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Unfair Contract Terms

Construction Industry Submission to the Federal Government

Top row L-R: Andrew O'Connor (SCA), James Cameron (ACIF), Jason Tait (MPA), Andrew Wallace, MP, Ben Hawkins (AMCA), Scott Bryant (Fredon), Stafford Poyser (NECA), Chris Lehmann (MEA), Lauren O'Keefe (NECA). Bottom row L-R: Larry Moore (RACCA, SCA and NECA SA/NT), Trevor Gauld (ETU), Irma Beganovic (NECA), Dai Le, MP, Kent Johns (NECA), Nathanial Smith (MPNSW).

Foreword

On Monday 13 November 2023, NECA together with Ms Dai Le, Federal Member for Fowler hosted a roundtable at Parliament House Canberra to discuss unfair contract terms within the construction industry.

The use of unfair contract terms is placing unnecessary pressure on an industry that is already facing unprecedented challenges including escalating labour and material costs, skills shortages and supply chain issues.

Australian subcontractors, the parties in the contractual chain carrying disproportionate risk, are calling for removal of unfair, partial, imbalanced, and anti-competitive contract terms for the construction industry.

While the government aims to establish efficient and cost-effective processes by awarding contracts to head contractors, it is crucial to ensure that favourable and fair terms granted to head contractors also cascade to the subcontractor in full.

To ensure government policy effectively promotes fairness in contracting for all industry participants, and as an outcome of the roundtable, I support this joint industry submission comprising a range of recommendations to the Commonwealth Government.

Dai Le
Federal Member for Fowler

Overview

Unfair Contract Terms has emerged as a crucial issue across the construction sector particularly in specialist subcontracting trades and businesses.

The presence of Unfair Contract Terms within subcontracting agreements undermines the principles of fair competition, collaboration and equitable treatment of all parties involved.

It creates an imbalance of power between the head contractor and subcontractor, which not only hampers the ability of subcontractors to operate efficiently, but inhibits economic growth, commercial fairness, critical infrastructure project delivery and innovation within the industry.

The industry acknowledges that large-scale projects often involve complex contracts, requiring the involvement of multiple subcontractors.

More burdensome clauses than those in the head contract should not be applied to the subcontractor delivering the physical works, which at times total costs and expenses carried by the subcontractors can be as high as 85% of works completed ie 85% vs 15% risk allocation to subcontractors.

As advocates for fair business practices for subcontractors and the wider construction industry, the organisations involved in the preparation of this document would like to emphasise how Unfair Contract Terms can impact subcontractors, both economically and legally, and what can be achieved to improve the sector as a whole.

Additionally Unfair Contract Terms can also place significant impacts and undue pressures on tradespeople, especially when project timeframes become compressed and subsequent clashes of trades on site start affecting people's wellbeing and general workplace health and safety.

Unfair Contract Terms that result in project delays also run the risk of subcontractors losing workforces to other projects, in a climate where workforce shortages have never been so severe in the industry.

This submission has been jointly prepared by the National Subcontractors Forum industry members including:

- National Electrical and Communications Association
- Refrigeration and Airconditioning Contractors Association
- Specialist Contractors Association
- Electrical Trades Union

- Airconditioning and Mechanical Contractors Association
- Electrical Inspectors Victoria
- Master Plumbers Australia New Zealand
- National Fire Industry Association Australia
- National Electrical Switchboard Manufacturers Association
- Australian Cabinet and Furniture Association
- Civil Contractors Federation
- Fredon
- Master Electricians Australia
- Australian Cabler Registration Service
- Surveyors Australia.

Industry representatives expressed their concerns directly to government, including to the Honourable Dr Andrew Leigh MP, Assistant Minister for Competition, Charities and Treasury, and Assistant Minister for Employment, who was in attendance and whose work was also instrumental in the development and release of the Commonwealth Government's Unfair Contract Terms (UCT) Reform Bill, which came into effect on 9 November 2023.

Background

In October 2022, the Federal Government announced amendments to the Competition and Consumer Act 2010 (CCA) including the Australian Consumer Law (ACL) and the ASIC Act, in relation to Unfair Contract Terms.

The Unfair Contract Terms (UCT) Reform Bill passed in November 2022, and commenced on 9 November 2023.

However, both the existing terms and the recent legislative amendments to the UCT may present a wider unintended consequence to the construction industry which can impact the standard contracts, contract terms and customer engagement processes.

On 13 November 2023, members from the National Subcontractors Forum and other industry bodies representing specialist contractors attended an industry roundtable at Federal Parliament to analyse UCT issues facing the industry and reach a consensus as to a path forward to advocate for the removal of unfair, partial, imbalanced, and anti-competitive contracts and terms when supplying services to the industry.

The industry has identified a range of factors currently impacting the industry in relation to Unfair Contract Terms as outlined below.

Unreasonable risk allocation

Subcontractors are often burdened with an unfair share of risk compared to the head contractors.

This may include excessive liability clauses that hold subcontractors responsible for damages or delays caused by factors beyond their control or their scope of works.

Such terms unfairly shift the risk from the principal contractor to the subcontractor, creating an unequal distribution of responsibility.

It also places risk on parties that are not capable of managing the risk.

Further, subcontractors do not have any in-house solicitors to issue/respond to highly complicated legal notices (as a result of unfair contract terms), which result in subcontractors being time barred from making or defending claims.

Unilateral variation clauses or termination for convenience

Some subcontracting agreements containing unfair contract terms grant principal contractor's unilateral authority to modify or

terminate the terms of the contract without obtaining the subcontractor's consent.

This can lead to arbitrary changes in scope, pricing, or project requirements, leaving subcontractors in vulnerable positions where they have limited control over their rights, obligations, and compensation.

If not carefully considered, this can also lead to significant loss of work for tradespeople and consequently loss of workforces, because subcontractors and their workers expect to be engaged to deliver the work that they agreed to do.

Payment delays or non-payment for variations

Some agreements containing unfair contract terms may include extended payment periods or introduce complicated and unachievable payment conditions when seeking payment for variations to the contract.

Subcontractors are often left waiting for extended periods to receive payment (or not at all), which forces them into litigation, places strain on their cash flow, hampers their ability to cover expenses, and impacts financial stability, including non-payments of super obligations.

Unbalanced indemnification clauses

Indemnification clauses in subcontracting agreements can disproportionately burden subcontractors with the responsibility to compensate the principal contractor for damages or legal costs, in circumstances where fairness would dictate that subcontractors should shoulder no responsibility.

These clauses are often one-sided, neglecting to address instances where the principal contractor may be at fault or responsible for the issues at hand; Such clauses unfairly expose subcontractors to potential financial risks and legal disputes.

Lack of transparency

Many subcontracting agreements are complex and difficult to understand, particularly for small businesses or individual subcontractors with limited legal resources.

Unclear language, ambiguous provisions, or hidden clauses can be used to exploit subcontractors who may unknowingly agree to terms that are disadvantageous to their interests; greater transparency and simplified contract language would help ensure fair and informed agreements.

Provisions concerning delays to projects and associated costs

The usual term in most Commonwealth project subcontracts is that, "an Extension of Time is the subcontractor's sole remedy for any delay".

This makes it impossible to seek any additional payment caused by extensions of time for the completion of work, even when the reason for the extension is caused by other parties.

For example, a subcontractor enters into a six month contract.The contract runs for two years through no fault of the subcontractor.

The subcontractor has to carry all the additional labour and equipment hire costs for the additional 18 month period.

Generally all subcontracts have Extension of Time clauses, however these are usually unfair and onerous, with strict time barring provisions.

Many subcontractors experience difficulties complying with these onerous clauses, especially without the assistance of experienced inhouse solicitors.

In the circumstances, this results in subcontractors having to compress their timetable to complete work, which results in greater costs associated with employees having to work overtime.

Delays are rarely compensated for rising goods, services, or labour costs where delays are extended over extremely long periods of months and years. Most suppliers of goods and services provide pricing for set periods which cannot be fixed should project delays extend past the pricing period.

Labour cost increases via either an award or EBA renegotiation that has occurred cannot be recovered should a project be delayed where a lump sum fixed contract has been agreed.

Subcontracts that do not reflect head contract terms or conditions

Many subcontracts provided to small and medium-sized subcontractors bear no relation to the head contract provided to the principal contractor.

Many clauses are amended or deleted where they may allow relief to the subcontractor, yet the head contractor can utilise these clauses for their benefit without providing the same relief to their subcontractor.

Differing head contractor terms and conditions can often lead to subcontractors having disparate employment arrangements for their workers which cause further friction on sites (eg site allowances).

Legislation and Standards

As a result of the amendments to UCT laws passed by the Federal Government in November 2022, a range of subsequent changes came into effect on 9 November 2023.

The existing UCT laws, contained in the ACL and ASIC Acts, have been in place since July 2010 for consumer contracts, and November 2016 for small business contracts.

The legislative changes follow years of advocacy by the Australian Competition and Consumer Commission (ACCC), which claimed the existing UCT regime did not provide a strong enough deterrent for businesses whom the ACCC found, were continuing to use and rely on unfair contract terms in their standard form contracts.

The amending legislation overhauls the existing UCT regimes in both Acts by aiming to:

- Strengthen and clarify the existing UCT regime to reduce the prevalence of unfair contract terms in consumer and small business standard form contracts
- Introduce a civil penalty regime prohibiting the use of and reliance on UCTs in standard form contracts
- Expand the class of contracts that are covered by the UCT provisions
- Clarify the power of courts to make orders to void, vary or refuse to enforce part, or all, of a contract containing UCTs.

The ACL provides protection for consumers and small businesses, but the unfair contract terms are in all contracts which effect all commercial contracts regardless of the business practices and size of the commercial entity.

The legislation needs to go one step further and prohibit certain 'unfair' clauses commonly found in construction contracts.

A $50 million fine does not save a small business from insolvency. Immediate relief and action is required for small businesses to survive.

Many small businesses are family businesses with family members and friends either on the tools, doing the books, or working as apprentices.

Generally small businesses do not have the means or the time (before their businesses collapse) to go to court to have unfair terms set aside.

This is a denial of natural justice to small contractors.

The current changes to UCT will leave mid-sized commercial entities who fall outside the definition of a small business exposed when dealing with larger contracting companies, or principal entities.

The UCT laws provide that a contract term is an 'unfair' term where:

- The term causes a significant imbalance in the parties' rights and obligations arising under the contract
- The term is not reasonably necessary to protect the legitimate interests of the party who would be advantaged by the term; and
- The term would cause detriment (whether financial or otherwise) to a party if it were to be applied or relied on.

The legislation focuses heavily on the consumer impact and whilst it is an important step forward to addressing unfair contract terms, the construction industry believes that a stronger approach is required – whether that be more streamlined procurement practices at all levels of government or extending the legislative scope to remove specific clauses that are deemed to be unfair.

Additionally, the industry is asking the Government to intervene with Standards Australia processes that enable amendments to be made to standard form contracts to the extent that they no longer resemble a standard form contract.

For example, whilst it is acknowledged that AS2124 are general conditions of a contract which can be merged with other contractual terms, the basic principles of the contract should be maintained to be recognised as the Australian Standard Form contract.

This is particularly important where a significant shift in risk allocation is contained in the amended contract which changes the outcome for the subcontractor who thinks the contract is a genuine Australian Standard.

This practice must be minimised to ensure subcontractors and their workers are not unfairly treated by head contractors.

Industry Recommendations

To further build trust in the building and construction sector the federal government needs to enhance legislation and contractual practices to better reflect fairness and transparency in contracting.

Adopting fair and balanced terms and prohibiting unfair terms consistently found in construction contracts will foster healthier relationships with all contracting parties and create a more ethical and sustainable business environment for all industry participants.

Members of the National Subcontractor Forum agreed on recommendations to the Federal Government to ensure the newly enacted legislation does not result in unintended consequences for the construction industry.

1. Fairer commercial balance and fairer risk allocation in contracts

Often a subcontracting business is hesitant to legally challenge unfair contract terms due to the possibility that the principal contractor and/or major client will cease to engage them and seek a competitor willing to accept the proposed contract terms without pushback or hesitation.

This can result in businesses accepting unfair contract terms to maintain relationships and secure future contract opportunities.

Many subcontractors have identified excessive liability clauses that hold them responsible for damages or delays caused by factors beyond their control or totally unrelated to their scope of works.

This includes areas such as liquidated damages and consequential loss claims that are disproportionate to the quantum of works undertaken by the subcontractor and outside of their control.

Removal of reasonable and fair rise and fall clauses from subcontracts, placing the burden of market forces beyond the contractor's control squarely on smaller enterprises, protects the head contractor from any economic consequences while exposing subcontractors to greater financial risks.

In the current economic climate of supply chain disruption, skills shortages, industrial relations reforms, and interest rate fluctuations the risk is growing ever greater.

> It is recommended that the Federal Government work with both the industry and with Standards Australia to review Standard Form Contracts and all process associated amendments of Standard Form Contracts, in an effort to ensure future transparency, consistency, compliance and fairness for all parties.

2. Stronger government procurement practices to benefit all contractors

Public funds need to be expended in a manner which is transparent and fair for all levels of procurement and purchasing.

This fairness does not stop at the head contractor level and needs to trickle down to all parties involved in the works funded by the government.

There are head contractors (on government projects) whose modus operandi is push the subcontractor to do substantial work without paying that subcontractor.

The head contractor then back charges that subcontractor with liquidated and other damages, cashes in their bank guarantees, terminates the subcontract with the assistance of unfair contract terms, then get another subcontractor to complete those works.

The head contractor not only has a win fall for all the unpaid work carried out but also for the win fall of the subcontractor's bank guarantees.

Dependence on a single head contractor without providing fair terms to subcontractors creates an inherent risk for government projects.

If the head contractor faces financial challenges, disputes, or delays, subcontractors may bear the brunt of the consequences, potentially leading to project disruptions or even failure.

Contractual arrangements included for head contractors on government-funded projects need to be reflected in subcontractor contracts to ensure a proportionate distribution of commercial risks and benefits (for example consistent approaches to the inclusion of liquidated damages in contracts for contractors and those of subcontractors).

It is simply unacceptable for such imbalances to exist on any projects, especially on publicly funded initiatives.

> To support industry stability for subcontractors, ensure continuity and minimise project risks, the industry recommends that government procurement ensures contract clauses for head contractors on government contracts are reflected all the way through the contractual chain.

Principal contractors typically request bank guarantees from subcontractors; these guarantees are commonly agreed upon to be returned to the subcontractor upon the practical completion of a project and at the conclusion of the defect liability period.

However, subcontractors are not always informed of the practical completion, which makes it challenging for them to determine the end of the liability period.

> We advocate for contracts to include mandatory communication of completion to all subcontractors.

Moreover, discussions have revealed that contractual deadlines are frequently not met and are often substantially delayed.

These delays lead to additional interest expenses for the subcontractor and significantly limit their operational capacity for other projects, as a substantial amount of capital remains tied up in completed projects.

Additional reform to place legislative expiry dates on bank guarantees to ensure that they expire on the dates agreed to within the original contract will result in a significant reduction in subcontractor interest expenses.

This reform would create certainty for business planning and free up a subcontractor's own capital associated with work that has been completed for employment and business growth.

3. Expanded coverage of national unfair contract terms legislation

Specific definition of small business being legislated requires at a minimum an expansion to include medium-sized firms if not expanded to cover all contracts.

An unfair contract term is by definition, unfair and should be removed from all contracts once deemed to be unfair, no matter the size of organisations involved.

It is commercially and morally appropriate to ensure unfair contracts terms are unable to be used at any level.

The amended definition of small business has been expanded to include businesses that employ fewer than 100 employees or had less than $10 million in annual turnover in the previous financial year.

The definition of small business must be uniform throughout all legislation both State and Federal jurisdictions.

The absence of such uniformity can cause a power imbalance upstream from which stops at mid-sized contractors.

If terms are deemed unfair, they should be available to all businesses; if a contract term is unfair, it should by definition be unfair to all.

The industry recommends the Federal Government amends the legislation to also include medium-sized businesses.

> The industry also recommends the Federal Government expands the coverage of UCT legislation to include a range of specific provisions and clauses for ease of identification of unfair contracts.
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> The Queensland Government is currently consulting with the industry on a range of clauses that could potentially be prescribed in the state's legislation to ensure stronger fairness in contracting.
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> These include for example: indemnity clauses that excessively extend liability, warranties for design and document accuracy and wrongful termination deemed to be for convenience.
>
> The industry strongly recommends the Federal Government consult with the Queensland Government on these provisions to ensure future consistency in legislation and fairness in contracting nationally.

4. Greater powers to adjudicators

Justice delayed is justice denied.

While litigation is available to everyone, it unfortunately is not accessible to smaller operators due to costs associated with the process.

Further small businesses require immediate relief, delays in payment cause bankruptcy, breakup of marriages, families and homes.

Court proceedings are time consuming and cost prohibitive.

It is well known that cashflow is the lifeblood of the construction Industry.

Many businesses cannot afford to engage solicitors and barristers, or to seek remedies that only a judge has the power to provide relief from.

Creating a system that allows subcontractors to engage with an independent adjudicator that has the authority to expeditiously rule on unfair contract terms, will further ensure that this

legislation saves many small businesses from insolvency/bankruptcy.

In addition the balance of power in contract negotiations will remain fair and not at the financial expense of the smaller business.

In line with John Murray's *Review of Security of Payment Laws* report, the industry supports the following recommendations relating to improvements to adjudication processes:

- Looking at how adjudication applications are made, the associated timeframes, how adjudicators are appointed, the requirements for responding to an adjudication application and the timeframes for decisions.
- Considering what actions should be available to the parties following an adjudication determination, including whether there should be a process for review of adjudicators' decisions.
- Defining the role of the Regulator and Authorised Nominating Authorities in the appointment process for adjudicators, the skills, qualifications and experience and the statutory obligations adjudicators should have.

5. Ongoing and regular government and industry consultation forum

Collaboration is vital for the successful execution of government contracts; treating subcontractors as valued partners rather than mere service providers creates an environment of trust and collaboration.

When subcontractors are offered fair terms and recognised as essential contributors, it enhances their motivation, commitment, and dedication to delivering quality work.

This, in turn, leads to improved project outcomes and greater overall project success.

Industry recommends establishing a Federal Government subcommittee to discuss, finalise and implement the recommendations raised in this submission.

It is recommended that this government and industry subcommittee meets twice per year.

The industry also offers to provide case studies and real-life examples to the Government based on the progress of the newly enacted UCT legislation and the experience of the construction sector as the new provisions come into effect.

Participating industry representatives

This submission was prepared in close collaboration and agreement between the following industry organisations:

national electrical and communications association
www.neca.asn.au

Specialist Contractors Association
www.specialistcontractors.asn.au

ETU Electrical Trades Union
www.etu.org.au

RACCA AUSTRALIA
www.racca.asn.au

AMCA AUSTRALIA
www.amca.com.au

MASTER PLUMBERS AUSTRALIA AND NEW ZEALAND
www.masterplumbersanz.com

National Fire Industry Association Australia
www.nfia.com.au

Surveyors Australia
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