

21 February 2020

To the Manager, Consumer Policy Unit

Enhancements to Unfair Contract Term Protections - Regulation Impact Statement

The National Electrical and Communications Association (NECA) is the peak industry body for Australia's electrical and communications contracting industry, which employs more than 165,000 workers and delivers an annual turnover in excess of \$23 billion. We represent the best interests of over 5,200 electrical contracting businesses across all Australian States and Territories.

NECA has been advocating for, and on behalf of, the electrotechnology industry for over 100 years. We aim to help our members and the wider industry to operate and manage their business more effectively and efficiently whilst representing their interests to Federal and State Governments, regulators and principal industry bodies such as the Australian Chamber of Commerce and Industry (ACCI) and Standards Australia.

Unfair Contract Terms impacting Small Business in the Electrotechnology Industry

Small business and family owned enterprises (SME) are the lifeblood of the electrical and communications contracting industry, over 79% of the businesses within our industry employ up to 25 staff¹. These businesses generate the vast majority of their work as sub-contractors.

The relationship between sub-contractor and principal contractors is fundamentally imbalanced for the following reasons:

- electrical sub-contracting businesses are generally characterised as an SME, offering specialised electrical skillsets and capabilities. This profile is in direct

¹ NECA 2019 Industry Market Monitor <https://neca.asn.au/content/market-monitor-2019-0>

NATIONAL OFFICE

Level 4,
30 Atchison Street,
St Leonards NSW 2065
Locked Bag 1818,
St Leonards NSW 1590

T +61 2 9439 8523
F +61 2 9439 8525
E necanat@neca.asn.au
W www.neca.asn.au
ABN 78 319 016 742



contrast to principal contractors, which are mostly characterised as much larger, diverse and well-resourced organisations. Given the very polarised nature, scale and capabilities of these entities, sub-contractors are generally disproportionately disadvantaged in their ability to equitably participate and negotiate fair contracts;

- in general, the relationship between principal and sub-contractors is such that a dependency exists by the sub-contractor onto the principal contractor. This relationship also infers a power imbalance. Contractors are aware of this dependency and imbalance. NECA has concerns that this imbalance is often exploited by unscrupulous principal contractors;
- further to the size and power yielded by these principal contractors, there is only a very small pool of these principal contractors. This means there is limited competition in the area of principal contracting, resulting in sub-contractors regularly and consistently engaging with the same small group of principal contractors.

One of the most serious and ongoing issues facing SMEs is that unscrupulous principal contractors abuse their power and size to enforce detrimental and unfair contracts on smaller parties on a 'take-it or leave-it' basis. Sub-contractors, who tend to be smaller businesses often do not have the capacity to fairly and equitably negotiate contracts with larger principal contracts. This exposes SMEs in our industry to the potential to be taken advantage of, or enter into adverse and compromising contracts.

These conditions are resulting in the following adverse and inequitable outcomes:

- reinforcing the ongoing imbalance between principal contractors and sub-contractors in contract negotiations, given the inherent imbalance due to the power, scale and access to resources of larger organisations;
- deterring new entrants and existing tradespeople from owning and operating electrical SMEs, this is having a knock-on impact to the depleted and declining electrical skills workforce;



- penalising sub-contractors by effectively rendering them de-facto underwriters to unscrupulous or inefficient principal contractors;
- compromising quality assurance and the timely delivery of much needed new development, which is directly impacting the end consumers;
- legal disputes and bankruptcies across the electrotechnology industry; and
- broader economic impacts at both a local and national level, detrimental to the overall competitiveness, productivity and sustainability of our industry in Australia.

Unscrupulous principal contractors will often seek to shift and allocate risks and costs associated with projects e.g. overruns/delays, design variations and changes to materials/finishes, down the contract hierarchy, and onto sub-contractors through, and embedded within an inherently unfair contract. Due to the imbalanced size, power and capacity between principal contractors and sub-contractors as outlined in this submission, sub-contractors have a compromised ability to mitigate the transfer of these risks, or the capacity to control or manage the risks once they have been transferred. This again can have dire financial consequences for a small business, and potentially result in insolvency. Arrangements need to be designed and implemented to address the transfer of risk through a building contract from a principal contractor to a sub-contractor.

Under the current law, one of the requirements for a contract to be considered a small business contract is that at least one party to the contract employs fewer than 20 persons at the time the contract is entered into². NECA's experience indicates that businesses are much larger, and that the definition and size of a business should be amended from 20 to 100 persons employed, reflecting a more accurate picture of the business size employed to work on larger construction projects across many of our States and Territories.

² Enhancement of Unfair Contract Term Protections <https://ris.pmc.gov.au/2019/12/20/enhancements-unfair-contract-term-protections>



Further, NECA argues that the threshold on upfront price payable on the contract should be increased from \$300,000 to \$3,000,000 for contracts of 12 months or less, and from \$1,000,000 to \$9,000,000 for contracts greater than 12 months in scope. These thresholds reflect a far more realistic value on the price of contracts across the electrical contracting sector, particularly for medium scale enterprises with a larger number of staff involved, with more time consuming and complex project scales.

Security of Payments

Within the broader context of contract equity and fairness, we request that the Government consider the long-standing and secondary issue of Security of Payments. Fundamentally, NECA strongly advocates that sub-contractors should be paid for the work they do, and that safeguards be put in place to ensure that there is fairness, security and certainty in their payment as part of the contract for work undertaken.

Of all 'finishing trade' sub-contractors, electrical sub-contractors provide the highest value inputs by way of fixtures, fittings and labour towards the latter stages of the construction cycle. In this regard, there is a high element of financial risk to SMEs. It is not uncommon for sub-contractors to be one of the last in the credit line for payment, in the event of a principal contractor falling into receivership, sub-contractors are at risk of wearing the costs.

NECA seeks to ensure that electrical contractors are entitled to receive, and to recover, progress payments in relation to the carrying out of that work and the supplying of those goods and services. To this effect, NECA calls for national Payment Withholding Request legislation to allow the principal contractor to be more easily served with a claim for payment, and the introduction of a low cost, Retention Money Trust Account scheme - similar to models used in real estate and legal professions - with a threshold for construction project work to a value of \$1 million. These arrangements should be administered by a Government department to reduce costs and burdens and create a level playing field for industry.



NECA's recommendations

Whilst NECA commends the Government for extending the unfair contract term protections to SMEs in November 2016 under the Treasury Legislation Amendment (Small Business and Unfair Contract Terms) Act 2015, there is more work to be done as unfair contracts are still highly prevalent within our industry.

To this effect, we make the following recommendations to the Government to enhance the unfair contract protections and ensure a level playing field for small business and consumers:

- adopt Payment Withholding Request legislation nationally;
- introduce a low-cost Retention Money Trust Account scheme (similar to models used in real estate and legal professions) across all State/Territory legislatures with a threshold for construction industry project work to a value of \$1 million;
- amend the size of an SME to 100 employees as this would more accurately reflect the size of businesses engaged to work on larger construction projects across Australia; and
- the threshold on the upfront price payable on a building contract should be increased to:
 - \$3 million for contracts of 12 months or less, and
 - \$9 million for contracts greater than 12 months.

This more realistically reflects the price of contracts across the industry, particularly for medium size enterprises where larger numbers of staff are involved and project scales are more complex and time consuming.

Should you wish to discuss this submission or matters concerning our industry, I can be contacted on 02 9439 8523 or by email suresh.manickam@neca.asn.au

Yours faithfully

A handwritten signature in black ink, appearing to read 'Suresh Manickam', written over a horizontal line.

Suresh Manickam
Chief Executive Officer