

The Secretary

17 December 2018

South Australian Productivity Commission

GPO Box 2343,
Adelaide SA. 5001.
sapc@sa.gov.au

Re: SOUTH AUSTRALIAN PRODUCTIVITY COMMISSION - GOVERNMENT PROCUREMENT
INQUIRY.

Executive Summary

The Air Conditioning & Mechanical Contractors' Association of SA Incorporated is pleased to make a qualified submission to this Inquiry (the South Australian Productivity Commission – Issues Paper – *Government Procurement Inquiry*. 16 November 2018.)

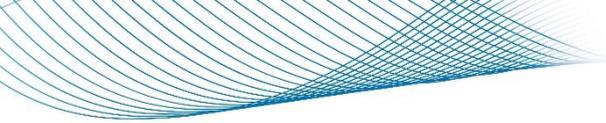
AMCA SA members are primarily sub-contractors or suppliers in the building and construction industry.

The terms of reference of this Inquiry exclude capital projects and therefore limits our response in this submission. Government procurement is oversighted by the South Australian Procurement Board (SAPB). The governing act and regulations of the SAPB, excludes it from reviewing building and construction work, greater in value than \$165,000.

It has been the AMCA SA members experience, along with a range of other specialist contractor associations that, with the exception of the Department of Planning, Transport and Infrastructure's excellent work over the past several months, there are few processes in place for sub-contractor members, undertaking government work in building and construction, to see processes are in place to:

- monitor consistent terms and conditions throughout the contractual chain, at the time of the issuing of head contracts and sub-contracts;
- or their operation during the project;
- the proportional allocation of risk, or;
- the application of the government's commitment to pay the sub-contractor within 30 days.

We hope that future inquiries will look to review government procurement in the building and construction industry.



Industry Background

AMCA is the industry's voice in dealing with governments, other construction and service industry groups and the unions.

Since its inception in 1961, AMCA's objectives have been to promote and protect the interests and welfare of the air conditioning and mechanical services industry, its members, and the public they serve.

AMCA members design, install and provide ongoing service of air conditioning and mechanical ventilation systems to the vast majority of city buildings, hospital, schools sporting and community, industrial office and defence infrastructure.

The air conditioning and mechanical services industry is diverse, complex and at the cutting edge of environmental and energy efficiency issues. Our members collectively are responsible for:

- \$1.2B in value of new plant installed annually.
- \$500M in equipment service and maintenance work.
- The directly employ some 8,000 people.

Our South Australian AMCA (AMCA SA) members account for almost twenty five million dollars of new plant installed, approximately eighteen million in service and maintenance work. These members directly employ over 600 people and another 1,500 employees via sub-contractors and supplier members.

An overview of the AMCA SA Submission

Our members have seen the benefits of the industry participation focussed on creating opportunities for local business, including building and construction. The Department of Planning, Transport and Infrastructure is an example of SME business engagement.

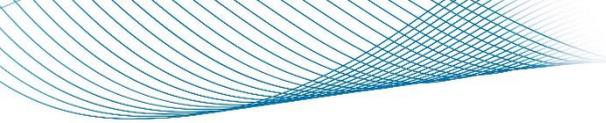
In no small part, advocacy across the building and construction industry and other areas of procurement has come about by the oversight of the Office of the Industry Advocate. However, there remains concerns that, not all procurement in all departments, conform to the procurement standards or payment standards the State Government requires.

The office of the Small Business Commissioner has through their oversight of business contracts and payment and is currently working on the national review of payments in the building and construction industry, in particular its response to and application of the J Murray report.¹

The Government Procurement Inquiry (the Inquiry) precludes capital projects and prescribed authorities, e.g. SA Water and the South Australian Housing Trust².

¹ Australian Government. *Review of Security of Payment Laws – Building Trust and Harmony*. John Murray AM. December 2017.

² The 13 public authorities prescribed by the *State Procurement Regulations 2005* are: Adelaide Venue Management Corporation, Architectural Practice Board of South Australia, Construction Industry Training Board, Health Services Charitable Gifts Board, Legal Profession Conduct Commissioner, Local Government Finance Authority of South Australia, Motor Accident Commission, Return to Work Corporation of South Australia, South Australian Forestry Corporation, South Australian Housing Trust, South Australian Water Corporation, Superannuation Funds Management Corporation of South Australia and Urban Renewal Authority.



AMCA SA members are engaged in a large number of building and construction projects, whose procurement, tendering, contracts, administration and completion are undertaken by the Department of Planning, Transport & Infrastructure (DPTI). Based on the Figure 3. of the Inquiry paper, DPTI accounts for 15% of Agencies' share of procurement spending on goods and services, but this amount does not include the capital projects the department undertakes for the government and its various departments.

Notwithstanding the DPTI, which adheres to practices around:

- indigenous participation schemes;
- training and apprenticeship ratios;
- local (SA Businesses) participation and supply;
- contractor pre-qualification standards; and
- working with the building construction sector, on contractual terms & conditions and risk management allocation through the contractual chain.

are other state departments adhering to those standards and who oversees those procurement matters?

The State Procurement Board precludes itself from oversight of almost all building and construction procurement activities of the states' various departments³.

On the above basis, AMCA SA has been hesitant to make a submission to this Inquiry.

AMCA SA is very disappointed that such restrictions have been placed on this Inquiry.

AMCA SA could make a more substantial contribution to this Inquiry, were it to include capital projects procurement.

AMCA SA will outline the areas in which it could make comment on.

Notwithstanding government (South Australia or Federal) undertakings and statements in the Inquiry paper, to the effect that, both in building and construction and service and maintenance contracts:

“... government requirements to the contrary (government expects sub-contractors to receive contract terms consistent with the head contract terms and conditions, and agencies are to undertake financial checks before the letting of the contract and during its operation).”⁴

AMCA SA has not been made aware that such processes are in place to monitor consistent terms and conditions throughout the contractual chain, at the time of the issuing of head

³ 5—**Certain prescribed construction projects excluded from definition of procurement operations (section 4 of Act)**

(1) For the purposes of the definition of **procurement operations** in section 4 of the Act, a prescribed construction project of a cost exceeding \$150 000³ is excluded from the definition.

(2) A **prescribed construction project**—

(a) is a project that primarily involves the procurement of construction work; and

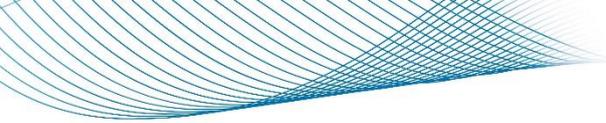
(b) encompasses—

(i) the acquisition and installation of fixtures, plant, equipment, appliances and fittings in conjunction with the construction work; and

(ii) the acquisition of survey, planning, design and other services in conjunction with the construction work; and

(c) does not encompass the acquisition of goods and services for the ongoing maintenance of a building or structure.

⁴South Australian Government. *Issues Paper: Government Procurement Inquiry*. November 16, 2018. Pg. 12.



contracts and sub-contracts, or their operation, the proportional allocation of risk, or the application of the government's commitment to payment within 30 days.

It is only the DPTI, in recent times that has begun to transform these processes in their capital projects work and the AMCA SA commends them for it.

AMCA is of the view that, there is a myopia adopted when discussing payment terms, at least in building and construction and goods and services contracts. The client (government) considers that it pays the contractor (the builder) within 30 days, but fails to recognise, or put in place, any visibility that the businesses (sub-contractors) who:

- supply the materials (which must be paid for from 7-30 days),
- pays the wages (7 – 14 days);
- build structure, install all the equipment, fixtures, finishes and fitouts (that must be paid for in 30 days)

are paid in 30 days.

Notwithstanding the combined cost of material, payment of wages and the building and installing, comprises more than 75% the total building project cost, being supplied by and paid for by sub-contractors - the sub-contractors, are not paid in 30 days.

In most cases, sub-contractors are not paid on time, regardless of what their contractual terms are under the sub-contract, or related to any government policy.

Reports prepared by Coggins, Teng and Rameezdeen⁵, Collins (2012), The Senate (SERC, 2015) and Murry J. (2018) indicated that:

Payment terms between principal contractors and their sub-contractors fell between 45 and 80 days, and in worst cases extended to between 90 and 120 days⁶. Globally⁷, Australia has the worst payment numbers / average days to pay at 26.4 days after the due date! In the building and construction industry that means that is more than sixty (60) days after the work is completed!

The construction industry accounted for 8-10% of national gross domestic product, but accounted for 23% of all external administrations⁸! These statistics finalised in 2014 and since then have changed little.

Combine consistent lagged payment to sub-contractors, combined with:

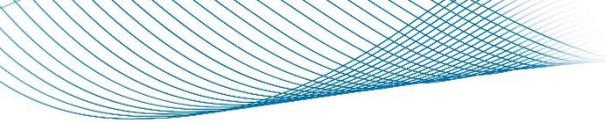
- the continual shifting of all forms of risk down through the building and construction contractual chain, away from those most capable of managing risk down to those least capable of managing that risk,

⁵ *Construction insolvency in Australia: Reigning in the Beast*. Coggins J, Teng B., Rameezdeen R. School of Natural and Built Environment, University of South Australia. Construction Economics and Building. 2016

⁶ Subsequent to this finding, the NSW Parliament introduced amendments to the *Building and Construction Industry Security of Payment Act 1999* (NSW) requiring that progress payments under a construction contract become due and payable on the date occurring no later than 15 business days after a payment claim is made by a head contractor, and no later than 30 business days after a payment claim is made by a subcontractor.

⁷ Source:MarketInvoice, The State of Late Payment 2016 www.marketinvoice.com. drawn from page 14, Review of Security of Payment Laws: Building Trust and Harmony, John Murray. 2018.

⁸ The next largest single identifiable industry is retail trade, accounting for 10% of all external administrations.

- 
- implementing head contractor sub-contracts conditions that bear little resemblance to the contract provided from the client to the head contractor; and
 - where the sub-contractor has little or no bargaining power to negotiate fairer contractual terms;

Is it any wonder that the level of insolvency in building and construction are so bad!

Key submission points:

AMCA SA could provide responses to:

- *delays and lack of transparency of the tender process*
- *aggregated contracts*
- *poor quality of tender*
- *focus on immediate cost instead of whole of life cost*
- *delayed payment*
- *sub-contractor exposure to head contractor failure*

In particular, areas raised of the issues paper on:

Delayed Payment

Late payment adversely affects small businesses, especially when payment terms are not aligned with completion of work. The size of final withholding payments at completion needs to be considered to preserve business cash-flow.

Conditions of Contract and the passing on of risk

This issue is mostly encountered in the building and construction industries, where subcontractors assert some head contractors impose onerous and unfair contract conditions despite government requirements to the contrary (government expects sub-contractors to receive contract terms consistent with the head contract terms and conditions, and agencies are to undertake financial checks before the letting of the contract and during its operation).

Insurance liability and indemnity requirements not commensurate to the tender

Business assert that contract performance is not being measured post award and most of the compliance effort is currently addressed through the tender process

Non-conforming materials and product

imported products entering Australia do not comply with environment and safety regulations that are applied to Australian products.

Auditing regimes: Anecdotal evidence suggests that the audits required to verify that standards specified in tenders are met are rarely done for interstate or overseas suppliers, in contrast to local businesses

Sub-contractor exposure to head contractor failure

This issue is mostly encountered in the building and construction industries, where subcontractors assert some head contractors impose onerous and unfair contract conditions despite government requirements to the contrary (government expects sub-contractors to receive contract terms consistent with the head contract terms and conditions, and agencies are to undertake financial checks before the letting of the contract and during its operation).

The procurement process:

The procurement process involves three stages:

- *Acquisition planning*
- *Supplier selection*
- *Contract management*

Post Procurement Reviews by SPB:

The Board can undertake: post-sourcing reviews for procurements exceeding \$4.4 million; or post-sourcing reviews for other procurements at the discretion of the board.29 Public authorities are also required to report specific milestone dates for contracts valued over \$220,000 (GST inclusive);

More generally, AMCA SA would respond to some of the Feedback Questions contained in the issues paper.

In closing, the AMCA SA would like to thank the South Australian Productivity Commission for opportunity respond to this Inquiry.

Yours sincerely,

Christopher Rankin



EXECUTIVE DIRECTOR

Air Conditioning & Mechanical Contractors' Association of South Australia Inc.,