insolvency. Master Builders, in that submission, highlights the importance of the current inquiry. We ask that the matters set out in that submission be taken into account by the Productivity Commission in the finalisation of the current inquiry.

3 Central Concern: Less Regulation

3.1 The central themes of the inquiry – the incidence of business entry and exit, and strategies for reducing business entry and exit (particularly relating to regulation) – are of central importance to the building and construction industry.

3.2 As we highlighted in the original submission, the building and construction industry accounts for almost eight per cent of gross national product, and more than nine per cent of employment, in Australia. At the same time, owner-occupied housing and other property investments account for more than two-thirds of the asset portfolios and the wealth of ordinary Australians.

3.3 The inquiry is also important for the building and construction industry given the entry and exit rates for the industry relative to the national average. While business entry rates for the building and construction industry are around the national average (both around 14 per cent per annum) the exit rates are noticeably different (15 per cent compared to 13 per cent). This issue is elaborated in Attachment A.

3.4 A key theme of our original submission related to the burden of regulation imposed on businesses, especially small businesses, in the building and construction industry, and the implications for housing supply and affordability.

3.5 The compliance and reporting burden of regulation diverts scarce resources away from entrepreneurial and innovative activities into (often unproductive) form-filling. This point has been echoed in messages emerging from focus groups conducted by Master Builders with builder-members on, inter alia, the priorities for regulation reform.

3.6 As one builder told us:

> *Battling with regulations and bureaucrats is taking me away from building my business. I should be out winning jobs and doing business.*

3.7 Further in the words of another builder:

> *Have a look at everyone who regulates the building industry: the ABCB; Standards Australia; the Banks (as sources of finance); the insurance companies (given they provide insurance cover, when you can get it); local governments (God help us); and, the various State fair trading and consumer protection agencies. (No wonder) you have to price red tape into your quote.*

3.8 Anecdotal evidence provided to Master Builders by our builder-members indicates regulations add between eight and twelve per cent to the cost of construction of the average Australian residential dwelling.

3.9 Against this background, Master Builders was looking to the Productivity Commission to make bold recommendations for rationalising and reducing the regulatory burden imposed upon business, especially small business, and for facilitating reform of the broader regulatory processes. In this regard, the primary recommendation in this context (Draft Recommendation 3.1) does not go far enough.

3.10 While Draft Recommendation 3.1 usefully reminds readers of the numerous reports and studies previously undertaken by the Productivity Commission which touch upon regulation review and reform, Master Builders would have anticipated more definitive recommendations of direct benefit to industry, and the building and construction industry in particular. These comments are given further impetus by the statements in the draft report which emphasise the restrictions imposed by government regulation. An example is at page 270 of the draft report where it is noted that:

> *Government assistance for business is less effective in the face of broader, persistent regulatory impediments.*

3.11 As we argued in our original submission, there are a number of priority areas where further meaningful action is required, all of which will contribute to reducing the regulatory burden imposed on businesses in the building and construction industry. These include:

- substantially reducing State, Territory and local Government variations to the National Construction Code (NCC) (discussed at paragraphs 7.8 to 7.10 of our original submission);

- eliminating the differential classification and treatment of employees and sub-contractors within and between jurisdictions (discussed at paragraphs 7.11 to 7.15); and,

- improving third-party regulatory processes, especially where these regulations and their associated requirements are imported and/or referenced in federal Government et al regulatory instruments (discussed at paragraphs 7.16 to 7.22).

3.12 Master Builders recommends the Productivity Commission re-examine these proposals for their inclusion in the final report of the inquiry and, at the same time, prioritise the leading practices from prior reports that the Commission believes should be implemented.

4 Two Specific Issues

4.1 Standard Form Contracts

The discussion at page 218 of the draft report has been overtaken by the introduction of the Treasury Legislation Amendment (Small Business and Unfair Contract Terms) Bill 2015.

4.2 Business Structures

Figure 4.4 contains very useful data. However, the construction of the graph makes it difficult to follow the various percentage figures. We would ask that these be made more discernible and any more research in relation to the rationale for the adoption of differing structures by sector be published. This is because this material is very useful in other contexts, for example as highlighted in the text at page 293 of the draft report.

5 Phoenix Activity

5.1 The draft report also addresses (at pages 379 – 384) the issue of what are sometimes called 'phoenix companies' – that is, firms which have previously failed, for whatever reason (but in the main illegitimate), re-engaging in business in a new corporate form. The Commission, in the draft report, seeks comment on the merit, or otherwise, of allowing courts of competent jurisdiction to 'pierce the corporate veil' to require parent or related companies to pay the debts of insolvent or related entities, and the complications which this approach may involve.

5.2 Master Builders supports measures which would operate to act against the fraudulent 'phoenixing' of companies. Our policy on phoenix company activity was communicated to the then Government at the time of the release of the Cole Royal Commission Report into the Building and Construction Industry.[1]

5.3 The Royal Commissioner discussed at some length the issue of fraudulent phoenix company activity in the building and construction industry. That

[1] Final report of the Royal Commission into the building and construction industry February 2003 http://www.royalcombci.gov.au/hearings/reports.asp

discussion is commended in the current context. Master Builders supports measures which would operate to act against the fraudulent phoenixing of companies. Fraudulent phoenix activity involves the evasion of tax and other liabilities such as employee entitlements through the deliberate, systematic and sometimes cyclic liquidation of related corporate trading entities and is, unfortunately, an activity that has been detected in the building and construction industry.

5.4 As stated at paragraph 5.2 Master Builders' policy on phoenix company activity was communicated to Government at the time of the release of the Cole Royal Commission Report into the Building and Construction Industry. Chapter 12 of Volume 8 of his report is devoted to this subject. At the time, Master Builders supported a number of the recommendations that were made by the Royal Commissioner. Recommendation 106, in particular, related to the need for greater scrutiny of ASIC registers and better enforcement of the current law. The issue and recommendation is as follows:

> *There is evidence of persons associated with fraudulent phoenix company activity in the building and construction industry being appointed as directors of companies operating in the building and construction industry, although they are bankrupt and disqualified to act as directors, without being detected by the regulatory authorities.*
>
> *The measures developed by the Australian Securities and Investments Commission to check all new company officers against the national Personal Insolvency Index and to check that current directors have not been declared bankrupt appear to address this issue and should be implemented without further delay.*[2]

5.5 The Productivity Commission's draft report reflects these sentiments (at Draft Recommendation 15.8), proposing section 117 of the *Corporations Act* 2001 (Commonwealth) be amended to require, at the time of company registration, directors to provide a Director Identity Number (DIN), obtainable from the Australian Securities and Investment Commission (ASIC) based on a '100 point proof of identity'.

5.6 Master Builders agrees that the introduction of simple safeguards around identification of company directors would assist along the lines of the Cole Royal Commission recommendation just cited. Recommendation 15.8 could

[2] Ibid Vol 8 Chapter 12 at 165

be expanded to encompass the Cole Recommendation as we do not believe all new company officers are subject to the relevant scrutiny. We note in particular, the introduction of a director identification number, underpinned by an identification process along the lines of the 100 point identity check required to establish a bank account, would enable the monitoring of director registration (including the detection of disqualified or fraudulent directors), the collection of data regarding director appointments over time (to establish patterns of director involvement in repeat business failures) and detection of possible fraudulent and phoenix activity by the Inter-agency Phoenix Forum and investors.

5.7 Whilst this measure alone will not solve the problem, it will assist with the current enforcement of the law, a matter that the Productivity Commission has indicated is the main problem with the issue of phoenix activity (p382 Draft Report). We commend draft recommendation 15.8 and its expansion as proposed above.

6 Conclusion

6.1 Master Builders would welcome an opportunity to further discuss this submission with the Commission.

6.2 We look forward to the release of the final report.

****

ATTACHMENT C

Master Builders Australia

Business Entry and Exit

in the

Building and Construction Industry

12 March 2015

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1 Introduction

1.1 Master Builders Australia is the nation's peak BCI association which was federated on a national basis in 1890. Master Builders Australia's members are the Master Builder State and Territory Associations.

1.2 Over 125 years the movement has grown to over 32,000 businesses nationwide, including the top 100 construction companies. Master Builders is the only industry association that represents all three sectors, residential, commercial and engineering construction.

1.3 The Building and Construction Industry (BCI) is a major driver of the Australian economy and makes a major contribution to the generation of wealth and the welfare of the community, particularly through the provision of shelter.

1.4 At the same time, the wellbeing of the BCI is closely linked to the general state of the domestic economy

2 Overview

2.1 Master Builders Australia welcomes the Productivity Commission Inquiry (the Inquiry) into barriers to entries and exits of business in the Australian economy. We particularly welcome the attention to be given to the impact of regulation in business start-up and close down.

2.2 The Inquiry is important for the BCI given:

- while the entry (start-up) rate for new firms in the industry was around the all-industry average; and,
- the exit (close down) rate for new firms in the industry was noticeably above the all-industry average.

2.3 Of particular concern are the high attrition rates for new firms created within the BCI, with:

- 27 per cent of new firms closing their doors within just one year of start-up; and,
- 45 per cent within two years, and 56 per cent within three years, of starting operation.

2.4 Such attrition rates must be a matter for concern, pointing to losses of skills, entrepreneurship and competition within the BCI, and to the wider Australian economy.

2.5 Master Builders believes decisive action is required in two key areas to improve business entry, and to reduce business exit, rates in the BCI, and the economy more generally.

2.6 These priority areas are regulation reform, and business skills training.

2.7 In the area of regulation reform, Master Builders calls for meaningful action to, inter alia:

- substantially reduce State, Territory and Local Government variations to the National Construction Code (NCC);
- eliminate the differential classification and treatment of employees and sub-contractors within and between jurisdictions; and,
- improve third-party regulatory processes, especially where these regulations and their associated requirements are imported and/or referenced in Federal Government et al regulatory instruments.

2.8 As one builder told Master Builders in a series of member-focus groups convened to discuss the issues before the current Inquiry:

> *Battling with regulations and bureaucrats is taking me away from building my business. I should be out winning jobs and doing business.*

And, another builder:

> *Have a look at everyone who regulates the building industry: the ABCB; Standards Australia; the Banks (as sources of finance); the insurance companies (given they provide insurance cover, when you can get it); local governments (God help us); and, the various State fair trading and consumer protection agencies. (No wonder) you have to price red tape into your quote.*

And, yet another builder:

> *We need seamless, back-to-back regulation, particularly between State and Local Governments.*
>
> *Can we do something about all of the local government variations to the National Construction Code.*

2.9 In the area of skills training, Master Builders calls for meaningful action to, inter alia:

- greater harmonisation of apprenticeship systems and public sector funding policies around the nation;
- the development of "Passports of Competencies"; and,
- wider industry-owned qualification and competency development.

2.10 A recurrent message from our member-focus groups, when discussion turned to the issue of skills training, was the need for greater emphasis on training in business skills. For example:

> *We do a good job teaching young blokes how to bang in a nail. But we need to teach (apprentices and young builders) more about business management.*
>
> *We need to do much more CPD (compulsory professional development), especially in how to run a business.*
>
> *We should add one or two modules on business management to Cert 4.*
>
> *Young blokes need more training in pricing work, managing cash flow, understanding their legal responsibilities, and in sales and marketing.*

3 Terms of Reference

3.1 The Federal Government has directed the Productivity Commission to undertake a review of barriers to entries and exits of business in the Australian economy.

3.2 Key amongst the Terms of Reference (see PC, 2014: iii), which sets the framework for the inquiry, are investigations into, inter alia:

- the nature and extent of business entry and exit, and the impact on Australia's economic performance; and,
- options and strategies for reducing barriers to entry and exit, ranging across, but not limited to, regulatory imposts by government, transfers and subsidies from governments, and personal and business insolvency regimes.

3.3 The Productivity Commission has released a useful Issues Paper (PC, 2014) which discusses several of these, and other related, issues, under two broad headings: barriers to new business entry and start-up; and barriers to business transfer or exit.

3.4 Under the sub-heading of ‘barriers to new business entry and start-up’, the Productivity Commission discusses topics such as regulatory barriers to commencing business, access to finance for newer firms, and constraints on new business structures.

3.5 Under the sub-heading of ‘barriers to business transfer or exit’, the Productivity Commission considers topics such as personal and corporate insolvency regimes, impediments to the transfer of ownership, and government assistance policies and programs acting as barriers to firm closure.

3.6 The Productivity Commission also raises the question of business and social attitudes to risk and innovation, in particular relating to firms who ‘tried and failed, and want to try again’ – in effect, our national attitude to entrepreneurship.

3.7 Master Builders’ submission seeks to address a number of these, and several other, important issues relating to business entry and exit from the standpoint of the BCI . These include:

- the entry and exit rates for firms in the industry, both in aggregate, and by sector within it; and,
- impediments to firm performance arising from poor regulatory design and practice, and from skills shortages.

3.8 The economic significance of the BCI is underscored by two important metrics:

- it accounts for almost 8 per cent of gross domestic product, and more than 9 per cent of employment, in Australia; and,
- owner-occupied housing and other property investments account for over two-thirds of the asset portfolio and wealth of ordinary Australians.

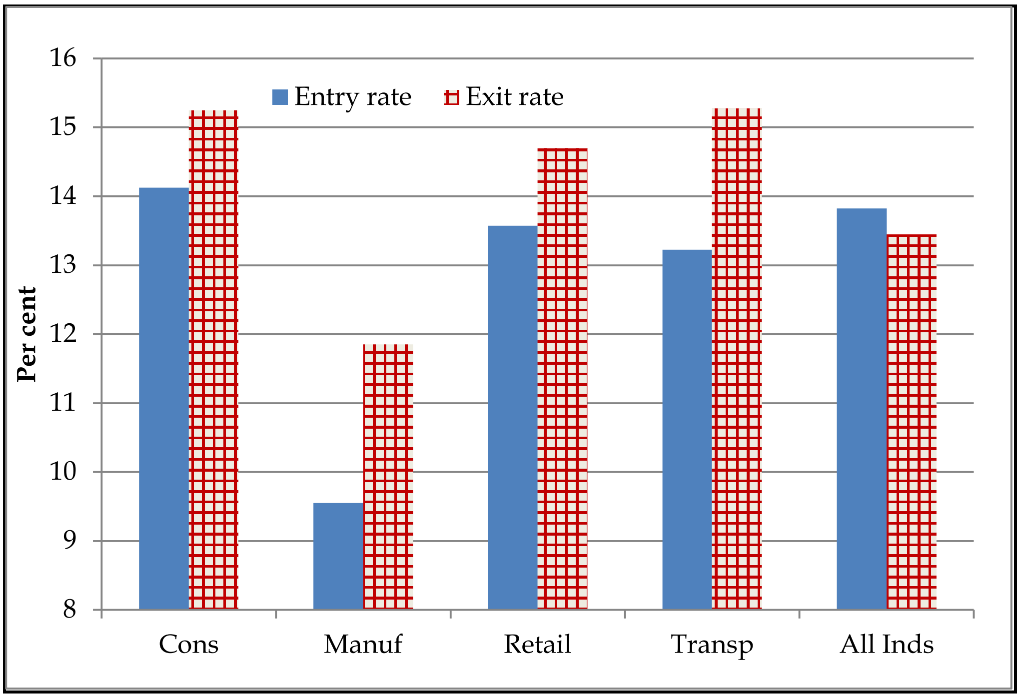
4 BCI Entry and Exit – In Aggregate

4.1 The Australian Bureau of Statistics (ABS, 2014) collections on business entry and exits provide one of the best quantitative insights into the creation and termination of commercial activity in Australia.

4.2 Amongst the main messages emerging from a careful review of this collection are some of Australia's key industries, including the fulcrum BCI are being caught in a tightening pincer of declining entry rates for new firms, and rising exit rates for existing firms.

4.3 Graph 1 reports the general pattern of business entries and exits for the BCI, the manufacturing, the retail and the transport industries, and an all-industry benchmark. All figures are entry or exit rates (that is, the number of entries or exits as a proportion of extant firms in the respective sectors), and are reported as averages for the four financial years up to and including 2012/13.

Graph 1: Business Entry and Exit for Selected Industries



4.4 The entry rate for new firms in the BCI averaged 14.1 per cent per annum in the four financial years under review. However, this average figure conceals a marked decline in the entry rate for the industry, from 16.7 per cent in 2009/10 to 10.3 per cent in 2012/13, or a fall of some 38 per cent in new start-ups.

4.5 The average <u>entry rate</u> for the:

- retail industry was 13.6 per cent per annum for the four years under review, falling from 17 per cent in 2009/10 to just 8.8 per cent in 2012/13;
- transport industry was 13.2 per cent per annum for the four years under review, dropping from 15.8 per cent in 2009/10 to 9.9 per cent in 2012/13; and,
- manufacturing industry was 9.6 per cent per annum for the four years under review, down from 11.6 per cent in 2009/10 to just 6.5 per cent in 2012/13.

4.6 The all-industry average entry rate for the four years under review was 13.8 per cent per annum (dropping from 16.7 per cent in 2009/10 to 11.2 per cent in 2012/13).

4.7 By comparison, the <u>exit rate</u> figures tell a much different story. For all four of the specific industry sectors under review – building and construction, manufacturing, retail, and transport – exit rates exceeded entry rates, on average, over the four years under review.

4.8 Exit rates for firms in the BCI averaged 15.3 per cent per annum, rising from 14.8 per cent in 2009/10 to 16.5 per cent in 2012/13, or an increase of just over 11 per cent in business closures. The average exit rate for the:

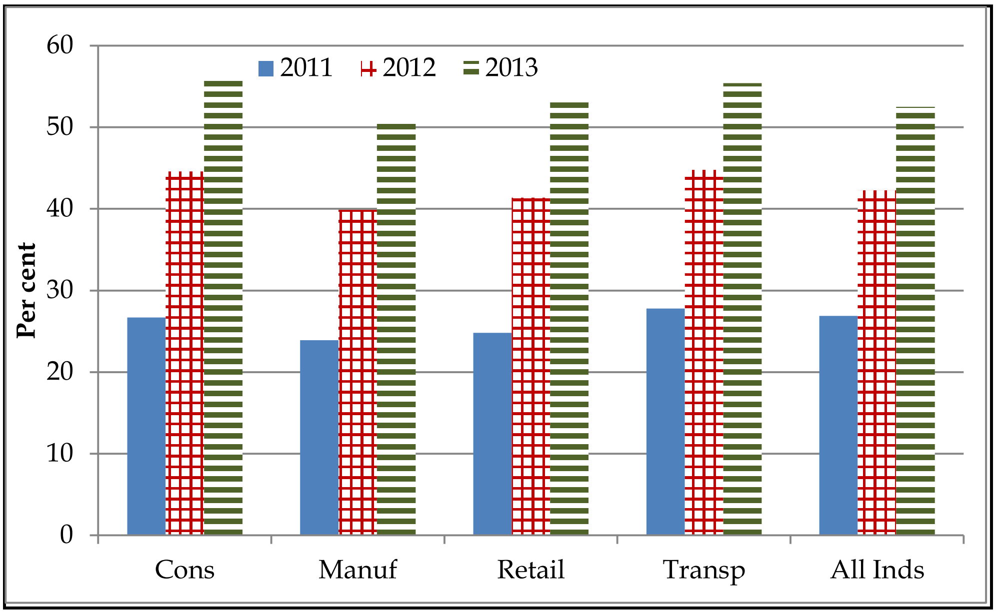
- retail industry was 14.7 per cent per annum for the four years under review, increasing from 14.0 per cent in 2009/10 to 15.7 per cent in 2012/13;
- transport industry was 15.3 per cent per annum for the four years under review, rising from 15.0 per cent in 2009/10 to 15.6 per cent in 2012/13; and,
- manufacturing industry was 11.9 per cent per annum for the four years under review, lifting from 11.8 per cent in 2009/10 to 12.5 per cent in 2012/13.

4.9 The all-industry average exit rate for the four years under review was 13.5 per cent per annum, moving from 13.1 per cent in 2009/10 to 14.1 per cent in 2012/13.

4.10 Another perspective on the entry and exit rates for businesses can be obtained from an examination of attrition and survival rates for new firms. The attrition and the survival rates are complements of each other: 100 – attrition rate = survival rate; or, 100 – survival rate = attrition rate.

4.11 Graph 2 reports the attrition rates for new firms in each of the industry sectors under review which commenced operation in 2010 – that is, essentially new, and most likely small, businesses.

Graph 2: Attrition Rates for New Firms in Selected Industries



4.12 The attrition rate for new firms established in 2010 in the BCI rose from 26.7 per cent of these firms after one year, to 44.6 per cent by the second year, to 56.1 per cent in the third year.

4.12.1 (All attrition rates are cumulative, so figures for the second year include those for the first year, with those for the third year including the two preceding years.) That is, over half of all new firms established in the BCI in 2010 had failed by 2013.

4.13 By comparison, the attrition rates for new firms established in the:

- manufacturing sector were 23.9 per cent in the first year, and 51 per cent by the third year;
- retail sector were 24.8 per cent in the first year, and 53.3 per cent by the third year; and,

- transport sector were 27.8 per cent in the first year, and 55.4 per cent by the third year.

4.14 The all-industries average attrition rates were 26.9 per cent in the first year, 42.3 per cent by the second year, and 52.5 per cent by the third year.

4.15 Nevertheless, it would at least appear the marginal rate of attrition (the change from one year to the next) appears to moderate with time, evident in the step-change in attrition between the third and second year of operation is smaller than that between second and first year of operation. However, further data collections and reports on business entries and exits will be required from the ABS to see if this 'flattening of the attrition rate curve' emerges for firms after four, five or more years in operation.

5 BCI Entry and Exit – By Sector

5.1 The ABS (ABS, 2014) also usefully reports business entry and exit rates for various sub-sectors within the BCI, summaries of which for the 2013 reporting year can be found in Tables 1 and 2, respectively.

Table 1: Entry Rates by Building Sector

	Entry Rate (%)	Entry Rate (%)	Entry Rate (%)
	All Firms	No Emps	1-19 Emps
Air Conditioning and Heating Services	9.4	11.6	7.8
Bricklaying Services	10.1	10.3	9.9
Carpentry Services	12.4	12.5	12.4
Concreting Services	11.2	11.7	10.9
Electrical Services	10.2	10.9	9.7
Fire and Security Alarm Install Services	8.1	8.4	8.2
Glazing Services	10.0	11.2	9.2
Hire of Cons. Machinery with Operator	4.5	3.4	6.4
House Construction	9.2	9.5	9.0
Land Development and Subdivision	4.8	4.9	4.6
Landscape Construction Services	9.9	10.8	8.8
Non-Residential Building Construction	7.7	7.0	9.6
Other Building Installation Services	9.9	9.1	11.0
Other Construction Services n.e.c.	12.0	12.1	12.4
Other Heavy and Civil Eng Construction	8.1	7.9	8.8
Other Residential Building Construction	7.4	7.1	8.6
Painting and Decorating Services	11.2	11.7	10.2
Plastering and Ceiling Services	14.6	14.4	15.1
Plumbing Services	9.9	11.5	8.4
Road and Bridge Construction	9.3	8.2	11.7
Roofing Services	12.5	14.4	11.0
Site Preparation Services	9.6	9.1	10.8
Structural Steel Erection Services	11.4	10.6	13.0
Tiling and Carpeting Services	11.4	10.7	13.2
Mean	9.8	10.0	10.0
Std Dev	2.3	2.7	2.3
CV	0.23	0.27	0.23
Min	4.5	3.4	4.6
Max	14.6	14.4	15.1

5.2 Looking first at entry rates for all firms in the BCI :

- the highest entry rates were experienced in the plastering and ceiling (14.8 per cent), roofing services (12.5 per cent) and carpentry services (12.4 per cent) sectors; and,
- the lowest entry rates were experienced in the hire of machinery with operator (4.5 per cent), the land development and subdivision (4.8 per cent) and the other residential building construction (7.4 per cent) sectors.

- The overall entry rate for all firms in the BCI was 9.8 per cent.

5.3 Turning to entry rates for firms without employees (essentially sole traders) the pattern is broadly similar to that for all firms:

- the highest entry rates were experienced in the plastering and ceiling (14.4 per cent), roofing services (14.4 per cent) and carpentry services (12.5 per cent) sectors; and,
- the lowest entry rates were experienced in the hire of machinery with operator (3.4 per cent), the land development and subdivision (4.9 per cent) and the other residential building construction (7.0 per cent) sectors.
- The overall entry rate for firms without any employees was 10.0 per cent.

5.4 The entry rate profile for firms in the BCI employing between 1 and 19 persons is slightly different:

- the highest entry rates were experienced in the plastering and ceiling (15.1 per cent), tiling and carpeting services (13.2 per cent) and structural steel erection services (13.0 per cent) sectors; and,
- the lowest entry rates were experienced in the land development and subdivision (4.6 per cent), the hire of construction machinery with operator (6.4 per cent) and the air-conditioning and heating services (7.8 per cent) sectors.
- The overall entry rate for firms employing between 1 and 19 persons was 10.0 per cent.

Table 2: Exit Rates by Building Sector

	Exit Rate (%)	Exit Rate (%)	Exit Rate (%)
	All Firms	**No Emps**	**1 - 19 Emps**
Air Conditioning and Heating Services	11.9	16.2	7.2
Bricklaying Services	12.6	13.4	7.3
Carpentry Services	17.5	19.2	7.2
Concreting Services	15.2	20.2	7.5
Electrical Services	12.9	22.0	7.8
Fire and Security Alarm Instal Services	15.4	21.2	9.8
Glazing Services	15.3	19.0	8.4
Hire of Cons Machinery with Operator	13.2	26.5	8.8
House Construction	13.9	18.2	8.3
Land Development and Subdivision	13.2	20.3	8.2
Landscape Construction Services	19.5	23.3	9.2
Non-Residential Building Construction	15.8	25.7	8.4
Other Building Installation Services	13.7	19.6	13.2
Other Construction Services n.e.c.	15.0	20.7	10.8
Other Heavy and Civil Eng Construction	20.0	20.1	7.5
Other Residential Building Construction	14.0	21.8	10.3
Painting and Decorating Services	17.2	19.2	11.9
Plastering and Ceiling Services	17.5	23.0	11.2
Plumbing Services	18.9	23.5	8.2
Road and Bridge Construction	17.5	20.2	11.6
Roofing Services	20.4	25.1	11.3
Site Preparation Services	18.7	22.2	11.8
Structural Steel Erection Services	19.0	26.5	12.5
Tiling and Carpeting Services	22.8	26.6	14.1
Mean	16.3	21.4	9.7
Std Dev	2.9	3.3	2.1
CV	0.18	0.15	0.22
Min	11.9	13.4	7.2
Max	22.8	26.6	14.1

5.5 Looking first at exit rates for all firms in the BCI :

- the highest exit rates were experienced in the plastering and ceiling (22.8 per cent), other construction services (20.4 per cent) and the bricklaying (20.0 per cent) sectors; and,
- the lowest exit rates were in the hire of construction machinery with operator (11.9 per cent), land development and sub-division (12.6 per cent), and fire and security alarm installation (12.9 per cent) sectors.

- The overall exit rate for all firms was 16.3 per cent, which was well above the entry rate for all firms of 9.8 per cent (a 6.5 percentage point difference).

5.6 For firms without employees:

- the highest exit rates were experienced in the plastering and ceiling (26.6 per cent), roofing services, and other building installation services (both at 26.5 per cent) sectors; and,
- the lowest exit rates were experienced in the land development and subdivision (13.4 per cent), the hire of machinery with operator (16.2 per cent),) and the site preparation (18.2 per cent) sectors.
- The overall exit rate for firms without any employees was 21.4 per cent, more than double the entry rate for such firms of 10.0 per cent.

5.7 For firms employing between 1 and 19 persons:

- the highest exit rates were experienced in the plastering and ceiling (14.1 per cent), bricklaying services (13.2 per cent) and the tiling and carpeting services (12.5 per cent) sectors; and,
- the lowest exit rates were experienced the air-conditioning and heating services, and the land development and subdivision (both 7.2 per cent), and the hire of construction machinery with operator (7.3 per cent) and sectors.
- the overall exit rate for firms employing between 1 and 19 persons was 9.7 per cent, compared to an entry rate for such firms of 10.0 per cent.

5.8 While there is a plethora of information contained in Tables 1 and 2 regarding entry and exit rates across 24 sectors across three types of firms in the BCI , of particular note must be the relatively high exit rates experienced by firms with no employees, averaging just over 21 per cent (or one-in-five of such firms).

5.9 This relatively high exit rate should be a matter for concern, suggesting a potential wastage of training, and losses of skills, entrepreneurship and competition within the sectors concerned, and the BCI. However, it is not clear, or discernible from these aggregate figures, where these people go.

5.10 If they exit the industry completely, then there are substantial losses of investments in training, of entrepreneurship and competition, and of future capacity in the industry. However, if they transition from being firms with no employees to being firms with between 1 and 19 employees (even by taking on a single employee, such as an apprentice) then there may well be no loss (indeed, even a gain) to the industry.

5.11 Unfortunately, absent rigorous time series-panel data, such as regular and up-to-date releases of the ABS Business Longitudinal Database, it is not possible to say with any degree of certainty the operational trajectories of such firms.

6 Constraints and Challenges

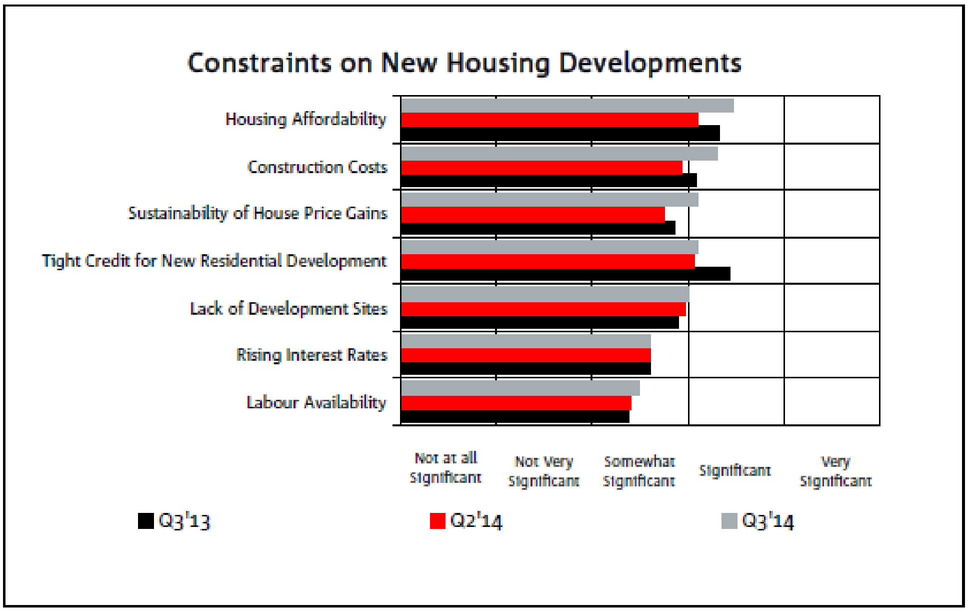
6.1 Master Builders is not aware of any specific, published detailed analyses of the drivers of business commencements and terminations in the BCI. However, an insight into some of the pressures on firms in the industry can be obtained from indicators published by the National Australia Bank for both the residential property (NAB, 2014a) and commercial property (NAB, 2014b) sectors.

6.2 The NAB's residential property survey asks respondents to comment upon constraints experienced on new housing developments and on demand for existing property, while its commercial property survey asks respondents to comment upon the critical challenges likely to confront the sector over the coming year.

6.2.1 These constraints (for residential property) and challenges (for commercial property) can be viewed as proxy indicators of likely stresses being experienced by firms in, and possible drivers for their exit from, the BCI.

6.3 Graphs 4 and 5 report constraints being experienced within the residential housing sector (NAB, 2014a) while Graph 6 reports on the challenges being confronted by the commercial property sector (NAB, 2014b).

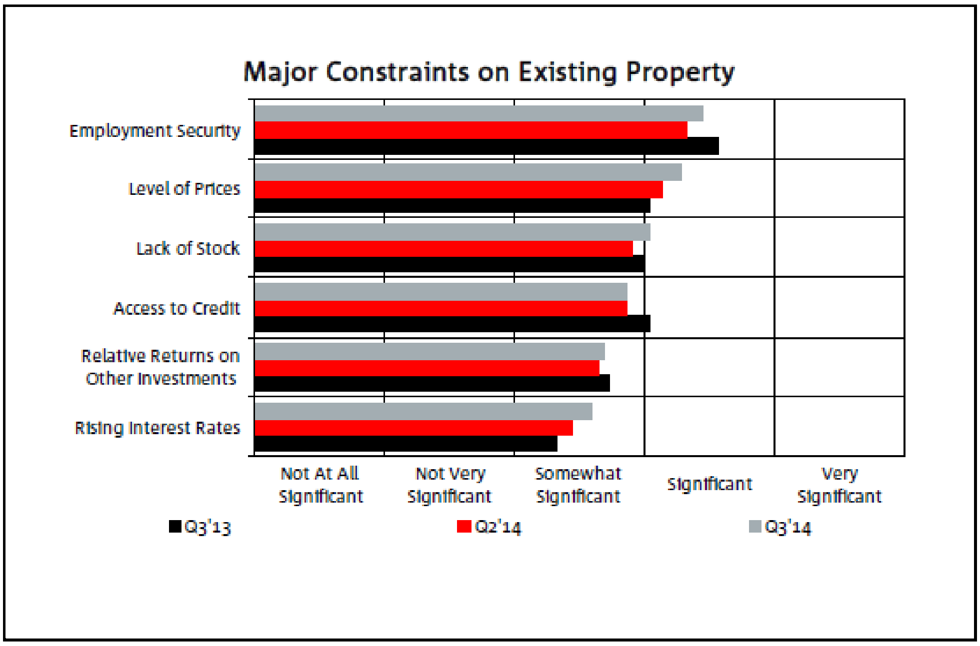
Graph 4: Constraints on New (Residential) Housing Developments



6.4 The most significant constraints on new housing development borne by the residential building sector relate to housing affordability, construction costs, tight credit for new residential development, and lack of development sites.

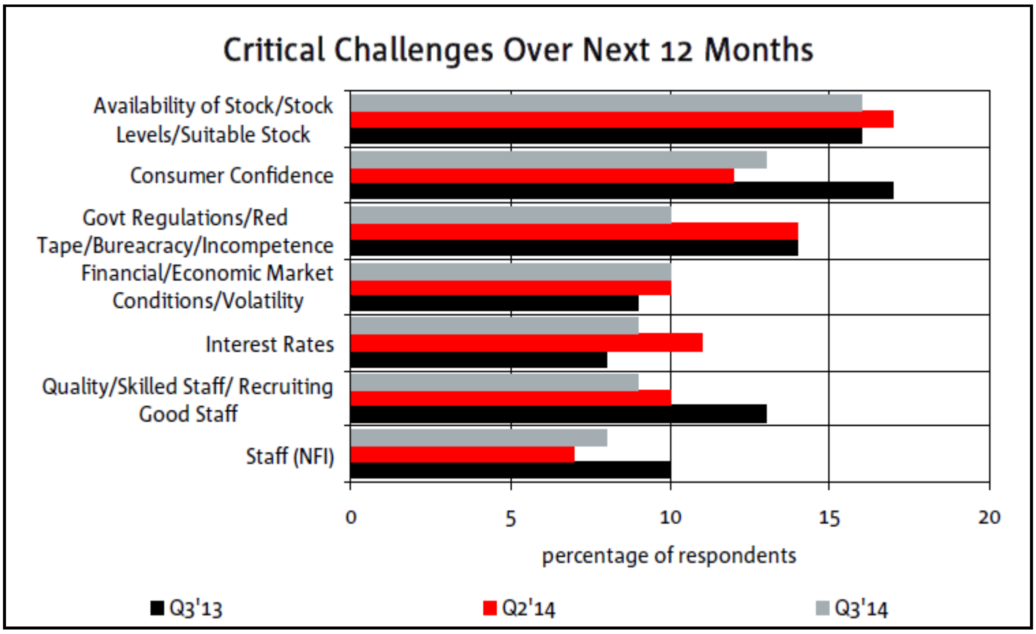
6.4.1 Constraints such as housing affordability and lack of development sites (both of which capture elements such as inadequate land supply, and poor planning and zoning arrangements), and construction costs (which can capture inefficient and unnecessary regulatory environments) can be traced back to government failure.

Graph 5: Major Constraints on Existing (Residential) Property



6.5 The most significant constraints on the existing residential property sector are essentially macroeconomic in nature, namely employment security and inflation (level of prices), although lack of stock and access also generally rank as somewhat significant barriers.

Graph 6: Critical Challenges for Commercial Property



6.6 The most important critical challenges confronting the commercial property sector are the availability of suitable stock, consumer confidence and poor government regulation/bureaucratic incompetence, the latter of which is indicative of government failure.

7 Regulations

7.1 Regulation, whether 'red' or 'green' tape, is a significant burden on the BCI, which is one of the most intensely regulated in Australia, with regulation imposed by all three tiers of government.

7.2 The compliance and reporting burden of regulation diverts scarce business resources away from entrepreneurial and innovative activities into form-filling (often of duplicative and/or of questionable value), and in the BCI this adds to the cost of housing supply and thus compounds other housing affordability stresses.

7.2.1 Anecdotal evidence provided to Master Builders by our rank-and-file members indicates regulations add between eight and twelve per cent to the cost of construction of the average Australian residential dwelling.

7.3 The Abbott Government has adopted an active and constructive regulation review, reform and repeal (4R) agenda, into which Master Builders has and will continue to advocate for a less burdensome and more efficient approach to regulation, in its design, in its administration, and in compliance.

7.4 In this context, Master Builders welcomes key initiatives taken by the Abbott Government, such as:

- publication of its "Australian Government Guide to Regulation", which will strengthen and make more transparent the regulatory development processes of federal agencies;
- publication of its "Regulator Performance Framework", which will improve the consistency and the transparency with which regulators undertake their responsibilities; and,
- twice-yearly regulation repeal days, which have, to date, made useful contributions to eliminating redundant regulations (although a sizeable challenge remains).

7.5 Nevertheless, Master Builders has identified a number of priority areas where further meaningful action is required, all of which will contribute to reducing the regulatory burden imposed on businesses in the BCI.

7.6 These include:

- substantially reducing State, Territory and Local Government variations to the National Construction Code (NCC);
- eliminating the differential classification and treatment of employees and sub-contractors within and between jurisdictions; and,
- improving third-party regulatory processes, especially where these regulations and their associated requirements are imported and/or referenced in Federal Government et al regulatory instruments.

7.7 Of particular irritation to rank-and-file builders are the sizeable (and growing) number of variations to the (supposedly) uniform NCC by State/Territory, but more significantly, Local Governments around the nation.

7.8 Such variations add to uncertainty in regulatory compliance for builders, and to the costs of construction for home and business owners. Rank-and-file builders have told Master Builders, inter alia:

> *There are too many documents to supply to councils that take too much time to get and in most cases are extremely expensive. e.g. Bushfire reports, acoustic reports, flood reports, shadow diagrams, site analysis, waste management plans, traffic management plans, streetscape analysis plans, hydraulic details, landscape plans, external colours, arborist reports, road opening permits and a myriad of council application documents.*
>
> *We deal with over 50 Councils and each one has a different set of application paperwork, documents, fees, contributions, building controls, cut and fill policies, stormwater policies and tree preservation policies.*
>
> *The time taken to approve very simple homes can take between 3 weeks to 3 months. If councils are busy e.g., Baulkham Hills, Blacktown or Liverpool then the time taken is ridiculous in most cases, up to 15 weeks.*
>
> *Additional quotes from our member-focus groups on regulation issues can be found at Appendix A.*

7.9 Master Builders recommends the Federal Department of Industry be charged with compiling and reporting on its website by the end of 2015 (with annual updates) a definitive and exhaustive list of all State, Territory and Local Government variations from the NCC.

7.10 In the short term, such a listing would promote greater transparency and competitive benchmarking of the incidence and impact of, as well as acting as the platform for subsequent program of work in reviewing, rationalising and potentially eliminating, such variations.

7.11 The BCI continues to have a very serious problem with the differential classification and treatment of employees and sub-contractors between and within jurisdictions in Australia. In the federal domain, this problem is particularly onerous under industrial relations and taxation law.

7.12 The status and treatment of employees vs sub-contractors under federal law is a significant issue for the BCI given these people, whether professionals such as architects, engineers or the like, or tradespeople, such as electricians, plumbers, concreters or the like, are the backbone of the industry.

7.13 Master Builders has identified a practical and workable solution to this problem, centred on a system of statutory registration, administered by the Australian Taxation Office, for those who choose to operate as an independent contractor.

7.14 Under our approach, persons looking to register for independent contractor status would be subject to a single set of tests, recognised across agencies and jurisdictions, which reflect the operation and conduct of a modern building sector. The tests would also establish clear separation between commercial law which should govern independent contractors, and workplace relations law which should govern employers and employees.

7.15 Master Builders recommends the Treasurer direct the Australian Taxation Office to establish a Government-Industry Working Party to implement by the end of 2015 the proposed system of statutory registration for independent contractors, and advance the necessary changes in federal law, regulation and/or administration.

7.16 Master Builders welcomes the directions set down in the "Australian Government Guide to Regulation" requiring regulators to consider alternatives to regulatory interventions, greater use and rigor in preparing high-quality cost/benefit and regulatory impact analyses, and increased transparency in the regulation development/review processes.

7.17 Of specific importance to the BCI is the obligation for Federal Government agencies, departments et al using standards et al created by third parties, such as Standards Australia, to ensure these instruments meet the Regulatory Impact Statement (RIS) requirements set down in the Guide.

7.18 This new threshold for the inclusion of third party standards or performance requirements into Federal regulations is significant for the BCI, given the expansive practice of the Australian Building Codes Board (ABCB) of importing Australian Standards into the NCC.

7.19 While Master Builders sees merit-in-principle in the privatisation of the regulatory process, through entities such as Standards Australia, this must not come at the expense of analytical rigor in the development and evaluation of the instruments thus created.

7.20 Master Builders recommends the ABCB be directed by the relevant Minister(s) that Standards or the like promoted or developed by third parties imported into federal government regulation be required to meet, as minimum, the performance thresholds set down in "The Australian Government Guide to Regulation".

7.21 At the very least, this must include rigorous and transparent Preliminary Impact Analyses, Cost/Benefit Analyses and RISs for each and every third party instrument adopted or imported into federal legislation or regulation.

7.22 To ensure third party instruments remain relevant to current practices, and do not unnecessarily impede innovation and change in future practices, such instruments where adopted or imported in to federal legislation or regulation should be subject to mandatory, defined (preferably not more than five year) sunset provisions.

8 Skills and Training

8.1 The BCI is 'moving up the skills curve', evident in the changing skills composition of its labour force – a trend which Master Builders expects to continue well into the foreseeable future. However, the gradient and the pace with which the industry is able to move up this 'skills curve' is, according to our rank-and-file members, being held back by shortages of skilled and para-professional labour.

8.2 At the same time, the nature of employment in the BCI is changing due to the introduction of new technologies and pre-fabrication. This is leading to altered work practices which no longer guarantee traditional career paths will generate the mix of skills needed to meet the future demands of the industry, and through it the Australian economy.

8.3 This situation is being compounded by the mismatch between Australia's industrial relations and its workplace relations systems.

8.3.1 Consultations with our members continually report the workplace relations system does not currently complement the Australian Apprenticeship system and has created potential barriers to the apprenticeship system being able to deliver maximum productivity benefits.

8.4 Other key messages coming from our member consultations, such as the member-focus groups conducted specifically for this submission, include:

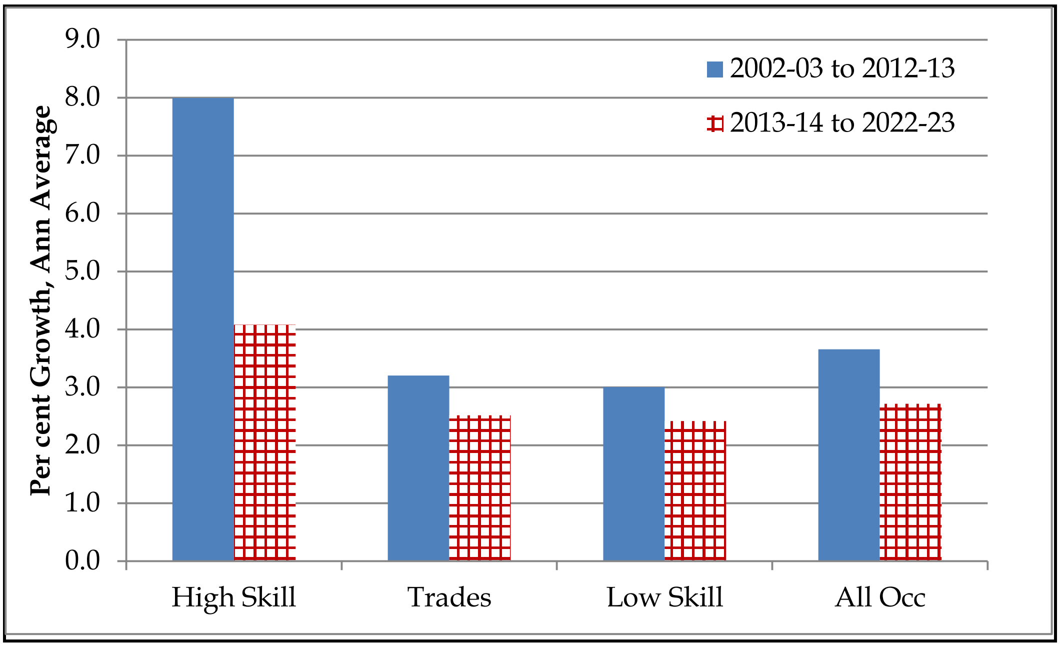
> *If the young blokes don't have business or entrepreneurial skills then they won't last very long in the industry.*
>
> *Getting (home warranty insurance) is a huge issue for new builders. But, they don't teach them this at trade school.*
>
> *The industry needs more business skills training. As an industry we do a poor job of teaching apprentices about business management.*
>
> *We should add one or two modules on business management to Cert 4.*

8.5 Additional quotes from our member focus groups on skills and training issues can be found at Appendix B

8.6 Graph 7 reports the changing skills composition of the BCI over the period 2002-03 to 2012-13 (n = 11 years), and then our forecasts of what we expect to happen over the 2013-14 to 2022-23 (n = 10 years).

8.6.1 The actual and forecast figures cover high skilled occupations (such as engineers and surveyors), tradespeople (such as electricians, plumbers), and lower skilled labour (such as general hand labourers).

Graph 7: Building Labour Force: Actuals and Forecasts



8.7 As can be seen, high skilled labour expanded by 8 per cent per annum, annual average, over the period 2003-03 to 2012-13, far-and-away ahead of the comparable growth rates for trades-skilled person (3.2 per cent) and low-skilled labour (3.0 per cent).

8.8 Master Builders expects this outperformance to continue over the 2013-14 to 2022-23 period, albeit with a narrower gap between the growth of highly skilled compared to trades- and low-skilled labour.

8.8.1 The growth rate for highly skilled labour is forecast to average around 4.1 per cent per annum over the forecast horizon, ahead of that for trades-skilled (2.5 per cent) and low-skilled (2.4 per cent).

8.9 Looked at another way, highly skilled labour accounted for 11 per cent of the labour force in the BCI in 2002/03. Master Builders forecasts this share will increase to 16.4 per cent by 2022/23.

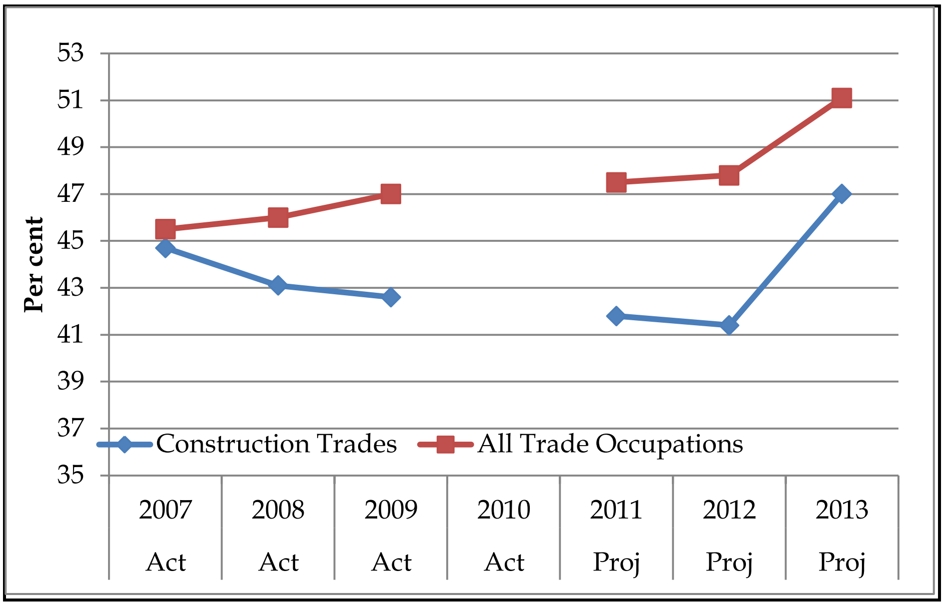
8.9.1 This increase will be accounted for by declines in the shares of both trades-skilled (down from 53 per cent to 50.4 per cent), and low-skilled (down from 36 per cent to 33.2 per cent) over the same period.

8.10 While the faster growth/rise in the share of highly skilled labour in the BCI is to be welcomed, of concern is the slower/growth decline in the share of skilled trades people in the industry, which if left unactioned could cause serious 'labour bottlenecks' in the building supply chain, and the efficiency and productivity of the industry.

8.11 This problem in part reflects, and is likely to be compounded by, the relatively lower completion/higher attrition rates for apprentices in the BCI (NCVER 2014).

8.12 Graph 8 reports completion rates for apprentices and trainees in the BCI, and all trades occupations, over the 2007 to 2009 (actual) and the 2011 to 2013 (projections) period (all data are derived from NCVER 2014).

Graph 8: Completion Rates



8.13 As can be seen, the completion rates for apprentices and trainees in the BCI (the blue line; diamond marker) has fallen below that for all trade occupations (red line; square marker) over the period under review.

8.13.1 Completion rates for apprentices and trainees in the BCI averaged 43.4 per cent for the six years for which there are reported observations, compared to 47.5 per cent for all trades occupations, a difference which is statistically significant ($t = 4.93$; t-crit = 2.57; $p = 0.00$) – that is, highly unlikely to be due to chance alone.

8.14 From a practical standpoint, it is deeply disturbing to observe more than half of all apprentices and trainees in the BCI (and indeed, in all trades occupations) fail to complete their apprentice/trainee-ships.

8.14.1 This situation amounts to an inefficient use of labour resources (both amongst the apprentice/trainee, and their mentors), the diversion of scarce financial resources (especially amongst smaller builders/firms) into activities which do not appear to generate a return to the individuals and the firm(s) concerned, and to the wider industry and the national economy.

8.15 This 'loss of return on investment' is especially disconcerting when it is realised (NCVER 2014) 34 per cent of apprentices/trainees in the BCI (and 31 per cent across all trades occupations) cease their training within just one year of commencement.

8.16 For many employers/mentors, this situation amounts to 'money down the drain', as few apprentices/trainees have acquired sufficient proficiency or skill in this short time frame to deliver any economic return-on-investment to their employer/mentor.

8.17 Master Builders has identified three potential initiatives which will help our industry and, if taken up and more widely applied elsewhere, the wider Australian economy to take meaningful action to deal with the existing, and potentially increasingly acute, shortage of skilled labour.

8.18 These initiatives are:

- greater harmonisation of apprenticeship systems and public sector funding policies around the nation;

- the development of “Passports of Competencies”; and,
- wider industry-owned qualification and competency development.

Harmonisation of apprenticeship systems:

8.19 The inconsistency of the apprenticeship system between State and Territories is a significant issue for the BCI, and it is important the development and enforcement processes of national qualifications be simplified.

8.20 The harmonisation of apprenticeship pathways and funding of qualifications is a micro-economic reform that is required to provide national consistency in the implementation of apprenticeship reform. This reform is necessary to reduce barriers to apprentice labour mobility and to reduce costs for business.

8.21 Against this background, Master Builders proposes the Vocational Education Training (VET) system become:

- nationally focussed with greater collaboration between the Commonwealth. and the States and Territories to meet the needs of industry and the economy including improved implementation and outcomes across jurisdictions;
- leading edge in the design and development of national training packages that are flexible to meet the needs of industry and provide clear guidance to Registered Training Organisations (RTOs) on the training and skills outcomes sought by industry. They must also clearly codify the skills and knowledge that a worker needs to perform a task or job; and,
- responsive to the ever changing needs of industry to compete within a globally competitive economy;

“Passport to Competencies”:

8.22 This initiative recognises Australia’s apprenticeship system is currently heavily focussed on the completion of full qualifications, despite the completion rate for publicly funded VET qualifications being only 36 per cent. A result of this is that in many trades the proportion of workers holding formal qualifications is actually dropping over time.

8.23 Part-qualifications, or skill sets, which may be appropriate to undertake a particular job role in the industry, should be recognised as a viable pathway to a job. Skill sets should not be seen as the end to training, but the “building blocks” to gain a full qualification over time where it is supported by the worker and employer.

8.24 Master Builders recommends the introduction of a ‘skills passport’ for the BCI where skill sets and individual units of competency can be undertaken in stages as a person’s skills needs develop over time.

8.25 The ‘passport’ would allow for improved safety and quality outcomes and enable employers to quickly access workers’ existing skills. The introduction of the Unique Student Identifier will be beneficial in helping employers and workers track their competencies.

8.26 By combining a series of units of competency and skill sets within the passport, students and workers could obtain a full qualification over time. The passport would be a mechanism to support life-long learning. In order to achieve this aim, the funding of skill sets and individual units of competency would need to be agreed on a national basis as currently there are different funding guidelines in each jurisdiction.

Industry-owned qualification and competency development:

8.27 Master Builders supports the Australian Government’s review into *Industry Engagement in Training Packages: Towards a Contestable Model*. The centrality of industry in training package design, development, implementation and review is the cornerstone of the National Training System.

8.28 As VET is essentially an economic strategy to develop a skilled workforce to enable Australia to compete globally, the Government must remain committed to supporting their continual development and review to ensure they are meeting the needs of industry. Training packages are an essential component of the national VET system. In fact, they are one of the few truly national components of the system.

8.29 Master Builders recommends training packages, inter alia:

- be informed by real time intelligence that identifies the changing nature of industry, work practices and disruptive events including technological change and its resulting impact on required skills and knowledge;
- specify the knowledge and skills required to perform effectively in the workplace as determined by industry;
- provide clear guidance to RTOs on the skills and knowledge students are expected to acquire; and inform course design and assessment practices to ensure consistent outcomes across VET; and,
- be responsive to changing industry requirements including ensuring licensing requirements for specific occupations are considered in training package development and continually updated as needed.

8.30 Absent such reforms the BCI will likely find it increasingly difficult over the coming decade, and potentially beyond, to meet the rising demand for a skilled workforce against a background of a decreasing number of apprentices in accredited training, high drop-out training rates, an ageing workforce and an exit rate of existing workers of 30,000 persons per annum.

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3. National Australia Bank (2014b) "NAB Commercial Property Survey - Market Overview Q3 2014", National Australia Bank, Melbourne

4. National Centre for Vocational Education Research (2014) "Completion and Attrition Rates for Apprentices and Trainees: 2013", National Centre for Vocational Education Research, Adelaide

5. Productivity Commission (2014) "Business Set-up, Transfer and Closure: Issues Paper", Productivity Commission, Canberra

Appendix A: Focus Groups on Regulation

"It really frustrates me that so many bureaucrats are really just trying to make work for themselves at my cost."

"I'm a small business, and really don't have the 'free time' for dealing with regulations. NSW is just so pro-reg."

"I'm not sure building regulators are always up to speed with the building regulations. Some of the things they ask for just make me wonder."

"The costs of going through the (regulator name here) are so prohibitive; we just had to settle (the claim) even though we were in the right. Our barrister just said 'pay up, and close it off'. We had to do, and fund, the remediation work when really it (the claim) was a maintenance issue which is the client's responsibility."

"The ATO (Australian Taxation Office) and some of the (State name here) regulators want builders to become their (enforcement) agents, which isn't right."

"You have to price red tape into your quote."

"Regulators don't understand the cash flow constraints small business in this industry work under. Workcover is the worst, with all of its upfront fees."

"There should be more use of 'one stop regulatory shops' – one place where you can go for advice and to get everything done, rather than having to run around all over the place."

"One area where they should tighten the regulations is owner builders."

"There really is two standards – one for registered builders, and one for owner-builders."

"Owner builders are a pain. They watch these (home renovation) shows on television, and think they can do it. Then we have to come along and clean up the mess."

"The worst thing (about local government) is inconsistency. One method or rule is applied in Gippsland, and another one in Kew."

"It is almost a lottery by postcode."

"Local governments are virtually unaccountable to anyone; little baronies."

"Regulations are a case of rolling with the punches."

"You can't afford to alienate local government. They get back at you, such as by delaying your paperwork."

Appendix B: Focus Groups on Skills and Training

"We need to train young builders much better in running a business. There is not enough 'running a business' (training) in Cert Four."

"We have to inculcate in apprentices that they are running a business – in building."

"If we sell a business, then 'long tail liabilities' go with the business."

"Most builders need to be 'off the tools' by the time they are forty (years of age). Their bodies just can't take it. So they need to have skills in project management."

"Building licences are too easy to get. We need to have a tiered licencing system. HWI (home warranty insurance) at the moment in (State name here) really is the de facto licencing system."

"HWI is really the framework for licencing – what you can do, the value of the work you can do."

"(Regulators and the industry) should look at a bronze/silver/gold tiered licensing system, which applies as the business scales up."

"We need tiering (of licences). Younger builders should have to get at least two years post ticket experience. They should also have a diversity of experience across a range of projects before they can get an unrestricted licence."

ATTACHMENT D

Master Builders Australia

Submission to the Senate Economic References Committee

on

Insolvency in the Australian Construction Industry

17 April 2015

MASTER BUILDERS AUSTRALIA

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1 Introduction

1.1 This submission is made on behalf of Master Builders Australia Ltd.

1.2 Master Builders Australia is the nation's peak building and construction industry association which was federated on a national basis in 1890. Master Builders Australia's members are the Master Builder state and territory Associations. Over 125 years the movement has grown to over 32,000 businesses nationwide, including the top 100 construction companies. Master Builders is the only industry association that represents all three sectors, residential, commercial and engineering construction.

1.3 The building and construction industry is a major driver of the Australian economy and makes a major contribution to the generation of wealth and the welfare of the community, particularly through the provision of shelter. At the same time, the wellbeing of the building and construction industry is closely linked to the general state of the domestic economy.

2 Purpose of Submission

2.1 On 4 December 2014 the Senate referred an inquiry into insolvency in the Australian construction industry to the Senate Economics References Committee (Committee) for inquiry and report by 11 November 2015. The closing date for submissions to the Committee's inquiry is 17 April 2015.

2.2 Master Builders notes that there is currently an inquiry underway by the Productivity Commission which bears on the work of the Committee in the current context. The Productivity Commission has been asked to undertake a broad ranging investigation and to specifically investigate, analyse and propose recommendations on:

- The nature and the scale/extent of barriers to entry and exit that currently exist for businesses and their impact on economic performance.
- Identify appropriate options for reducing these entry and exit barriers, including but not limited to advice on the potential impacts of:
    - the regulation of product and service markets;

- transfers and subsidies to businesses, including import barriers;
- regulations affecting the ease of starting, operationalising or closing a business;
- time spent on and cost of complying or dealing with government regulation, licensing and bureaucracy; and
- the personal/corporate insolvency regimes on business exits.[1]

2.3 The Issues Paper[2] produced by the Productivity Commission clearly flags the intention of the Commission to examine the improvement of insolvency arrangements in Australia as part of its current inquiry. The Issues Paper contains a number of questions that the Productivity Commission believes are relevant to recommending such improvements including, for example, the extent to which the existing insolvency arrangements facilitate or hinder business closure.[3]

2.4 The Productivity Commission inquiry report will undoubtedly benefit the understanding of a large number of issues that relate to business entry and exit in the building and construction industry. The questions posed by the Commission relate squarely to a number of the terms of reference of the Committee's current inquiry, noting that term of reference (h) of the Committee's inquiry seeks submitters to specifically address the adequacy of the current law and regulatory framework to reduce the level of insolvency in the construction industry. These matters are squarely before the Productivity Commission in that the adequacy of the current laws is integrally tied to how matters might be improved.

2.5 Master Builders made a comprehensive submission to the Productivity Commission on its reference into business set-up, transfer and closure. A copy is attached as Attachment A to this submission. Whilst we have provided this submission to the Committee, we would commend deferral of consideration of the matters currently before the Committee until the

[1] Inquiry into Business Set-up, Transfer and Closure http://www.pc.gov.au/inquiries/current/business

[2] http://www.pc.gov.au/inquiries/current/business/issues/business-issues.pdf

[3] Ibid at p 16-17

Productivity Commission produces its report set down for August 2015. That agency is, after all, responsible for advising Government on the best means to establish policy in the long term interests of Australians and its report is only a few months away and will be published before the Committee's reporting date in November 2015.

2.6 Master Builders commends to the Committee the matters of substance set out in the submission made to the Productivity Commission at Attachment A. This submission adopts all of the points made in Attachment A as being vital to understanding the entry to and exit from the building and construction industry and is therefore relevant to the Committee's terms of reference, particularly term of reference (c), the causes of construction industry insolvencies.

2.7 Master Builders in the following sections will address each of the Committee's terms of reference. For ease of reading the submission, we now set out the Committee's terms of reference:

a. the amount of money lost by secured and unsecured creditors in the construction industry and related insolvencies, including but not limited to:

   i. employees,

   ii. contractors and sub-contractors,

   iii. suppliers,

   iv. developers,

   v. governments, and

   vi. any other industry participants or parties associated with the Australian construction industry;

b. the effects, including the economic and social effects, of construction industry insolvencies, having particular regard to the classes of creditors in paragraph (a);

c. the causes of construction industry insolvencies;

d. the incidence of 'phoenix companies' in the construction industry, their operation, their effects and the adequacy of the current law and regulatory framework to curb the practice of 'phoenixing';

e. the impact of insolvency in the construction industry on productivity in the industry;

f. the incidence and nature of criminal and civil misconduct related to construction industry insolvencies, having particular regard to breaches of the Corporations Law both prior to and after companies enter external administration and/or liquidation;

g. the current extent and future potential for the amount of unpaid debt in the industry to attract non-construction industry participants to the industry for the purposes of debt collecting and related activities and the extent of anti-social and unlawful conduct related to debt collecting and related activities;

h. the adequacy of the current law and regulatory framework to reduce the level of insolvency in the construction industry; and

i. any other relevant matter.

3 Financial Loss

3.1 This section of the submission addresses term of reference (a). Master Builders notes that the extent of the problem of insolvency in the NSW building and construction industry came under intense scrutiny via the Collins Inquiry[4] (the NSW Inquiry) held in that State in late 2012.

3.2 The NSW Inquiry engaged the services of BIS Shrapnel to provide an analysis of insolvency statistics and provide a picture of the causes of insolvency, sector incidence of insolvency and forecasting data. The NSW Inquiry final report noted that the BIS Shrapnel Report confirmed that insolvency in the NSW building and construction industry accelerated over the years leading to the inquiry, a matter confirmed for Australia in the

[4] http://www.finance.nsw.gov.au/sites/default/files/pdfs/IICII-final-report.pdf

limited statistics available as set out in Attachment A, particularly sections 4 and 5 of that document.

3.3 Key issues contained in the BIS Shrapnel Report include:

> *The industry recorded the highest number of insolvencies of any defined industry for the financial year 2011/12, a total of 1,113 or 24.7% of external administrations reported to ASIC across NSW*
>
> *By size, a majority of the insolvencies being recorded are by small contractors and sub-contractors, entities with assets of less than $10,000.*
>
> *BIS Shrapnel found that:*
>
> *The surge in NSW insolvencies has been driven mostly by the prolonged stagnation in residential construction, exacerbated by the simultaneous slowdown in several key non-residential types:*
>
> - *engineering construction has not been a significant contributor to the recent insolvency surge in the NSW industry;*
> - *the residential sector is the biggest contributor, with both detached houses and multi-residential building (medium and high density apartments) both helping drive the rise in insolvencies;*
> - *in non-residential construction the simultaneous slowdown in key areas such as office, retail, warehouse and hotel construction has worsened the situation since the GFC.*[5]

3.4 Despite commissioning this work, the NSW Inquiry noted that there is lack of clarity on where the largest proportion of insolvencies in the industry exists, although there is some disaggregated material in Attachment A particularly at Table 2 on page 11 that shows sub-sectoral data on industry exits. We submit that there has been no assessment of the total losses from insolvencies either in aggregate or disaggregated in the manner sought by the Committee.

3.5 The statistics in Attachment A are able to be supplemented by data from the Australian Financial Security Authority (AFSA)[6] which has recently reported that the highest increase in the number of debtors entering business related personal insolvencies occurred in the occupation construction trades workers.

[5] Ibid at p 23 footnotes omitted

[6] https://www.afsa.gov.au/resources/media-kit/media-archive/media-release-australias-personal-insolvency-statistics-occupations-of-insolvent-debtors

Insolvent debtors increased from 504 debtors in 2010–11 to 669 in 2013–14. The largest increase was in painting trades workers.

4 The Effects of Insolvencies

4.1 This section deals with term of reference (b)

4.2 The NSW Inquiry found that the effects of insolvency on subcontractors were intense:

> *The Inquiry has heard of examples of the devastating impact insolvencies have had on subcontractors – financially, professionally and personally.*[7]

4.3 To Master Builders' knowledge, these personal and very concerning effects have not been translated to empirical study; that is the effects of insolvency have not otherwise been measured in a way that assesses the financial consequences for participants in the construction industry in the way those participants are described in terms of reference (a).

5 The Causes of Insolvencies

5.1 This section deals with terms of reference (c). We refer to the discussion of this issue in Attachment A. The constraints and challenges that affect insolvency are discussed at section 6 of Attachment A.

5.2 In addition, we note that the NSW Inquiry found:

> *It is important to note that a reduction in available work will always work to amplify the pressures on businesses operating in a competitive industry. In an industry such as building and construction where profit levels are relatively low compared to many others, a reduction in the volume of work inexorably leads to tighter margins, greater risks and an increase in the number of insolvencies.*[8]

5.3 This quotation essentially reflects the tenet of economic theory that the least efficient businesses are most likely to become insolvent once the volume of available work decreases.

5.4 The NSW Inquiry also found that the most common causes cited for insolvency are:

[7] Above note 4 at p 43

[8] Above note 4 at p 24

- insufficient capital together with excessive debt;
- poor financial management skills;
- an inability to manage the scope of projects;
- lack of requisite expertise for a particular project;
- low margins;
- payments withheld or not paid;
- fraud;
- poor economic conditions.[9]

6 Phoenix Companies

6.1 This section deals with term of reference (d).

6.2 Master Builders' policy is to support targeted action that punishes those who deliberately liquidate a company to avoid paying liabilities, including employee entitlements i.e. operates as a "phoenix" company. The business is then "re-created" and continues operations through another corporate entity, controlled by the same person or group of individuals, often with a very similar name and "free" of debts which have been fraudulently left behind in the liquidated structure. Master Builders endorses the definition of fraudulent phoenix activity set out in the November 2009 paper entitled *Action Against Fraudulent Phoenix Activity: Proposals Paper*[10] which captures the relevant practice:

> *Fraudulent phoenix activity involves the evasion of tax and other liabilities such as employee entitlements through the deliberate, systematic and sometimes cyclic liquidation of related corporate trading entities.*[11]

[9] Above note 4 at p 40

[10] http://www.treasury.gov.au/documents/1647/PDF/Phoenix_Proposal_Paper.pdf

[11] Id at p 1

6.3 This definition is similar to the definition proposed in the 2012 work commissioned by the Fair Work Ombudsman[12] (the PWC Report) as follows:

> *Phoenix activity is the deliberate and systematic liquidation of a corporate trading entity which occurs with the illegal or fraudulent intention to:*
>
> *avoid tax and other liabilities, such as employee entitlements*
>
> *continue the operation and profit taking of the business through another trading entity.*[13]

6.4 The structures referred to in paragraph 6.2 are built on fraud. The businesses do not intend to compete in the market except for a short period when debt levels are able to be built up without any intention of repaying the monies.

6.5 Master Builders condemns this practice, particularly as it disadvantages bona fide participants in the building and construction industry both in competitive terms and when caught up by the fraudulent practices.

6.6 Fraud has always been illegal and requires no new laws. Fraud is actionable both civilly and criminally and carries high maximum sentences discussed below in paragraph 6.6. The concept of fraud is flexibly defined at law, so as to permit relevant authorities to deal with particular behaviours and only those behaviours. In essence, it is the use of deception to obtain a benefit. As a result, the concept has not been a burden on ordinary commerce. The fact that some concerted effort by prosecuting authorities is involved in securing a conviction for a serious offence, with serious penalties, is not a basis on which change to the law should be made.

6.7 Master Builders has the policy that phoenix activity should be acted against with the full severity of the current law. We endorse the findings of the Cole Royal Commission[14] which pointed to the utility of current criminal law. We submit that the Commonwealth should pursue phoenix operators on the basis of the Cole findings. We contend that Cole isolated appropriate criminal law sanctions which should be used as follows:

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[12] Fair Work Ombudsman "Phoenix Activity: Sizing the Problem and Matching Solutions" report authored by PWC June 2012 http://www.fairwork.gov.au/ArticleDocuments/763/Phoenix-activity-report-sizing-the-problem-and-matching-solutions.pdf.aspx?Embed=Y

[13] Ibid iii

[14] Final report of the Royal Commission into the building and construction industry February 2003 http://www.royalcombci.gov.au/hearings/reports.asp

> *There are three relevant sections of the Commonwealth Criminal Code. They are: S134.1 (obtaining property by deception); s134.2 (obtaining financial advantage by deception); and s135.1(3) (causing a loss to a Commonwealth entity).*
>
> *Sections 134.1 and 134.2 carry a penalty of imprisonment for ten years. Section 135.1(3) offences carry a penalty of five years' imprisonment. Under s206B(B)(ii) of the Corporations Act 2001 (Cth), a conviction at least of the offences created by ss134.1 and 134.2 for any one of these offences means automatic disqualification as a company director, as they are offences which involve dishonesty and are punishable by imprisonment for at least three months.*[15]

6.8 In relation to these recommendations from the Cole Royal Commission, we note that the PWC Report indicated:

> *The AIG and Master Builders pointed out that the Cole Inquiry made a number of recommendations regarding mitigating phoenix activity and that many of these were never implemented. It was suggested that it could be beneficial to look back at the recommendations of previous inquiries and studies to complete a 'stocktake' of recommendations that had been implemented and those that had not been implemented.*[16]

6.9 We also note that in the PWC Report the following is said:

> *Master Builders indicated that there is still a disproportionate amount of phoenix activity in the building and construction industry and that they would hear of incidents on a monthly basis. They indicated that subcontractors and smaller businesses were particularly vulnerable to phoenix activity due to the high level of 'churn' at the lower end of the building and construction industry.*[17]

6.10 However, since the feedback given to PWC for the purposes of the compilation of its Report, Master Builders has not been informed of phoenix activity with the regularity previously noted. We are, however, currently involved with investigating a breach of Master Builders' trade mark by an alleged phoenix company and understand that a number of agencies, including the police, are involved. We would comment that the detection of illegal phoenix activity is difficult and requires coordinated resources and expertise amongst agencies and greater use of the current law. An important part of the PWC Report was its emphasis on inter-agency co-operation. That is at the essence of a crack-down in this area, not a change to the law.

---

[15] Ibid Vol 8 Chapter 12 at 137

[16] Above note 11 at p 62

[17] Above note 11 at p 61

6.11 Master Builders notes that in its response to the Treasury paper mentioned in paragraph 6.2 of this submission, the Australian Institute of Company Directors (AICD) took a similar view that more reliance on the current law should occur, thus:

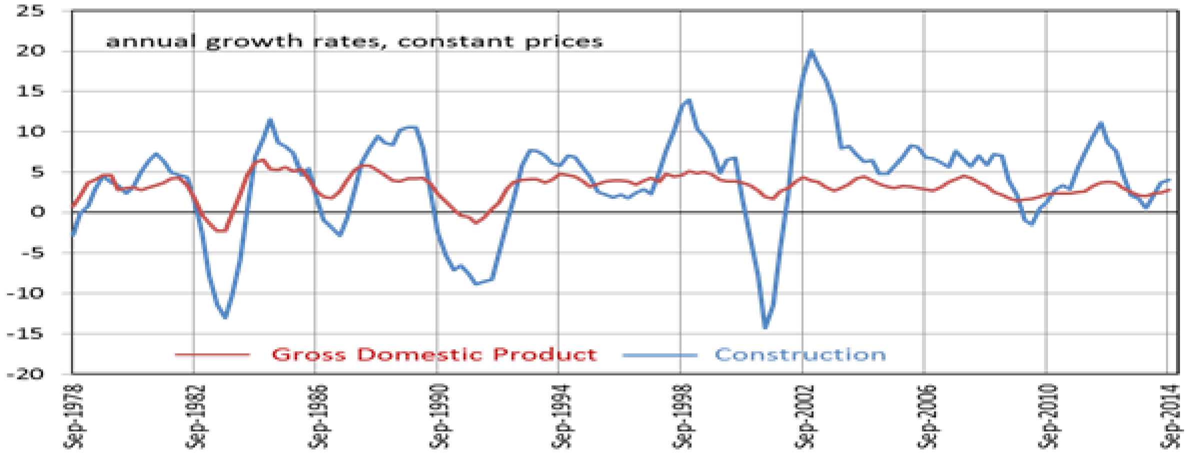
> *AICD strongly believes that there are a range of existing provisions under both the tax and corporations laws which give regulators wide powers to pursue those who have committed frauds of the kind identified in the case studies in the Paper. In particular, the 'trading while insolvent' provisions in Part 5.7B of the Corporations Act and ASIC's existing powers to disqualify persons from managing corporations where they have been involved in multiple corporate collapses (under s206F) provide appropriate measures for dealing with perpetrators of the kinds of undesirable actions identified.*

7 Insolvency and productivity

7.1 Whilst terms of reference (e) seeks feedback on the impact of insolvency on productivity in the industry, we are not aware of any studies that deal with this issue or isolate it as a variable in relation to studies of industry productivity.

7.2 It is important not to conflate the notion of insolvencies having an impact on the industry's productivity with the volatility of the industry. Building and construction is a highly cyclical industry with amplitude of peaks and troughs approximately three times that of the general economy. Real output and employment growth in the industry may realistically be expected to average 3 and 2 per cent per annum, respectively, but this will mask inherent volatility that can be extreme at times, particularly by sector and geographic region. Their volatility is demonstrated in Figure 1.

Figure 1 Construction Output and Real GDP



Source: ABS Cat No 5206.0

7.3 The industry functions in response to the need for buildings and structures that, in turn, derives from underlying economic, social and demographic factors. Cyclicality derives from the uncertainty attached to business investment and individual's consumption decisions that drive activity, with interest rates and other financial and tax-related factors accentuating the volatility, and hence providing the 'churn' in industry turnover referred to in paragraph 6.8 of this submission.

8 Criminality and Insolvency

8.1 Master Builders has no information that would assist the Committee in respect of item (f) of the terms of reference. We note the submission dated 24 March 2015 to the Committee by Anderson et al. We note from page 10 of that submission that the authors of the submission are currently involved with a data collection exercise that they hope will shed light on the incidence of criminal and civil misconduct in the current context.

8.2 We support the conduct of the work by Anderson et al.

9 Unlawful conduct, debt collecting and insolvency

9.1 We refer to term of reference (g). The fact that insolvencies occur should not be a catalyst for unlawful threats or unlawful behaviour to be manifest. There is no logical link between the use of unlawful tactics and increased insolvencies. We make that point despite media comment that seems to correlate the two factors as follows:

> *The NSW construction industry is hiring from the ranks of bikies, former criminals and colourful businessmen, including a convicted terrorist, to collect debts from building companies that have gone bust.*
>
> *Fairfax Media has found desperate companies are increasingly hiring self-described "mediators" like Ray "Rugby" Younan, James "Big Jim" Byrnes and Alex "Little Al" Taouil to resolve and collect debts.*
>
> *A series of high-profile multimillion-dollar bankruptcies over the last two years has created a domino effect resulting in out-of-pocket sub-contractors employing people with questionable pasts to chase debts for them.*
>
> *One of the state's most senior construction figures – Construction Forestry, Mining and Energy Union NSW secretary Brian Parker –*

> *says there has been an increase in middle men and debt collection in the construction industry due to the high-level of companies going bust, with little policing.*[18]

9.2 Master Builders points to the findings of the Royal Commission into Trade Union Corruption and Governance's interim report published in December 2014. We find it extraordinary that the CFMEU would seek to justify intervention of those described in the above extract as having 'questionable pasts' in the otherwise legitimate business of debt collection. In this context we note that the Heydon Royal Commission has found an unacceptable culture within the CFMEU. This has led the Heydon Royal Commission to find the overall legal system inadequate:

> *The defects reveal a huge problem for the Australian state and its numerous federal, State and Territory emanations. The defying of the Victorian Supreme Court's injunctions for nearly two years (by the CFMEU)… will make the Australian legal system an international laughing stock. A new form of 'sovereign risk' is emerging – for investors will not invest in countries where their legal rights receive no protection in practice.*[19]

9.3 Criminality in any part of the sector cannot and should not be tolerated. Defiance of the rule of law should not be tolerated.

10 Adequacy of the Current Law

10.1 As indicated earlier, consideration of the question raised by term of reference (h) should be deferred until the Productivity Commission reports.

10.2 We also point to the matters set out in Attachment A, particularly sections 7 and 8 which relate to term of reference (h).

11 Other Matters – Sham Contracting

11.1 This discussion relates to any other matter that might be relevant to the Committee's inquiry per item (i) of the terms of reference. Master Builders notes that some parties may argue to the Committee that there is a growing problem with the use of sham contracting or that the current law is insufficient. We reject the proposition that sham contracting has any influence on insolvencies. We reject the proposition that the current law in this context

[18] *Bikie gangs called in on building debts*, Ilya Gridneff, The Sun-Herald, 10 March 2013

[19] http://www.tradeunionroyalcommission.gov.au/reports/Pages/default.aspx at para 260 p1114

is inadequate save for where we have sought reform as set out in Attachment A for a better process for identifying genuine independent contractors which, at the same time, would bring clarity to the law about when a principal to contractor, as opposed to an employer to employee relationship arises.

11.2 A sham contract arrangement arises when an employer deliberately treats an employee as an independent contractor or coerces employees into signing contracts that represent them as being contractors rather than employees. This is currently proscribed in s357 to s359 *Fair Work Act 2009* (Cth). Master Builders stresses that this behaviour is a deliberate act by those who choose to act illegitimately. It is a practice we condemn. It should not, however, be confused with misclassifying an employee as a contractor, a mistake that may often be made because of the dense and confusing law that governs this distinction, inclusive of a multitude of statutory deeming provisions, alluded to in Attachment A.

11.3 The attempts to paint sham contracting as something different to the deliberate manipulation of the law promotes a range of other agendas. Firstly, it assumes that sham contracting is an endemic problem in the building and construction industry or other industries. This is not the case. Secondly, it enables unions where members are employees rather than a contractor to discourage the formation of independent businesses as a means to boost membership.

11.4 Relatedly it appears that some of the fallacious assumptions about this subject arise from the CFMEU's publication "Race to the Bottom: Sham Contracting in the Australian construction industry".[20] This report contains completely unreliable statistics which seek to demonstrate that nearly $2.5 billion a year is being allegedly lost in the tax system because of sham contracting. This is not the case. It is inaccurate and falsely damning of the industry.

11.5 In respect of the CFMEU's statistics in "Race to the Bottom" the former ABCC found that without further explanation by the CFMEU it is difficult to find other than the conclusions reached by the CFMEU are not reliable. We can be more direct. The Report is wrong and misconstrues the issues. The research

[20] http://www.cfmeu.asn.au/downloads/nat/reports/race-to-the-bottom-sham-contracting-in-australias-construction-industry Accessed 12 February 2015

released by the Fair Work Building Construction agency on 21 December 2012 about sham contracting[21] falls into error as well. The estimate of 50,000 people being potentially "on a sham contract" may indicate possible misclassification. But it does not represent a proper indication of sham arrangements – the deliberate misuse of the law. This is especially the case with the report's reliance on self-assessment combined with the finding that 54% of workers have never heard of the term "sham contracting". This finding leads to the conclusion that Government should provide funds for an industry-wide education programme; it does not call for a change to the law about sham contracting.

11.6 Much of the agenda of those who seek to oppose the current law is based upon making misclassification akin to sham contracting. This is lamentable given the state of the complex law which distinguishes between whether a worker is an employee or a contractor. Employers can already suffer very problematic financial burdens following misclassification if they are then asked to reverse the status of a contractor. Adverse cost consequence should not be added to by labelling misclassification an offence. The current provisions in the law should not be changed.

12 Conclusion

12.1 Master Builders notes the complexity of the influences on insolvencies, matters touched on in section 5 of this submission. That complexity makes the Committee's task difficult.

12.2 Master Builders commends the work of the Productivity Commission in relation to its reference on business set up, transfer and closure. We believe that, when published, the Productivity Commission inquiry report will assist the Committee in its work. Many of the complexities confronted by the Committee will be addressed by the Productivity Commission. That work will only assist the Committee.

****

[21] http://www.fwbc.gov.au/sham-contracting-research-released-0. Accessed 12 February 2015

Attachment A

Master Builders Australia

Business Entry and Exit

in the

Building and Construction Industry

12 March 2015

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CONTENTS

1 Introduction

1.1 Master Builders Australia is the nation's peak BCI association which was federated on a national basis in 1890. Master Builders Australia's members are the Master Builder State and Territory Associations.

1.2 Over 125 years the movement has grown to over 32,000 businesses nationwide, including the top 100 construction companies. Master Builders is the only industry association that represents all three sectors, residential, commercial and engineering construction.

1.3 The Building and Construction Industry (BCI) is a major driver of the Australian economy and makes a major contribution to the generation of wealth and the welfare of the community, particularly through the provision of shelter.

1.4 At the same time, the wellbeing of the BCI is closely linked to the general state of the domestic economy

2 Overview

2.1 Master Builders Australia welcomes the Productivity Commission Inquiry (the Inquiry) into barriers to entries and exits of business in the Australian economy. We particularly welcome the attention to be given to the impact of regulation in business start-up and close down.

2.2 The Inquiry is important for the BCI given:

- while the entry (start-up) rate for new firms in the industry was around the all-industry average; and,
- the exit (close down) rate for new firms in the industry was noticeably above the all-industry average.

2.3 Of particular concern are the high attrition rates for new firms created within the BCI, with:

- 27 per cent of new firms closing their doors within just one year of start-up; and,
- 45 per cent within two years, and 56 per cent within three years, of starting operation.

2.4 Such attrition rates must be a matter for concern, pointing to losses of skills, entrepreneurship and competition within the BCI, and to the wider Australian economy.

2.5 Master Builders believes decisive action is required in two key areas to improve business entry, and to reduce business exit, rates in the BCI, and the economy more generally.

2.6 These priority areas are regulation reform, and business skills training.

2.7 In the area of regulation reform, Master Builders calls for meaningful action to, inter alia:

- substantially reduce State, Territory and Local Government variations to the National Construction Code (NCC);
- eliminate the differential classification and treatment of employees and sub-contractors within and between jurisdictions; and,
- improve third-party regulatory processes, especially where these regulations and their associated requirements are imported and/or referenced in Federal Government et al regulatory instruments.

2.8 As one builder told Master Builders in a series of member-focus groups convened to discuss the issues before the current Inquiry:

> *Battling with regulations and bureaucrats is taking me away from building my business. I should be out winning jobs and doing business.*

And, another builder:

> *Have a look at everyone who regulates the building industry: the ABCB; Standards Australia; the Banks (as sources of finance); the insurance companies (given they provide insurance cover, when you can get it); local governments (God help us); and, the various State fair trading and consumer protection agencies. (No wonder) you have to price red tape into your quote.*

And, yet another builder:

> *We need seamless, back-to-back regulation, particularly between State and Local Governments.*
>
> *Can we do something about all of the local government variations to the National Construction Code.*

2.9 In the area of skills training, Master Builders calls for meaningful action to, inter alia:

- greater harmonisation of apprenticeship systems and public sector funding policies around the nation;
- the development of "Passports of Competencies"; and,
- wider industry-owned qualification and competency development.

2.10 A recurrent message from our member-focus groups, when discussion turned to the issue of skills training, was the need for greater emphasis on training in business skills. For example:

> *We do a good job teaching young blokes how to bang in a nail. But we need to teach (apprentices and young builders) more about business management.*
>
> *We need to do much more CPD (compulsory professional development), especially in how to run a business.*
>
> *We should add one or two modules on business management to Cert 4.*
>
> *Young blokes need more training in pricing work, managing cash flow, understanding their legal responsibilities, and in sales and marketing.*

3 Terms of Reference

3.1 The Federal Government has directed the Productivity Commission to undertake a review of barriers to entries and exits of business in the Australian economy.

3.2 Key amongst the Terms of Reference (see PC, 2014: iii), which sets the framework for the inquiry, are investigations into, inter alia:

- the nature and extent of business entry and exit, and the impact on Australia's economic performance; and,
- options and strategies for reducing barriers to entry and exit, ranging across, but not limited to, regulatory imposts by government, transfers and subsidies from governments, and personal and business insolvency regimes.

3.3 The Productivity Commission has released a useful Issues Paper (PC, 2014) which discusses several of these, and other related, issues, under two broad headings: barriers to new business entry and start-up; and barriers to business transfer or exit.

3.4 Under the sub-heading of 'barriers to new business entry and start-up', the Productivity Commission discusses topics such as regulatory barriers to commencing business, access to finance for newer firms, and constraints on new business structures.

3.5 Under the sub-heading of 'barriers to business transfer or exit', the Productivity Commission considers topics such as personal and corporate insolvency regimes, impediments to the transfer of ownership, and government assistance policies and programs acting as barriers to firm closure.

3.6 The Productivity Commission also raises the question of business and social attitudes to risk and innovation, in particular relating to firms who 'tried and failed, and want to try again' – in effect, our national attitude to entrepreneurship.

3.7 Master Builders' submission seeks to address a number of these, and several other, important issues relating to business entry and exit from the standpoint of the BCI . These include:

- the entry and exit rates for firms in the industry, both in aggregate, and by sector within it; and,
- impediments to firm performance arising from poor regulatory design and practice, and from skills shortages.

3.8 The economic significance of the BCI is underscored by two important metrics:

- it accounts for almost 8 per cent of gross domestic product, and more than 9 per cent of employment, in Australia; and,
- owner-occupied housing and other property investments account for over two-thirds of the asset portfolio and wealth of ordinary Australians.

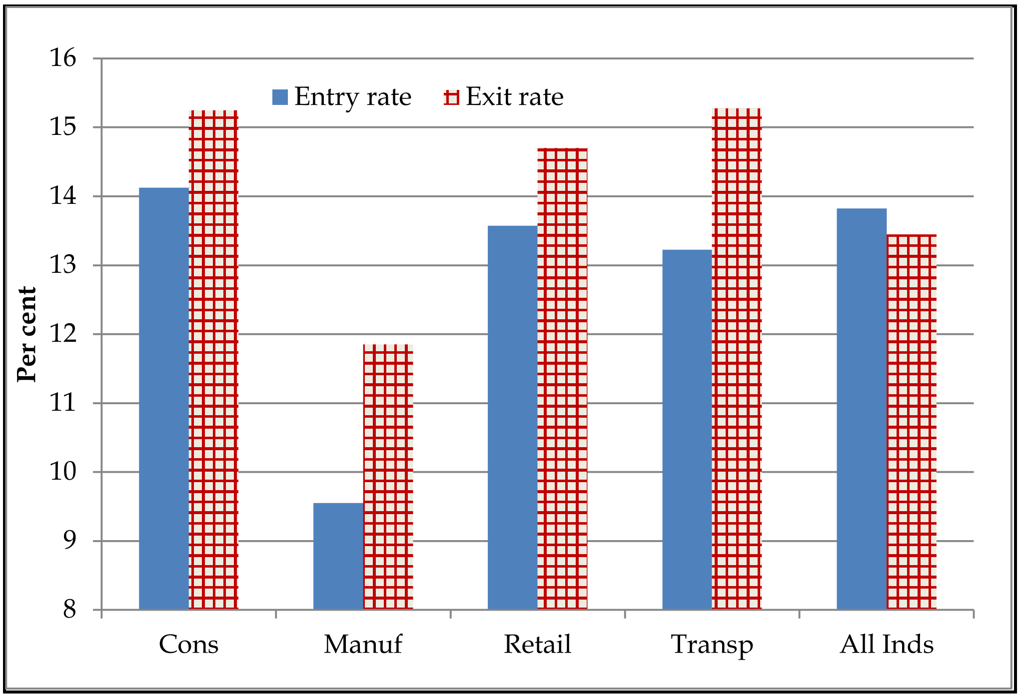
4 BCI Entry and Exit – In Aggregate

4.1 The Australian Bureau of Statistics (ABS, 2014) collections on business entry and exits provide one of the best quantitative insights into the creation and termination of commercial activity in Australia.

4.2 Amongst the main messages emerging from a careful review of this collection are some of Australia's key industries, including the fulcrum BCI are being caught in a tightening pincer of declining entry rates for new firms, and rising exit rates for existing firms.

4.3 Graph 1 reports the general pattern of business entries and exits for the BCI, the manufacturing, the retail and the transport industries, and an all-industry benchmark. All figures are entry or exit rates (that is, the number of entries or exits as a proportion of extant firms in the respective sectors), and are reported as averages for the four financial years up to and including 2012/13.

Graph 1: Business Entry and Exit for Selected Industries



4.4 The entry rate for new firms in the BCI averaged 14.1 per cent per annum in the four financial years under review. However, this average figure conceals a marked decline in the entry rate for the industry, from 16.7 per cent in 2009/10 to 10.3 per cent in 2012/13, or a fall of some 38 per cent in new start-ups.

4.5 The average entry rate for the:

- retail industry was 13.6 per cent per annum for the four years under review, falling from 17 per cent in 2009/10 to just 8.8 per cent in 2012/13;
- transport industry was 13.2 per cent per annum for the four years under review, dropping from 15.8 per cent in 2009/10 to 9.9 per cent in 2012/13; and,
- manufacturing industry was 9.6 per cent per annum for the four years under review, down from 11.6 per cent in 2009/10 to just 6.5 per cent in 2012/13.

4.6 The all-industry average entry rate for the four years under review was 13.8 per cent per annum (dropping from 16.7 per cent in 2009/10 to 11.2 per cent in 2012/13).

4.7 By comparison, the exit rate figures tell a much different story. For all four of the specific industry sectors under review – building and construction, manufacturing, retail, and transport – exit rates exceeded entry rates, on average, over the four years under review.

4.8 Exit rates for firms in the BCI averaged 15.3 per cent per annum, rising from 14.8 per cent in 2009/10 to 16.5 per cent in 2012/13, or an increase of just over 11 per cent in business closures. The average exit rate for the:

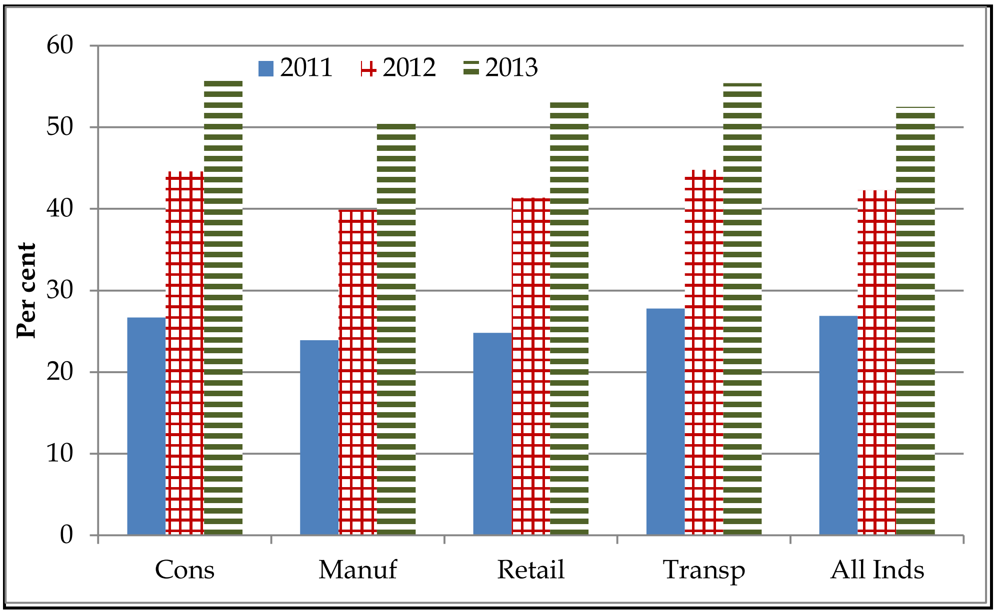
- retail industry was 14.7 per cent per annum for the four years under review, increasing from 14.0 per cent in 2009/10 to 15.7 per cent in 2012/13;
- transport industry was 15.3 per cent per annum for the four years under review, rising from 15.0 per cent in 2009/10 to 15.6 per cent in 2012/13; and,
- manufacturing industry was 11.9 per cent per annum for the four years under review, lifting from 11.8 per cent in 2009/10 to 12.5 per cent in 2012/13.

4.9 The all-industry average exit rate for the four years under review was 13.5 per cent per annum, moving from 13.1 per cent in 2009/10 to 14.1 per cent in 2012/13.

4.10 Another perspective on the entry and exit rates for businesses can be obtained from an examination of attrition and survival rates for new firms. The attrition and the survival rates are complements of each other: 100 – attrition rate = survival rate; or, 100 – survival rate = attrition rate.

4.11 Graph 2 reports the attrition rates for new firms in each of the industry sectors under review which commenced operation in 2010 – that is, essentially new, and most likely small, businesses.

Graph 2: Attrition Rates for New Firms in Selected Industries



4.12 The attrition rate for new firms established in 2010 in the BCI rose from 26.7 per cent of these firms after one year, to 44.6 per cent by the second year, to 56.1 per cent in the third year.

4.12.1 (All attrition rates are cumulative, so figures for the second year include those for the first year, with those for the third year including the two preceding years.) That is, over half of all new firms established in the BCI in 2010 had failed by 2013.

4.13 By comparison, the attrition rates for new firms established in the:

- manufacturing sector were 23.9 per cent in the first year, and 51 per cent by the third year;
- retail sector were 24.8 per cent in the first year, and 53.3 per cent by the third year; and,

- transport sector were 27.8 per cent in the first year, and 55.4 per cent by the third year.

4.14 The all-industries average attrition rates were 26.9 per cent in the first year, 42.3 per cent by the second year, and 52.5 per cent by the third year.

4.15 Nevertheless, it would at least appear the marginal rate of attrition (the change from one year to the next) appears to moderate with time, evident in the step-change in attrition between the third and second year of operation is smaller than that between second and first year of operation. However, further data collections and reports on business entries and exits will be required from the ABS to see if this ‘flattening of the attrition rate curve’ emerges for firms after four, five or more years in operation.

5 BCI Entry and Exit – By Sector

5.1 The ABS (ABS, 2014) also usefully reports business entry and exit rates for various sub-sectors within the BCI, summaries of which for the 2013 reporting year can be found in Tables 1 and 2, respectively.

Table 1: Entry Rates by Building Sector

	Entry Rate (%)	Entry Rate (%)	Entry Rate (%)
	All Firms	No Emps	1-19 Emps
Air Conditioning and Heating Services	9.4	11.6	7.8
Bricklaying Services	10.1	10.3	9.9
Carpentry Services	12.4	12.5	12.4
Concreting Services	11.2	11.7	10.9
Electrical Services	10.2	10.9	9.7
Fire and Security Alarm Install Services	8.1	8.4	8.2
Glazing Services	10.0	11.2	9.2
Hire of Cons. Machinery with Operator	4.5	3.4	6.4
House Construction	9.2	9.5	9.0
Land Development and Subdivision	4.8	4.9	4.6
Landscape Construction Services	9.9	10.8	8.8
Non-Residential Building Construction	7.7	7.0	9.6
Other Building Installation Services	9.9	9.1	11.0
Other Construction Services n.e.c.	12.0	12.1	12.4
Other Heavy and Civil Eng Construction	8.1	7.9	8.8
Other Residential Building Construction	7.4	7.1	8.6
Painting and Decorating Services	11.2	11.7	10.2
Plastering and Ceiling Services	14.6	14.4	15.1
Plumbing Services	9.9	11.5	8.4
Road and Bridge Construction	9.3	8.2	11.7
Roofing Services	12.5	14.4	11.0
Site Preparation Services	9.6	9.1	10.8
Structural Steel Erection Services	11.4	10.6	13.0
Tiling and Carpeting Services	11.4	10.7	13.2
Mean	9.8	10.0	10.0
Std Dev	2.3	2.7	2.3
CV	0.23	0.27	0.23
Min	4.5	3.4	4.6
Max	14.6	14.4	15.1

5.2 Looking first at entry rates for all firms in the BCI :

- the highest entry rates were experienced in the plastering and ceiling (14.8 per cent), roofing services (12.5 per cent) and carpentry services (12.4 per cent) sectors; and,

- the lowest entry rates were experienced in the hire of machinery with operator (4.5 per cent), the land development and subdivision (4.8 per cent) and the other residential building construction (7.4 per cent) sectors.

- The overall entry rate for all firms in the BCI was 9.8 per cent.

5.3 Turning to entry rates for firms without employees (essentially sole traders) the pattern is broadly similar to that for all firms:

- the highest entry rates were experienced in the plastering and ceiling (14.4 per cent), roofing services (14.4 per cent) and carpentry services (12.5 per cent) sectors; and,
- the lowest entry rates were experienced in the hire of machinery with operator (3.4 per cent), the land development and subdivision (4.9 per cent) and the other residential building construction (7.0 per cent) sectors.
- The overall entry rate for firms without any employees was 10.0 per cent.

5.4 The entry rate profile for firms in the BCI employing between 1 and 19 persons is slightly different:

- the highest entry rates were experienced in the plastering and ceiling (15.1 per cent), tiling and carpeting services (13.2 per cent) and structural steel erection services (13.0 per cent) sectors; and,
- the lowest entry rates were experienced in the land development and subdivision (4.6 per cent), the hire of construction machinery with operator (6.4 per cent) and the air-conditioning and heating services (7.8 per cent) sectors.
- The overall entry rate for firms employing between 1 and 19 persons was 10.0 per cent.

Table 2: Exit Rates by Building Sector

	Exit Rate (%) All Firms	Exit Rate (%) No Emps	Exit Rate (%) 1 - 19 Emps
Air Conditioning and Heating Services	11.9	16.2	7.2
Bricklaying Services	12.6	13.4	7.3
Carpentry Services	17.5	19.2	7.2
Concreting Services	15.2	20.2	7.5
Electrical Services	12.9	22.0	7.8
Fire and Security Alarm Instal Services	15.4	21.2	9.8
Glazing Services	15.3	19.0	8.4
Hire of Cons Machinery with Operator	13.2	26.5	8.8
House Construction	13.9	18.2	8.3
Land Development and Subdivision	13.2	20.3	8.2
Landscape Construction Services	19.5	23.3	9.2
Non-Residential Building Construction	15.8	25.7	8.4
Other Building Installation Services	13.7	19.6	13.2
Other Construction Services n.e.c.	15.0	20.7	10.8
Other Heavy and Civil Eng Construction	20.0	20.1	7.5
Other Residential Building Construction	14.0	21.8	10.3
Painting and Decorating Services	17.2	19.2	11.9
Plastering and Ceiling Services	17.5	23.0	11.2
Plumbing Services	18.9	23.5	8.2
Road and Bridge Construction	17.5	20.2	11.6
Roofing Services	20.4	25.1	11.3
Site Preparation Services	18.7	22.2	11.8
Structural Steel Erection Services	19.0	26.5	12.5
Tiling and Carpeting Services	22.8	26.6	14.1
Mean	16.3	21.4	9.7
Std Dev	2.9	3.3	2.1
CV	0.18	0.15	0.22
Min	11.9	13.4	7.2
Max	22.8	26.6	14.1

5.5 Looking first at <u>exit</u> rates for all firms in the BCI :

- the highest exit rates were experienced in the plastering and ceiling (22.8 per cent), other construction services (20.4 per cent) and the bricklaying (20.0 per cent) sectors; and,
- the lowest exit rates were in the hire of construction machinery with operator (11.9 per cent), land development and sub-division (12.6 per cent), and fire and security alarm installation (12.9 per cent) sectors.

- The overall exit rate for all firms was 16.3 per cent, which was well above the entry rate for all firms of 9.8 per cent (a 6.5 percentage point difference).

5.6 For firms without employees:

- the highest exit rates were experienced in the plastering and ceiling (26.6 per cent), roofing services, and other building installation services (both at 26.5 per cent) sectors; and,
- the lowest exit rates were experienced in the land development and subdivision (13.4 per cent), the hire of machinery with operator (16.2 per cent),) and the site preparation (18.2 per cent) sectors.
- The overall exit rate for firms without any employees was 21.4 per cent, more than double the entry rate for such firms of 10.0 per cent.

5.7 For firms employing between 1 and 19 persons:

- the highest exit rates were experienced in the plastering and ceiling (14.1 per cent), bricklaying services (13.2 per cent) and the tiling and carpeting services (12.5 per cent) sectors; and,
- the lowest exit rates were experienced the air-conditioning and heating services, and the land development and subdivision (both 7.2 per cent), and the hire of construction machinery with operator (7.3 per cent) and sectors.
- the overall exit rate for firms employing between 1 and 19 persons was 9.7 per cent, compared to an entry rate for such firms of 10.0 per cent.

5.8 While there is a plethora of information contained in Tables 1 and 2 regarding entry and exit rates across 24 sectors across three types of firms in the BCI , of particular note must be the relatively high exit rates experienced by firms with no employees, averaging just over 21 per cent (or one-in-five of such firms).

5.9 This relatively high exit rate should be a matter for concern, suggesting a potential wastage of training, and losses of skills, entrepreneurship and competition within the sectors concerned, and the BCI. However, it is not clear, or discernible from these aggregate figures, where these people go.

5.10 If they exit the industry completely, then there are substantial losses of investments in training, of entrepreneurship and competition, and of future capacity in the industry. However, if they transition from being firms with no employees to being firms with between 1 and 19 employees (even by taking on a single employee, such as an apprentice) then there may well be no loss (indeed, even a gain) to the industry.

5.11 Unfortunately, absent rigorous time series-panel data, such as regular and up-to-date releases of the ABS Business Longitudinal Database, it is not possible to say with any degree of certainty the operational trajectories of such firms.

6 Constraints and Challenges

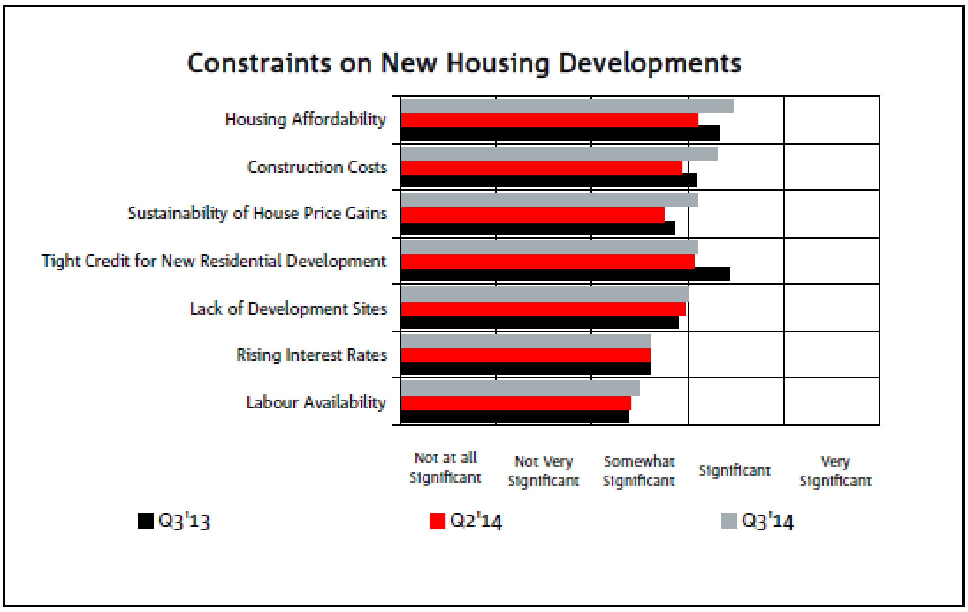
6.1 Master Builders is not aware of any specific, published detailed analyses of the drivers of business commencements and terminations in the BCI. However, an insight into some of the pressures on firms in the industry can be obtained from indicators published by the National Australia Bank for both the residential property (NAB, 2014a) and commercial property (NAB, 2014b) sectors.

6.2 The NAB's residential property survey asks respondents to comment upon constraints experienced on new housing developments and on demand for existing property, while its commercial property survey asks respondents to comment upon the critical challenges likely to confront the sector over the coming year.

6.2.1 These constraints (for residential property) and challenges (for commercial property) can be viewed as proxy indicators of likely stresses being experienced by firms in, and possible drivers for their exit from, the BCI.

6.3 Graphs 4 and 5 report constraints being experienced within the residential housing sector (NAB, 2014a) while Graph 6 reports on the challenges being confronted by the commercial property sector (NAB, 2014b).

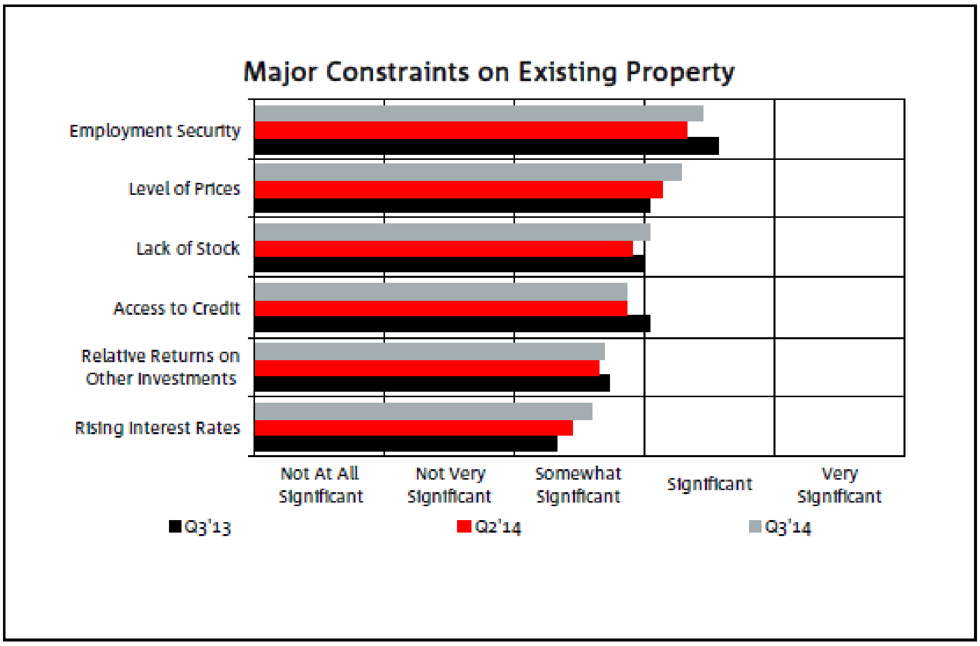
Graph 4: Constraints on New (Residential) Housing Developments



6.4 The most significant constraints on new housing development borne by the residential building sector relate to housing affordability, construction costs, tight credit for new residential development, and lack of development sites.

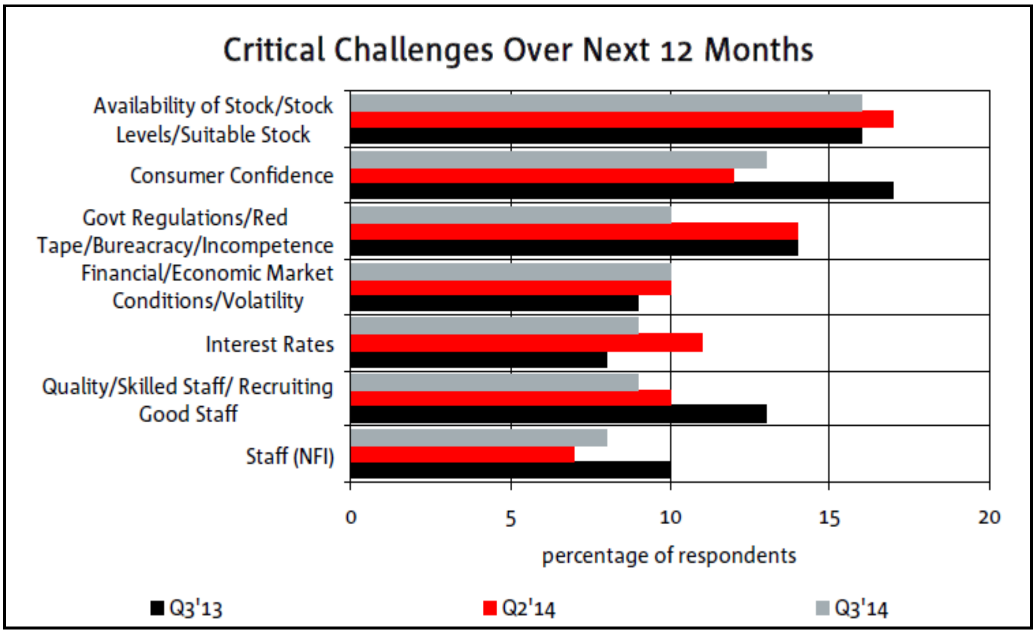
6.4.1 Constraints such as housing affordability and lack of development sites (both of which capture elements such as inadequate land supply, and poor planning and zoning arrangements), and construction costs (which can capture inefficient and unnecessary regulatory environments) can be traced back to government failure.

Graph 5: Major Constraints on Existing (Residential) Property



6.5 The most significant constraints on the existing residential property sector are essentially macroeconomic in nature, namely employment security and inflation (level of prices), although lack of stock and access also generally rank as somewhat significant barriers.

Graph 6: Critical Challenges for Commercial Property



6.6 The most important critical challenges confronting the commercial property sector are the availability of suitable stock, consumer confidence and poor government regulation/bureaucratic incompetence, the latter of which is indicative of government failure.

7 Regulations

7.1 Regulation, whether 'red' or 'green' tape, is a significant burden on the BCI, which is one of the most intensely regulated in Australia, with regulation imposed by all three tiers of government.

7.2 The compliance and reporting burden of regulation diverts scarce business resources away from entrepreneurial and innovative activities into form-filling (often of duplicative and/or of questionable value), and in the BCI this adds to the cost of housing supply and thus compounds other housing affordability stresses.

7.2.1 Anecdotal evidence provided to Master Builders by our rank-and-file members indicates regulations add between eight and twelve per cent to the cost of construction of the average Australian residential dwelling.

7.3 The Abbott Government has adopted an active and constructive regulation review, reform and repeal (4R) agenda, into which Master Builders has and will continue to advocate for a less burdensome and more efficient approach to regulation, in its design, in its administration, and in compliance.

7.4 In this context, Master Builders welcomes key initiatives taken by the Abbott Government, such as:

- publication of its "Australian Government Guide to Regulation", which will strengthen and make more transparent the regulatory development processes of federal agencies;
- publication of its "Regulator Performance Framework", which will improve the consistency and the transparency with which regulators undertake their responsibilities; and,
- twice-yearly regulation repeal days, which have, to date, made useful contributions to eliminating redundant regulations (although a sizeable challenge remains).

7.5 Nevertheless, Master Builders has identified a number of priority areas where further meaningful action is required, all of which will contribute to reducing the regulatory burden imposed on businesses in the BCI.

7.6 These include:

- substantially reducing State, Territory and Local Government variations to the National Construction Code (NCC);
- eliminating the differential classification and treatment of employees and sub-contractors within and between jurisdictions; and,
- improving third-party regulatory processes, especially where these regulations and their associated requirements are imported and/or referenced in Federal Government et al regulatory instruments.

7.7 Of particular irritation to rank-and-file builders are the sizeable (and growing) number of variations to the (supposedly) uniform NCC by State/Territory, but more significantly, Local Governments around the nation.

7.8 Such variations add to uncertainty in regulatory compliance for builders, and to the costs of construction for home and business owners. Rank-and-file builders have told Master Builders, inter alia:

> *There are too many documents to supply to councils that take too much time to get and in most cases are extremely expensive. e.g. Bushfire reports, acoustic reports, flood reports, shadow diagrams, site analysis, waste management plans, traffic management plans, streetscape analysis plans, hydraulic details, landscape plans, external colours, arborist reports, road opening permits and a myriad of council application documents.*
>
> *We deal with over 50 Councils and each one has a different set of application paperwork, documents, fees, contributions, building controls, cut and fill policies, stormwater policies and tree preservation policies.*
>
> *The time taken to approve very simple homes can take between 3 weeks to 3 months. If councils are busy e.g., Baulkham Hills, Blacktown or Liverpool then the time taken is ridiculous in most cases, up to 15 weeks.*
>
> *Additional quotes from our member-focus groups on regulation issues can be found at Appendix A.*

7.9 Master Builders recommends the Federal Department of Industry be charged with compiling and reporting on its website by the end of 2015 (with annual updates) a definitive and exhaustive list of all State, Territory and Local Government variations from the NCC.

7.10 In the short term, such a listing would promote greater transparency and competitive benchmarking of the incidence and impact of, as well as acting as the platform for subsequent program of work in reviewing, rationalising and potentially eliminating, such variations.

7.11 The BCI continues to have a very serious problem with the differential classification and treatment of employees and sub-contractors between and within jurisdictions in Australia. In the federal domain, this problem is particularly onerous under industrial relations and taxation law.

7.12 The status and treatment of employees vs sub-contractors under federal law is a significant issue for the BCI given these people, whether professionals such as architects, engineers or the like, or tradespeople, such as electricians, plumbers, concreters or the like, are the backbone of the industry.

7.13 Master Builders has identified a practical and workable solution to this problem, centred on a system of statutory registration, administered by the Australian Taxation Office, for those who choose to operate as an independent contractor.

7.14 Under our approach, persons looking to register for independent contractor status would be subject to a single set of tests, recognised across agencies and jurisdictions, which reflect the operation and conduct of a modern building sector. The tests would also establish clear separation between commercial law which should govern independent contractors, and workplace relations law which should govern employers and employees.

7.15 Master Builders recommends the Treasurer direct the Australian Taxation Office to establish a Government-Industry Working Party to implement by the end of 2015 the proposed system of statutory registration for independent contractors, and advance the necessary changes in federal law, regulation and/or administration.

7.16 Master Builders welcomes the directions set down in the "Australian Government Guide to Regulation" requiring regulators to consider alternatives to regulatory interventions, greater use and rigor in preparing high-quality cost/benefit and regulatory impact analyses, and increased transparency in the regulation development/review processes.

7.17 Of specific importance to the BCI is the obligation for Federal Government agencies, departments et al using standards et al created by third parties, such as Standards Australia, to ensure these instruments meet the Regulatory Impact Statement (RIS) requirements set down in the Guide.

7.18 This new threshold for the inclusion of third party standards or performance requirements into Federal regulations is significant for the BCI, given the expansive practice of the Australian Building Codes Board (ABCB) of importing Australian Standards into the NCC.

7.19 While Master Builders sees merit-in-principle in the privatisation of the regulatory process, through entities such as Standards Australia, this must not come at the expense of analytical rigor in the development and evaluation of the instruments thus created.

7.20 Master Builders recommends the ABCB be directed by the relevant Minister(s) that Standards or the like promoted or developed by third parties imported into federal government regulation be required to meet, as minimum, the performance thresholds set down in "The Australian Government Guide to Regulation".

7.21 At the very least, this must include rigorous and transparent Preliminary Impact Analyses, Cost/Benefit Analyses and RISs for each and every third party instrument adopted or imported into federal legislation or regulation.

7.22 To ensure third party instruments remain relevant to current practices, and do not unnecessarily impede innovation and change in future practices, such instruments where adopted or imported in to federal legislation or regulation should be subject to mandatory, defined (preferably not more than five year) sunset provisions.

8 Skills and Training

8.1 The BCI is 'moving up the skills curve', evident in the changing skills composition of its labour force – a trend which Master Builders expects to continue well into the foreseeable future. However, the gradient and the pace with which the industry is able to move up this 'skills curve' is, according to our rank-and-file members, being held back by shortages of skilled and para-professional labour.

8.2 At the same time, the nature of employment in the BCI is changing due to the introduction of new technologies and pre-fabrication. This is leading to altered work practices which no longer guarantee traditional career paths will generate the mix of skills needed to meet the future demands of the industry, and through it the Australian economy.

8.3 This situation is being compounded by the mismatch between Australia's industrial relations and its workplace relations systems.

8.3.1 Consultations with our members continually report the workplace relations system does not currently complement the Australian Apprenticeship system and has created potential barriers to the apprenticeship system being able to deliver maximum productivity benefits.

8.4 Other key messages coming from our member consultations, such as the member-focus groups conducted specifically for this submission, include:

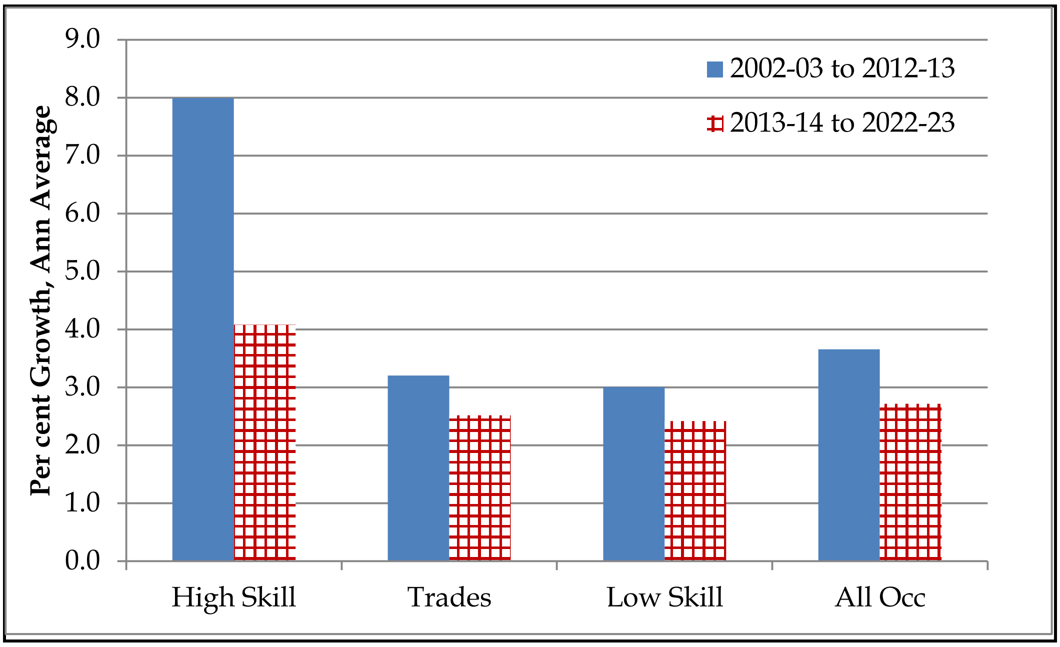
> *If the young blokes don't have business or entrepreneurial skills then they won't last very long in the industry.*
>
> *Getting (home warranty insurance) is a huge issue for new builders. But, they don't teach them this at trade school.*
>
> *The industry needs more business skills training. As an industry we do a poor job of teaching apprentices about business management.*
>
> *We should add one or two modules on business management to Cert 4.*

8.5 Additional quotes from our member focus groups on skills and training issues can be found at Appendix B

8.6 Graph 7 reports the changing skills composition of the BCI over the period 2002-03 to 2012-13 (n = 11 years), and then our forecasts of what we expect to happen over the 2013-14 to 2022-23 (n = 10 years).

8.6.1 The actual and forecast figures cover high skilled occupations (such as engineers and surveyors), tradespeople (such as electricians, plumbers), and lower skilled labour (such as general hand labourers).

Graph 7: Building Labour Force: Actuals and Forecasts



8.7 As can be seen, high skilled labour expanded by 8 per cent per annum, annual average, over the period 2003-03 to 2012-13, far-and-away ahead of the comparable growth rates for trades-skilled person (3.2 per cent) and low-skilled labour (3.0 per cent).

8.8 Master Builders expects this outperformance to continue over the 2013-14 to 2022-23 period, albeit with a narrower gap between the growth of highly skilled compared to trades- and low-skilled labour.

8.8.1 The growth rate for highly skilled labour is forecast to average around 4.1 per cent per annum over the forecast horizon, ahead of that for trades-skilled (2.5 per cent) and low-skilled (2.4 per cent).

8.9 Looked at another way, highly skilled labour accounted for 11 per cent of the labour force in the BCI in 2002/03. Master Builders forecasts this share will increase to 16.4 per cent by 2022/23.

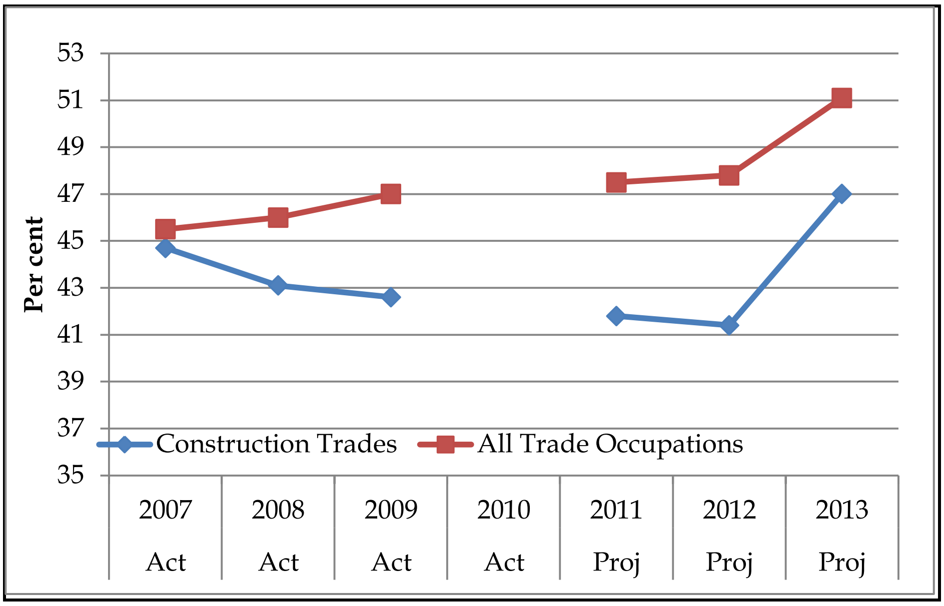
8.9.1 This increase will be accounted for by declines in the shares of both trades-skilled (down from 53 per cent to 50.4 per cent), and low-skilled (down from 36 per cent to 33.2 per cent) over the same period.

8.10 While the faster growth/rise in the share of highly skilled labour in the BCI is to be welcomed, of concern is the slower/growth decline in the share of skilled trades people in the industry, which if left unactioned could cause serious 'labour bottlenecks' in the building supply chain, and the efficiency and productivity of the industry.

8.11 This problem in part reflects, and is likely to be compounded by, the relatively lower completion/higher attrition rates for apprentices in the BCI (NCVER 2014).

8.12 Graph 8 reports completion rates for apprentices and trainees in the BCI, and all trades occupations, over the 2007 to 2009 (actual) and the 2011 to 2013 (projections) period (all data are derived from NCVER 2014).

Graph 8: Completion Rates



8.13 As can be seen, the completion rates for apprentices and trainees in the BCI (the blue line; diamond marker) has fallen below that for all trade occupations (red line; square marker) over the period under review.

8.13.1 Completion rates for apprentices and trainees in the BCI averaged 43.4 per cent for the six years for which there are reported observations, compared to 47.5 per cent for all trades occupations, a difference which is statistically significant ($t = 4.93$; t-crit = 2.57; $p = 0.00$) – that is, highly unlikely to be due to chance alone.

8.14 From a practical standpoint, it is deeply disturbing to observe more than half of all apprentices and trainees in the BCI (and indeed, in all trades occupations) fail to complete their apprentice/trainee-ships.

8.14.1 This situation amounts to an inefficient use of labour resources (both amongst the apprentice/trainee, and their mentors), the diversion of scarce financial resources (especially amongst smaller builders/firms) into activities which do not appear to generate a return to the individuals and the firm(s) concerned, and to the wider industry and the national economy.

8.15 This 'loss of return on investment' is especially disconcerting when it is realised (NCVER 2014) 34 per cent of apprentices/trainees in the BCI (and 31 per cent across all trades occupations) cease their training within just one year of commencement.

8.16 For many employers/mentors, this situation amounts to 'money down the drain', as few apprentices/trainees have acquired sufficient proficiency or skill in this short time frame to deliver any economic return-on-investment to their employer/mentor.

8.17 Master Builders has identified three potential initiatives which will help our industry and, if taken up and more widely applied elsewhere, the wider Australian economy to take meaningful action to deal with the existing, and potentially increasingly acute, shortage of skilled labour.

8.18 These initiatives are:

- greater harmonisation of apprenticeship systems and public sector funding policies around the nation;

- the development of “Passports of Competencies”; and,
- wider industry-owned qualification and competency development.

Harmonisation of apprenticeship systems:

8.19 The inconsistency of the apprenticeship system between State and Territories is a significant issue for the BCI, and it is important the development and enforcement processes of national qualifications be simplified.

8.20 The harmonisation of apprenticeship pathways and funding of qualifications is a micro-economic reform that is required to provide national consistency in the implementation of apprenticeship reform. This reform is necessary to reduce barriers to apprentice labour mobility and to reduce costs for business.

8.21 Against this background, Master Builders proposes the Vocational Education Training (VET) system become:

- nationally focussed with greater collaboration between the Commonwealth. and the States and Territories to meet the needs of industry and the economy including improved implementation and outcomes across jurisdictions;
- leading edge in the design and development of national training packages that are flexible to meet the needs of industry and provide clear guidance to Registered Training Organisations (RTOs) on the training and skills outcomes sought by industry. They must also clearly codify the skills and knowledge that a worker needs to perform a task or job; and,
- responsive to the ever changing needs of industry to compete within a globally competitive economy;

“Passport to Competencies”:

8.22 This initiative recognises Australia’s apprenticeship system is currently heavily focussed on the completion of full qualifications, despite the completion rate for publicly funded VET qualifications being only 36 per cent. A result of this is that in many trades the proportion of workers holding formal qualifications is actually dropping over time.

8.23 Part-qualifications, or skill sets, which may be appropriate to undertake a particular job role in the industry, should be recognised as a viable pathway to a job. Skill sets should not be seen as the end to training, but the "building blocks" to gain a full qualification over time where it is supported by the worker and employer.

8.24 Master Builders recommends the introduction of a 'skills passport' for the BCI where skill sets and individual units of competency can be undertaken in stages as a person's skills needs develop over time.

8.25 The 'passport' would allow for improved safety and quality outcomes and enable employers to quickly access workers' existing skills. The introduction of the Unique Student Identifier will be beneficial in helping employers and workers track their competencies.

8.26 By combining a series of units of competency and skill sets within the passport, students and workers could obtain a full qualification over time. The passport would be a mechanism to support life-long learning. In order to achieve this aim, the funding of skill sets and individual units of competency would need to be agreed on a national basis as currently there are different funding guidelines in each jurisdiction.

Industry-owned qualification and competency development:

8.27 Master Builders supports the Australian Government's review into *Industry Engagement in Training Packages: Towards a Contestable Model*. The centrality of industry in training package design, development, implementation and review is the cornerstone of the National Training System.

8.28 As VET is essentially an economic strategy to develop a skilled workforce to enable Australia to compete globally, the Government must remain committed to supporting their continual development and review to ensure they are meeting the needs of industry. Training packages are an essential component of the national VET system. In fact, they are one of the few truly national components of the system.

8.29 Master Builders recommends training packages, inter alia:

- be informed by real time intelligence that identifies the changing nature of industry, work practices and disruptive events including technological change and its resulting impact on required skills and knowledge;
- specify the knowledge and skills required to perform effectively in the workplace as determined by industry;
- provide clear guidance to RTOs on the skills and knowledge students are expected to acquire; and inform course design and assessment practices to ensure consistent outcomes across VET; and,
- be responsive to changing industry requirements including ensuring licensing requirements for specific occupations are considered in training package development and continually updated as needed.

8.30 Absent such reforms the BCI will likely find it increasingly difficult over the coming decade, and potentially beyond, to meet the rising demand for a skilled workforce against a background of a decreasing number of apprentices in accredited training, high drop-out training rates, an ageing workforce and an exit rate of existing workers of 30,000 persons per annum.

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Appendix A: Focus Groups on Regulation

"It really frustrates me that so many bureaucrats are really just trying to make work for themselves at my cost."

"I'm a small business, and really don't have the 'free time' for dealing with regulations. NSW is just so pro-reg."

"I'm not sure building regulators are always up to speed with the building regulations. Some of the things they ask for just make me wonder."

"The costs of going through the (regulator name here) are so prohibitive; we just had to settle (the claim) even though we were in the right. Our barrister just said 'pay up, and close it off'. We had to do, and fund, the remediation work when really it (the claim) was a maintenance issue which is the client's responsibility."

"The ATO (Australian Taxation Office) and some of the (State name here) regulators want builders to become their (enforcement) agents, which isn't right."

"You have to price red tape into your quote."

"Regulators don't understand the cash flow constraints small business in this industry work under. Workcover is the worst, with all of its upfront fees."

"There should be more use of 'one stop regulatory shops' – one place where you can go for advice and to get everything done, rather than having to run around all over the place."

"One area where they should tighten the regulations is owner builders."

"There really is two standards – one for registered builders, and one for owner-builders."

"Owner builders are a pain. They watch these (home renovation) shows on television, and think they can do it. Then we have to come along and clean up the mess."

"The worst thing (about local government) is inconsistency. One method or rule is applied in Gippsland, and another one in Kew."

"It is almost a lottery by postcode."

"Local governments are virtually unaccountable to anyone; little baronies."

"Regulations are a case of rolling with the punches."

"You can't afford to alienate local government. They get back at you, such as by delaying your paperwork."

Appendix B: Focus Groups on Skills and Training

"We need to train young builders much better in running a business. There is not enough 'running a business' (training) in Cert Four."

"We have to inculcate in apprentices that they are running a business – in building."

"If we sell a business, then 'long tail liabilities' go with the business."

"Most builders need to be 'off the tools' by the time they are forty (years of age). Their bodies just can't take it. So they need to have skills in project management."

"Building licences are too easy to get. We need to have a tiered licencing system. HWI (home warranty insurance) at the moment in (State name here) really is the de facto licencing system."

"HWI is really the framework for licencing – what you can do, the value of the work you can do."

"(Regulators and the industry) should look at a bronze/silver/gold tiered licensing system, which applies as the business scales up."

"We need tiering (of licences). Younger builders should have to get at least two years post ticket experience. They should also have a diversity of experience across a range of projects before they can get an unrestricted licence."