



Report 4: 2022-23 | 11 August 2022

**PERFORMANCE AUDIT**

# Payments to Subcontractors Working on State Government Construction Projects



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Western Australia**

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***The Office of the Auditor General acknowledges the traditional custodians throughout Western Australia and their continuing connection to the land, waters and community. We pay our respects to all members of the Aboriginal communities and their cultures, and to Elders both past and present.***

## WESTERN AUSTRALIAN AUDITOR GENERAL'S REPORT

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### **Payments to Subcontractors Working on State Government Construction Projects**

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11 August 2022

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**THE PRESIDENT  
LEGISLATIVE COUNCIL**

**THE SPEAKER  
LEGISLATIVE ASSEMBLY**

**PAYMENTS TO SUBCONTRACTORS WORKING ON STATE GOVERNMENT  
CONSTRUCTION PROJECTS**

This report has been prepared for submission to Parliament under the provisions of section 25 of the *Auditor General Act 2006*.

Performance audits are an integral part of my Office's overall program of audit and assurance for Parliament. They seek to provide Parliament and the people of WA with assessments of the effectiveness and efficiency of public sector programs and activities, and identify opportunities for improved performance.

This audit assessed if State government entities have effective controls in place to ensure timely payments to subcontractors working on government construction projects.

I wish to acknowledge the entities' staff for their cooperation with this audit.

A handwritten signature in black ink, appearing to be 'C Spencer'.

CAROLINE SPENCER  
AUDITOR GENERAL  
11 August 2022

# Contents

Auditor General's overview.....	5
Executive summary .....	6
Introduction .....	6
Background.....	6
Conclusion .....	8
Findings .....	10
PBA payment controls are not effectively implemented .....	10
Effective controls are not in place to identify and act on poor payment practices.....	12
Recommendations.....	15
Response from Department of Finance .....	18
Response from Main Roads WA .....	18
Response from Western Power.....	19
Audit focus and scope .....	20

## Auditor General's overview

The building and construction industry is vital to the Western Australian economy. Thousands of people are employed in the industry and many more enjoy the benefits of the infrastructure it creates.

The State Government invests billions of dollars a year in building and construction projects. Typically, the delivery of these projects is outsourced to private head contractors, who in turn hire subcontractors to perform specific works. These subcontractors vary from sizable or small businesses, to individuals. The State is not a party to the contractual arrangements between head contractors and their subcontractors, but its efforts to improve the security of payments recognises it has some obligation to subcontractors working on State projects.



Issues around subcontractor vulnerability to non-payment by head contractors have been well publicised and the subject of various reviews, recommendations, and reforms. Of note was the State Government's 2019 decision to require project bank accounts (PBAs) on government construction projects. When subcontractors are not paid, they and those that work for them can experience financial distress and may also be less willing to work on State projects. A solution is not simple, especially as contractual reasons are sometimes behind subcontractor payment issues.

Our audit looked at the effectiveness of three State government entities' controls to protect subcontractor payments, including their administration of PBAs in accordance with government requirements, recognising the use of PBAs is still in the early years of implementation. We did not seek to identify specific instances of subcontractor non-payment but rather aimed to provide transparency into how these entities have implemented PBAs at a systemic level, including how they become aware of issues and what they do to limit them happening.

While the three audited entities used PBAs, we found their administration of the accounts was done without due scepticism as there was little or no checking of the information provided by head contractors. Concerningly, incomplete and erroneous head contractor statutory declarations were accepted without follow up. Making a false statutory declaration is a serious offence and may be a warning sign about other compliance problems that entities must promptly address.

Entities consistently told us they rely on complaints to alert them to instances of head contractors not paying their subcontractors. However, not all entities provided subcontractors with clear and discrete ways to raise complaints, and subcontractors told us they fear reprisal and loss of work if they complain. Entities that rely on complaints without other complementary controls will not know the extent of subcontractor payment issues or be able to effectively address them.

Every State entity must ensure they comply with PBA policy requirements, but sole reliance on this dispersed model of accountability will not ensure government achieves its objective to better protect subcontractor payments. More central entity whole-of-government leadership is required. This sits with the Department of Finance given its whole of government procurement leadership responsibility and significant experience delivering billions of dollars of construction projects.

The recommendations in this report aim to strengthen entities' controls and thus the effectiveness of PBA reforms. They do not seek to encroach on the State's commercial arrangements to deliver building and constructions projects or intervene in head contractor and subcontractor commercial relationships. I am grateful for the insights shared with us by subcontractors working on government projects who completed our survey, especially around early warning signs that they may experience payment difficulties (page 13).

# Executive summary

## Introduction

The objective of this audit was to assess if State government entities (entities) have effective controls in place to ensure timely payments to subcontractors working on government construction projects. We focussed on the Department of Finance (Finance), Main Roads Western Australia (Main Roads) and the Electricity Networks Corporation (trading as Western Power).

In 2016, we completed two audits of payments to subcontractors: *Payment of Construction Subcontractors - Perth Children's Hospital*<sup>1</sup> and *Assessment of Progress to Improve Payment Security for Government Construction Subcontractors*<sup>2</sup>. This audit builds on these previous audits, which were undertaken in response to concerns raised by Parliament.

Finance has two roles in relation to this aspect of public administration. It enters into construction contracts that engage subcontractors, and it is the central entity responsible for the WA public sector's procurement framework. This audit makes findings and recommendations in relation to these roles separately.

## Background

Every year State government entities enter into significant contracts with private head contractors to deliver a wide range of government construction and infrastructure projects. In 2021-22, the State Government's asset investment program for the total public sector was \$7 billion.<sup>3</sup>

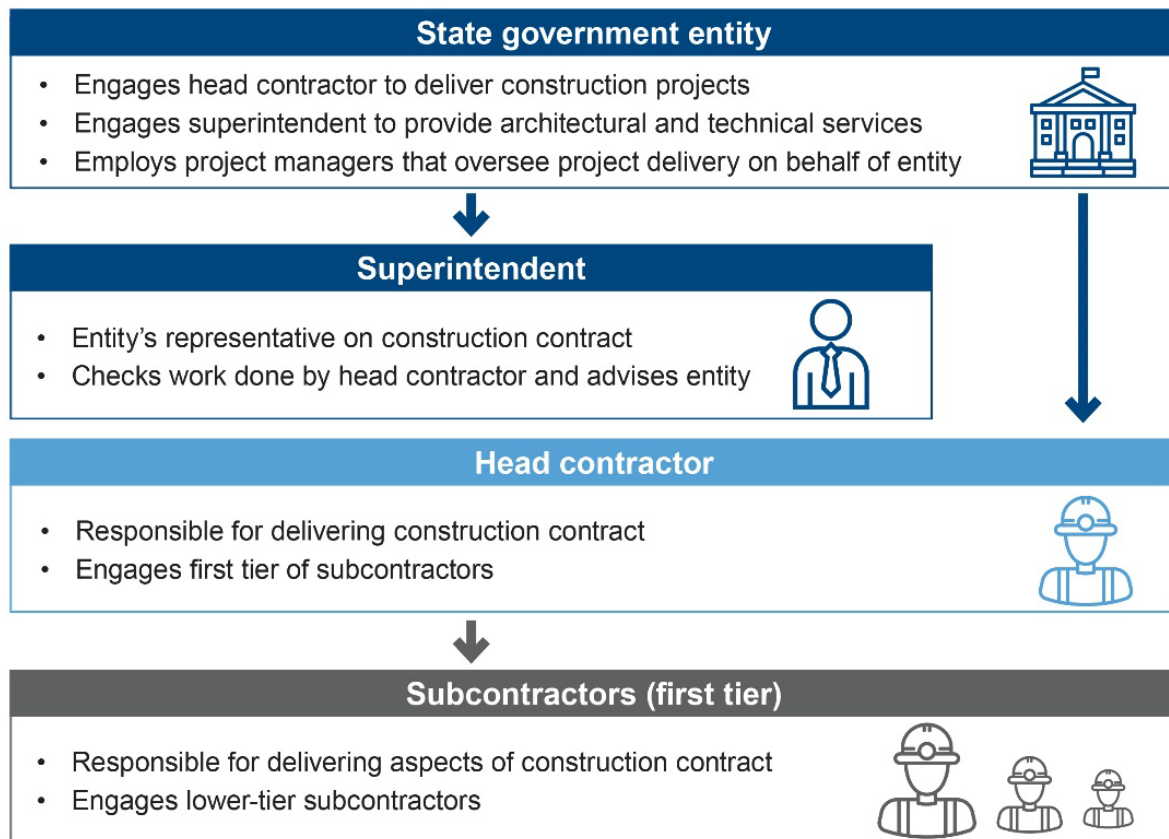
Head contractors often hire subcontractors to help them deliver projects (Figure 1). These 'first tier' subcontractors may then hire their own subcontractors creating a tiered subcontracting model. We refer to first tier subcontractors as 'subcontractors' in this report except when specifically distinguishing from lower tier subcontractors.

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<sup>1</sup> Office of the Auditor General, [Payment of Construction Subcontractors – Perth Children's Hospital](#), OAG, Perth, 2016.

<sup>2</sup> Office of the Auditor General, [Assessment of Progress to Improve Payment Security for Government Construction Subcontractors](#), OAG, Perth, 2016.

<sup>3</sup> Government of Western Australia, [Western Australia State Budget 2022-23, Budget Paper No.3, Economic and Fiscal Outlook](#), Government of Western Australia, Perth, 2022, p. 4.



Source: OAG

**Figure 1: Some of the parties involved in the delivery of government construction projects**

Subcontractors are essential to the State Government's delivery of projects. Their viability and willingness to work on projects relies on the timely cascading of payments from the head contractor down the subcontracting tiers.

Head contractor insolvency is a key risk to subcontractors being paid. Between 2020 and 2022 several head contractors working in Western Australia (WA) entered administration. Some of these had State Government construction contracts, including with the entities we audited. To protect subcontractors, entities need to take reasonable steps to safeguard payments to them.

Since 1 July 2019, State entities have been required to ensure head contractors, working on projects that exceed \$1.5 million, open a project bank account (PBA) with a financial institution.<sup>4</sup> Finance has been required to have PBAs since 30 September 2016.<sup>5</sup> PBAs were introduced in response to the 2018 Fiocco report on *Security of Payment Reform in the WA Building and Construction Industry*.<sup>6</sup>

PBAs were designed to protect payments to first tier subcontractors and in so doing offer some payment protection for lower tiers. Finance and the Department of the Premier and Cabinet (DPC) were both involved in the initial implementation of PBAs. DPC chaired the

<sup>4</sup> P Papalia (Minister for Small Business), B Johnston (Minister for Commerce and Industrial Relations), B Wyatt (Minister for Finance), [McGowan Government to expand Project Bank Accounts in 2019](#), Government of Western Australia, 4 December 2018.

<sup>5</sup> S L'Estrange (Minister for Finance), [WA leads the way with project bank accounts](#), Government of Western Australia, 30 September 2016.

<sup>6</sup> J Fiocco, [Final Report to the Minister for Commerce: Security of Payment Reform in the WA Building and Construction Industry](#), Department of Mines, Industry Regulation and Safety, Perth, 2018.

PBA Implementation Working Group in its role to promote matters that require Cabinet approval. Finance provided advice to the working group about its experience trialling PBAs consistent with its lead entity role for State government procurement.

Entities have some discretion in how they implement PBAs. Entities we audited had established PBAs with two sub-accounts. Each sub-account has a different purpose and controls:

- general sub-account – money is paid into it by the entity and the entity approves release of progress payments to the head contractor and first tier subcontractors, when requested by the head contractor
- retention sub-account – retention money owed to subcontractors is paid into it by the entity when requested by the head contractor. The head contractor approves the release of payments to first tier subcontractors or itself when it is contractually obliged or decides to do so. Retention funds are a percentage of money owed to subcontractors that is held until the head contractor is satisfied that subcontractor work is completed without defects. The retention exists to protect the head contractor.

Head contractors are required to provide entities with statutory declarations but are not obliged to provide any supporting information. The declarations are a key control that entities rely on to confirm the accuracy of information about payments to subcontractors and when releasing funds to the PBA.

Since 1 June 2021, the requirement to establish a PBA has been included in Rule F9 of the Procurement Rules (Rules) issued under the *Procurement Act 2020* (the Act). Responsibility for compliance with the Rules rests with each State government entity's Accountable Authority. Entities exempt from the Act, such as Government Trading Enterprises, like Western Power, are not required to implement PBAs but can choose to do so.

Section 12 of the Act requires Finance, as the lead entity, to provide whole of government leadership in the procurement of goods, services or works by entities. Further, section 14 requires the CEO of Finance to establish an investigation and audit program to maintain the integrity of, and public confidence in, the State's procurement activities.

The Government continues to work on reforms to strengthen subcontractor payment protections. In particular, development of regulations to support the *Building and Construction Industry (Security of Payment) Act 2021*. These regulations intend to expand retention account protections from February 2023 to cover more subcontractors (it will apply to some private construction projects and will cascade to lower tiers of subcontractors) and provide subcontractors a right to review accounting records of retention accounts, for which they are beneficiaries.<sup>7</sup>

## Conclusion

State government entities have not yet implemented effective controls to protect payments to subcontractors who work on their construction projects. While this is a relatively new policy area, control weaknesses leave Government policy objectives vulnerable to not being achieved and subcontractors exposed to not being paid.

All three audited entities have implemented project banks accounts (PBAs). These are a key payment protection for first tier subcontractors, but their effectiveness is eroded by weak government entity controls. Before paying money into the PBA, entities do not do enough to check information provided by head contractors is accurate. Two entities had poorly

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<sup>7</sup> Department of Mines, Industry Regulation and Safety, [Action Plan for Reform: Better Payment Protections for Contractors in the WA Building and Construction Industry](#), DMIRS, Perth, 2021.

implemented statutory declaration requirements despite their importance as a payment control. These weaknesses leave PBA funds susceptible to inappropriate release.

Entities' other controls for protecting payments are also only partly effective. Not all entities had effective complaint mechanisms for subcontractors to raise payment issues or proactively checked head contractor payment performance through means such as spot checks. Practical mechanisms to address and deter head contractor poor payment performance were also lacking. As a result, entities may not know when payment issues exist or have practical ways to address them.

There is currently no whole of government guidance and leadership on PBAs. This may diminish the effectiveness of stated Government policy objectives to protect subcontractors working on State Government construction projects. The Department of Finance's role to provide whole of government leadership in procurement should reasonably include this proportional to its other responsibilities.

# Findings

## PBA payment controls are not effectively implemented

### Entities have implemented PBAs, but weaknesses leave subcontractors exposed

#### *PBAs have been implemented*

Finance and Main Roads are required by the Rules to use PBAs and have done so.

Finance had implemented PBAs on all eligible contracts awarded since 1 July 2019 and Main Roads on all contracts advertised after that date. Despite being exempt from the requirement to implement PBAs, Western Power had trialled PBAs on two contracts and told us it may apply PBAs in the future, following a review of its trial. Subcontractors currently working on Western Power construction projects have limited coverage from PBA payment protections.

	Finance	Main Roads	Western Power
<b>PBAs required by State directive<sup>8</sup></b>	✓	✓	✓
<b>PBAs required by Procurement Rules</b>	✓	✓	✗*
<b>Date PBAs required from</b>	30 September 2016 <sup>9</sup>	1 July 2019	1 July 2019
<b>Testing showed PBAs implemented on</b>	Contracts awarded from 1 July 2019	Contracts advertised from 1 July 2019	2 trial projects
<b>Number of eligible contracts at time of testing</b>	112	57	34*

Source: OAG

\* Western Power is not required to implement PBAs because it is exempt from the Procurement Act 2020.

**Table 1: PBA coverage at audited entities**

#### *Entities do not do enough to verify the accuracy of information in payment documents or check the proper form of statutory declarations they receive from head contractors*

None of the entities routinely verify information provided by head contractors. Entities rely on this information to make payments through PBAs. None checked that payment instructions reflected what subcontractors were owed (see point 3 in Figure 2). Entities don't know if payment amounts are right and could do more to improve their visibility of subcontractor payment claims.

Two entities had weak statutory declaration processes:

- We examined a statutory declaration submitted to Western Power. We found it did not include a declaration from the head contractor as to the truth and accuracy of the

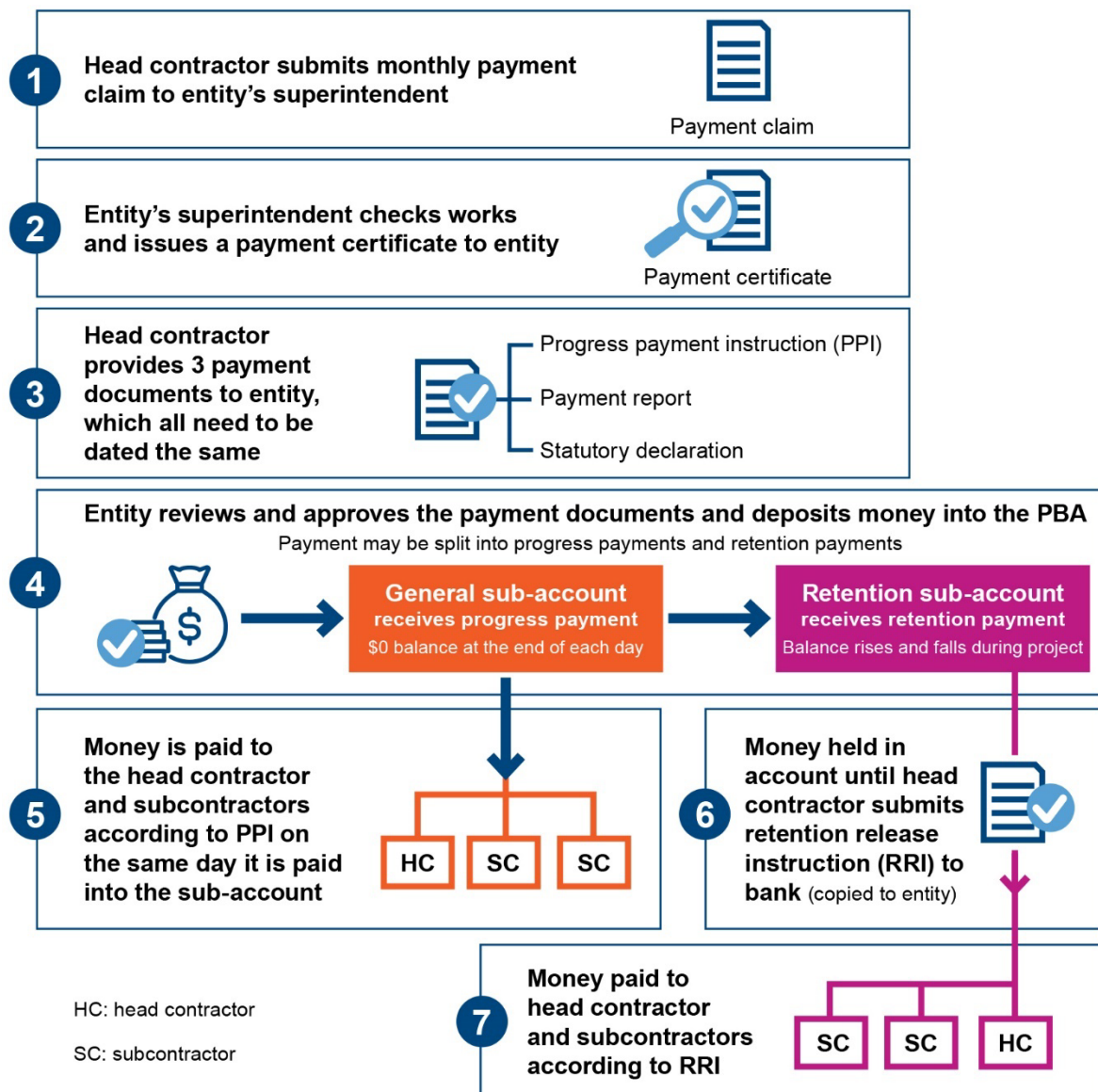
<sup>8</sup> P Papalia (Minister for Small Business), B Johnston (Minister for Commerce and Industrial Relations), B Wyatt (Minister for Finance), [McGowan Government to expand Project Bank Accounts in 2019](#), Government of Western Australia, 4 December 2018.

<sup>9</sup> S L'Estrange (Minister for Finance), [WA leads the way with project bank accounts](#), Government of Western Australia, 30 September 2016.

information in the PBA payment documents. This means Western Power lacks commitment from the head contractor that the information provided is correct.

- Main Roads did not effectively implement its statutory declaration requirements. We examined 23 and found issues in eight including unsigned forms or forms signed before the intended payment date (contrary to Main Road's own guidance). By accepting incorrect or incomplete statutory declarations, Main Roads reduces the effectiveness of this important control.

While we identified no reason to believe any issues we sighted were intentional, statutory declarations are a legal document and making false statements is a crime under WA's Criminal Code. Contractors could be excluded from government contracts if they are found to have made false statements.



Source: OAG

**Figure 2: Project bank account payment process**

PBA documents require head contractors to provide detailed information about the movement of retention funds. We found this information was not always provided or accurate, and none of the entities routinely checked or used it. We compared the information

provided by head contractors against PBA statements for three Finance and two Main Roads projects. For two Finance projects, we found the head contractor information overstated the retention account balance, by a third in one case.<sup>10</sup> Entities could use the information to identify discrepancies and potential payment issues, despite them not approving the release of retention sub-account funds.

	Finance	Main Roads	Western Power
<b>No. of retention accounts OAG checked</b>	3	2	0*
<b>No. with correct balance</b>	1	2	-
<b>No. with less funds than reported</b>	2	0	-

Source: OAG

\* No funds had been released from retention accounts on Western Power contracts at the time of our testing.

**Table 2: Results of OAG reconciliation of a sample of retention sub-account balances**

We note the Government's intent to introduce an expanded retention trust scheme from February 2023 through regulations under the *Building and Construction Industry (Security of Payment) Act 2021*. The trust scheme intends to cascade down to lower tiers of subcontractors and provide improved transparency through a right to access records of retention accounts, for which they are beneficiaries.<sup>11</sup>

## There is limited guidance on PBAs and no whole of government leadership

There is no clear guidance on when PBAs are required. The State Government has not developed definitive guidance, despite its 2018 announcement stating it would<sup>12</sup>, nor do the Rules provide clarity. The entities we audited had developed their own understandings. For example, Main Roads chose not to require PBAs for extensions of contracts initially awarded before 1 July 2019 whereas other entities may have chosen differently. In the absence of clear guidance, entities may not know when to implement a PBA and subcontractors may not know when they should expect PBA protection.

No central entity currently monitors whether PBAs are implemented well. Doing so would be consistent with Finance's responsibilities to provide whole of government leadership and audit compliance of State entities with policies set under the *Procurement Act 2020*. While each entity's Accountable Authority is responsible for compliance, central entity leadership would help support the effectiveness of Government policy objectives to protect subcontractor payments through the use of PBAs.

## Effective controls are not in place to identify and act on poor payment practices

### Entities do not do enough to identify subcontractor payment issues

All audited entities told us they rely on complaints from subcontractors to identify and understand the extent of payment problems. Complaints are valuable but cannot identify all

<sup>10</sup> This fund had a reported balance of \$154,727, but an actual balance of \$106,965 (\$47,761 less).

<sup>11</sup> Department of Mines, Industry Regulation and Safety, [Action Plan for Reform: Better Payment Protections for Contractors in the WA Building and Construction Industry](#), DMIRS, Perth, 2021.

<sup>12</sup> P Papalia (Minister for Small Business), B Johnston (Minister for Commerce and Industrial Relations), B Wyatt (Minister for Finance), [McGowan Government to expand Project Bank Accounts in 2019](#), Government of Western Australia, 4 December 2018.

issues, as subcontractors simply may not report them. In responding to our online survey, subcontractors told us they were reluctant to raise complaints as they feared they would not win future work from the head contractor. Without other mechanisms, such as spot checks, entities may not know when issues arise.

Not all entities have effective processes to receive complaints. For example, Main Roads' website only refers subcontractors to external complaint options and only Finance has a detailed process for investigation with clear escalation thresholds. Entities may miss information about the extent of subcontractor payment concerns if they do not engage with complaints.

None of the entities had fully effective processes to identify non-payment issues. We found:

- Only Finance proactively checked that subcontractors were paid. It has a program of spot checks but had not fully implemented it. We sampled 10 of Finance's contracts and found only 16 of the required 27 spot checks were done and only one contract had as many checks as required. Despite this, spot checks have led to more than one-third of the non-payment issues identified in Finance's complaints register indicating that, when undertaken, they are an important way to identify payments problems. Finance told us it is making further changes to its spot check processes to respond to market conditions.
- Main Roads told us its superintendents have asked subcontractors about payment issues, but it does not have a formal requirement for them to do so and could not provide evidence of the checks they had done.
- Western Power told us it does not check if subcontractors are paid.

In responding to our online survey, subcontractors told us there are often early warning signs of payment issues (Case study 1). By not proactively engaging with subcontractors, entities are missing opportunities to identify payment issues.

### **Case study 1: Subcontractors flag early warning signs of payment issues**

As part of this audit, we surveyed subcontractors working on government construction projects. Of the 33 respondents, 22 said they had experienced payment issues on government projects, most late and reduced payments.

Subcontractors provided the following examples of early warning signs that head contractors might not pay them correctly:

- lack of communication from the head contractor
- poor project management and blow-out of timelines
- high head contractor staff turnover
- increased queries on submitted invoices
- trading terms in a contract being extended.

All entities require head contractor performance to be assessed. However, these assessments were not always done or used to identify subcontractor payment issues. At the time of our audit, Western Power did not use its assessments to identify payment issues. We have been advised they have started to do so and are making broader improvements to their contract management processes. Finance and Main Roads' assessments do consider payment issues but too few had been completed. For the projects we sampled, we found

they had only completed 52% and 5% respectively of the assessments required by their guidelines. Entities are missing these formal opportunities to proactively identify non or late payment early warning signs.

### Existing deterrents are not always practicable

Project contracts include two main ways for entities to act on payment issues, but they may not always be appropriate or practical to use. Entities can remove head contractors from the project or withhold money from head contractors and pay subcontractors directly. Entities should have a range of non-contractual options available to address subcontractor payment concerns.

Finance and Main Roads do not solely rely on contractual provisions. We saw instances where they had directly contacted head contractors, assessed their performance, cancelled prequalification status or not awarded them further contracts. Timely actions such as these can help resolve issues and avoid the need for more serious action.

Since July 2017, Finance has had a supplier demerit scheme to manage head contractors with very poor performance. Between July 2017 and September 2021, Finance used the scheme to issue infractions to two head contractors for unsatisfactory payment of subcontractors, but neither needed to be escalated to a demerit. Finance told us it has used the scheme more recently to issue demerits on two occasions.

Reforms under the *Building and Construction Industry (Security of Payment) Act 2021* are intended to provide higher standards of professional and ethical behaviour in the construction industry. For example, from 1 February 2023, the Building Services Board will be able to exclude people with a history of financial failure from the registered building contractor market and building contractors may be subject to disciplinary action or exclusion from registration for not paying debts ordered by courts or adjudication.<sup>13</sup>

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<sup>13</sup> Department of Mines, Industry Regulation and Safety, [Action Plan for Reform: Better Payment Protections for Contractors in the WA Building and Construction Industry](#), DMIRS, Perth, 2021.

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## Recommendations

### 1. Finance should:

- a. better implement its risk-based approach to identify non-payment issues and verify information in PBA payment documents, especially through subcontractor non-payment spot checks and direct communication with subcontractors
- b. reassess what retention sub-account information it requires and how this will be used
- c. continue to implement practical mechanisms to act on poor payment practices by head contractors that include clear thresholds for when they will be applied
- d. provide whole of government leadership and monitor if PBAs are implemented well as part of its central entity role for the State's procurement framework, and proportional to its other responsibilities in this area.

**Implementation timeframe:** by December 2023

#### **Finance response:**

- a. Accepted. Finance will continue to strengthen its existing mechanisms to support the verification of payments to subcontractors through PBAs.
- b. Accepted.
- c. Accepted. Finance supports the intent of this recommendation. Finance will continue to examine ways to strengthen its existing mechanisms to deals with poor payment practices by head contractors, while maintaining a degree of flexibility.
- d. Accepted. Finance will use its procurement functional leadership role to audit establishment of PBAs in relevant projects, as defined in the WA Procurement Rules. This will be delivered through the scheduling of a thematic audit or audit(s) on a risk-based approach as required.

### 2. Main Roads should:

- a. implement controls to verify information in PBA payment documents, especially statutory declarations
- b. reassess what retention sub-account information it requires and how this will be used
- c. apply a risk-based approach to identify non-payment issues, such as through spot checks and direct communication with subcontractors
- d. implement practical mechanisms to act on poor payment practices by head contractors that include clear thresholds for when they will be applied.
- e. implement processes to receive and assess complaints about subcontractor non-payment, including anonymous options.

**Implementation timeframe:** 31 March 2023

**Main Roads response:**

- a. Agreed, Main Roads will strengthen its processes in relation to statutory declarations.
- b. Agreed, Main Roads will reassess the purpose and how retention sub-accounts are used under PBA processes.
- c. Agreed, Main Roads will continue to improve its processes in relation to applying a risk-based approach to spot checks and direct communication with subcontractors.
- d. Agreed, Main Roads will continue to consider improvements to practical mechanisms and thresholds to act on poor payment practices by head contractors.
- e. Agreed, Main Roads will strengthen its complaints process and options for subcontractors to raise concerns anonymously.

**3. Western Power should:**

- a. implement controls to verify information in PBA payment documents, especially statutory declarations
- b. reassess what retention sub-account information it requires and how this will be used
- c. apply a risk-based approach to identify non-payment issues, such as through spot checks and direct communication with subcontractors
- d. implement practical mechanisms to act on poor payment practices by head contractors that include clear thresholds for when they will be applied.

**Implementation timeframe:**

a-b by 31 July 2023

c-d over the next six months

**Western Power response:**

- a. Western Power has included in our statutory declaration template a declaration by the head contractor as to the truth and accuracy of the information in the PBA documents.
- b. Western Power will conduct an internal workshop to ascertain what information it requires to determine payments to subcontractors are made timely and correctly, and outline what actions we will take if discrepancies are found. The result of the workshop will be incorporated into our PBA processes and communicated to head contractors engaged on Western Power's qualifying construction projects.
- c. Western Power has enhanced the consistency of application of subcontractor qualitative criteria in tender events that includes an assessment of a potential supplier's risk mitigation strategies around subcontractor non-payments. We have also expanded our monthly contractor meeting agenda to include discussions about timely submission of payment claims and their accuracy, the accuracy of supporting information, and any other relevant details of the management of subcontractors. Further, we have improved information available on our public

facing website to make it clear how subcontractors can make a complaint directly to Western Power.

- d. Western Power will implement a recently developed Contractor Lifecycle Management Framework that overhauls our policies and procedures for managing contracts. The new framework will enhance Western Power's contractor management by establishing:
- A team dedicated to supplier performance management
  - New supplier performance management processes that strengthen KPI reporting, improve supplier performance scoring and allow non-performance to be considered in future tendering
  - Spot checks of payments to subcontractors, which will be included in assurance activities.

## Response from Department of Finance

The Department of Finance (Finance) welcomes the Auditor General's report on payments to subcontractors working on government construction projects and is pleased the performance audit acknowledges some of the leading practices Finance has implemented to improve security of payment, including its 'spot check' mechanism and supplier demerit scheme framework.

Finance is acutely aware of the importance of fair and prompt payment for small and local businesses, and continues to support sector-wide reforms in the building and construction industry, which are being led by the Department of Mines, Industry Regulation and Safety (DMIRS). As a result of its robust internal frameworks for the prequalification, assessment and management of head contractors, Finance believes the subcontractors working on its construction projects enjoy some of the highest levels of payment protection currently available, despite the issues raised by the Office of the Auditor General (OAG).

Finance appreciates the building and construction industry (both locally and abroad) is characterised by low barriers to entry, a heavy reliance on cashflow and disproportionately high rates of insolvency. For these reasons, Finance will continue to improve and refine its internal practices and procedures relating to security of payment, and offer support to other agencies, where possible.

While some of the issues identified by the OAG will be addressed through planned improvements within Finance and broader statutory reforms across industry, it is important to recognise that non-payment issues can arise for a variety of reasons, including but not limited to contractual disputes between subcontractors and head contractors. As Finance is not privy to the private commercial relationships that exist at all levels of a construction project's supply chain, it is not always best placed to intervene and resolve such matters.

It is important to note, a number of the issues raised by the OAG, including its recommendations regarding statutory declarations, were the subject of extensive consultation and advice during the development of the current project bank account (PBA) model. This model, and the supporting mechanisms implemented by Finance on its construction projects to improve security of payment were ultimately decided as a matter of government policy, having regard to the pros and cons of each possible approach.

## Response from Main Roads WA

Overall, Main Roads Western Australia accepts the findings and will continue to strengthen our controls over payment practices, in order to ensure controls over payments to subcontractors by head contractors continue to be effective.

The OAG audit report fails to recognise the improvements that have been made by Government in introducing Project Bank Accounts across all works contracts greater than \$1.5m, which is now driving an important change in the thinking of head contractors and their relationships with Government entities and subcontractors around timely and accurate payments through the supply chain. This reform is a very important effective control and should be acknowledged.

Main Roads is pleased that there were no specific findings of non-payment to subcontractors identified through the various contracts that were audited, which shows that controls are in place and working effectively.

In addition, Main Roads have established over a long period of time (over 20 years) important stakeholder relationships with the various civil construction industry bodies and meets

quarterly to improve practice in delivery of works in road and rail. This mature relationship helps self-regulate industry to be better across several areas in project and contract delivery. Improvements to payment practices are part of these discussions and hence the audit did not identify systemic issues in the contracts audited.

## **Response from Western Power**

I would like to thank the Office of the Auditor General for the professional engagement of its personnel with Western Power's staff during the Performance Audit and in the preparation of the report. Although Western Power acknowledges that it is not required to implement Project Bank Accounts (PBA), we remain committed to applying PBA on qualifying contracts as outlined in our Management Letter dated 13 December 2021. Western Power supports the Government objective of ensuring accurate and timely payments are made to subcontractors and we will further strengthen our controls to achieve this. We appreciate the opportunity to participate in the audit and receive improvement opportunities.

## Audit focus and scope

The objective of the audit was to assess if State government entities have effective controls in place to ensure timely payments to subcontractors working on government construction projects. The criteria were:

- Do entities have effective policies and processes to protect subcontractor payments and apply them consistently?
- Do entities monitor whether their policies and processes are effective and implement improvement opportunities where needed?

This audit was conducted between March 2021 and June 2022. We audited:

- the Department of Finance
- Main Roads Western Australia
- the Electricity Networks Corporation (trading as Western Power).

In undertaking the audit, we:

- reviewed policies, guidelines, complaints, templates, registers, contractor performance reports, risk assessments, meeting minutes and project documents
- examined entities' PBA documents, contractual provisions and monitoring processes (such as complaints and spot checks)
- tested a sample of PBAs and payments made on projects
- conducted preliminary work to establish if payments could be traced down through tiers of subcontractors
- interviewed staff from the three audited entities
- met with DPC to discuss their role in PBA implementation and ongoing oversight
- met with the Small Business Development Corporation, who has the authority to investigate complaints of non-payment and poor practice in the construction industry
- met with the Department of Mines, Industry Regulation and Safety to discuss reforms under the *Building and Construction Industry (Security of Payment) Act 2021*
- conducted an online survey from July to September 2021 to gather views and experiences on the payment process from subcontractors working on State government construction projects. We received 33 responses.

We did not interview head contractors or review their internal controls relating to payments to subcontractors.

This was an independent performance audit, conducted under Section 18 of the *Auditor General Act 2006*, in accordance with Australian Standard on Assurance Engagements ASAE 3500 *Performance Engagements*. We complied with the independence and other ethical requirements related to assurance engagements. Performance audits focus primarily on the effective management and operations of entity programs and activities. The approximate cost of undertaking the audit and reporting was \$510,000.

## Auditor General's 2022-23 reports

Number	Title	Date tabled
1	Opinion on Ministerial Notification – Wooroloo Bushfire Inquiry	18 July 2022
2	Financial Audit Results – Universities and TAFEs 2021	21 July 2022
3	Public Trustee's Administration of Trusts and Deceased Estates	10 August 2022

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