Improvements to the Minimum Financial Requirements for licensing in the building and construction industry

Introducing the new framework

Background

High profile insolvencies and corporate collapses continue to occur in Queensland's building and construction industry with wide-ranging financial and social impacts.

Queensland's building regulator, the Queensland Building and Construction Commission (QBCC), has historically required that financial information be provided to them with any application for a new licence or licence renewal. This requirement helps the QBCC identify applicants or licensees who may not be operating a financially sustainable business and take appropriate action to minimise the potential impacts.

Since 2014 however, the QBCC's access to a licensee's financial information, and therefore, its ability to monitor companies potentially at-risk of insolvency or collapse, has been reduced. This is because the current Minimum Financial Requirements (MFR) Policy removed the requirement for a licensee to lodge financial information annually. This means that regular, detailed information about a licensee's financial situation is no longer being provided to the QBCC.

Through the Queensland Building Plan, the Queensland Government committed to creating new laws that strengthen the MFR for licensing. The *Building Industry Fairness (Security of Payment) Act 2017* allows for the introduction of an MFR regulation which will be a step towards making the provisions more transparent.

The changes to the MFR are a result of consultation with industry on 18 improvement proposals outlined in the discussion paper *'The proposed improvements to the Minimum Financial Requirements for licensing in the building and construction industry'* which received over 50 responses.

Many of the key reform proposals were supported, including: increased financial reporting, particularly for larger, higher risk entities; and restrictions for accountants making changes to MFR reports. Respondents were also supportive of greater scrutiny around the use of forms of assurance, such as Deeds of Covenant and Assurance, and related entity loans to meet minimum asset thresholds.

Based on the consultation results, the Queensland Government is progressing a number of key reforms.

The new framework

The key reforms aim to:

- strengthen reporting requirements
- provide clarity about what can be included when calculating a licensee's assets and revenue
- improve data quality and availability for the QBCC.

This will ultimately enable the QBCC to more effectively detect and minimise the impact of potential insolvencies and corporate collapses. The changes to the framework are set out below.

Strengthening reporting requirements

- Licensees will need to provide financial information to the QBCC each year (as was the case prior to 2014). This is a key measure to provide QBCC with greater visibility over financial reporting.
- Annual reporting will leverage existing reporting requirements to make it as easy as possible for licensees to comply. For example, licensees who already provide the QBCC copies of their audited ASIC reports can continue to do so.
- Categories SC1 and SC2 (those with lower revenue):
  - Will continue to self-certify that they are meeting the requirements. The revenue threshold for self-certification categories will also be raised from $600,000 to $800,000.
  - Self-certifying licensees will also need to report their Current Ratio of assets to liabilities, to provide more complete financial information to the QBCC. A new online reporting tool will make it easy for licensees to comply.
- Categories SC1 to category 3:
  - The current requirement to report decreases in Net Tangible Assets of 30 per cent or more will continue.

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- Categories 4 to 7 (those with higher revenue):
  - Licensees will need to report decreases in Net Tangible Assets greater than 20 per cent. More sensitive reporting triggers for high risk licensees will let the QBCC know earlier of changes in a licensee's financial position.
  - Licensees must provide more detailed financial information in the form of a 'balanced scorecard'. A more holistic reporting approach will better equip the QBCC to detect potential insolvencies.

Providing clarity about calculating a licensee's assets and revenue

- Personal recreational vehicles, such as dirt bikes and golf carts, can no longer be used to meet minimum asset thresholds. These types of vehicles have limited liquidity and their value is not easy to determine and so should not be used to increase a licensee's asset position.
- When money held in a Project Bank Account can be included as a licensee's asset or revenue will be clarified:
  - Both head contractors and subcontractors will be able to include any amount in the general trust account they have a beneficial interest in as an asset.
  - Subcontractors will also be able to include retention amounts and disputed funds that are related to them.

Improving data quality and availability for the QBCC

- The QBCC will be able to seek advice from a suitably qualified, independent accountant to substantiate information in an MFR report.
- Licensees who provide incorrect information may need to meet the costs of the independent assessment.
- Any 'material changes' made by an accountant to an MFR report will need to be clearly identified and supported by updated financial information. This will improve transparency and encourage accountants to improve their practices when preparing MFR reports.
- If a licensee is relying on a Deed of Covenant and Assurance, they will need to provide the QBCC with detailed financial information about the covenantor to show they can honour their agreement.
- Similar requirements will be introduced for related entity loans so the QBCC can assess whether these loans will be collectable when due for payment.

How are the changes being implemented?

The reforms are being advanced in phases to expedite financial transparency and give industry time to adjust.

Phase 1 commenced on 1 January 2019 and:

- re-introduces mandatory annual reporting
- requires larger, higher risk licensees to report decreases in Net Tangible Assets of 20 per cent or more
- provides clarity about calculating a licensee's assets, that is, the exclusion of recreational vehicles and when to include Project Bank Account funds.

Phase 2 will implement the remaining reforms to raise the standard of reporting, particularly for larger, high risk licensees. A later commencement for Phase 2 on 1 April 2019 will allow industry to get ready for the changes. This phase will also provide stronger enforcement provisions under the *Queensland Building and Construction Commission Act 1991* (the Act).

What happens if a licensee doesn't meet the requirements?

Penalties for not complying with the MFR have been included in the regulation, for example, if a licensee fails to provide financial information annually.

Existing penalties will continue to apply. Under the Act, the QBCC can place conditions on a licence, or take steps to suspend or cancel the licence. Penalties also apply for providing false or misleading information or refusing to supply financial information at the QBCC's request.

The enforcement provisions under the Act are intended to be further strengthened as part of Phase 2, including executive officer liability and escalating penalties, to help ensure all parties involved in running a licensed company are motivated to meet the new MFR.

More information

For more information, please visit the Department of Housing and Public Works' website www.hpw.qld.gov.au or email Building Legislation and Policy at mfr@hpw.qld.gov.au.