



The Cost of Constructing the Commonwealth Games Village

Industrial Relations and the Struggle to Build in Victoria
Supplementary Report

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In November 2006, the IPA released a report titled *Industrial Relations and the Struggle to Build in Victoria*. The report demonstrated the huge extra cost imposed on the State of Victoria as a consequence of the lawlessness in the construction sector. It was the first case study into the positive impact of the new construction ‘cop’—the Australian Building and Construction Commission (ABCC). The report conducted a detailed analysis of the blow-out in the costs of construction of the CityLink project compared with the Eastlink project that were directly attributable to the bad industrial relations practices that applied at CityLink. The cost differential was assessed at 11.8 per cent.

This short report is a follow-up to *Industrial Relations and the Struggle to Build in Victoria*. It reinforces and adds further weight to the findings of the 2006 report. This report also forms part of the IPA’s submission to the Wilcox Review into the ABCC.

The IPA’s conclusion is that Victoria (as a case study) needs the retention of the ABCC because it has proven effective in ensuring improved lawful behaviour in the construction sector. It has also delivered substantial economic benefits to Victoria.

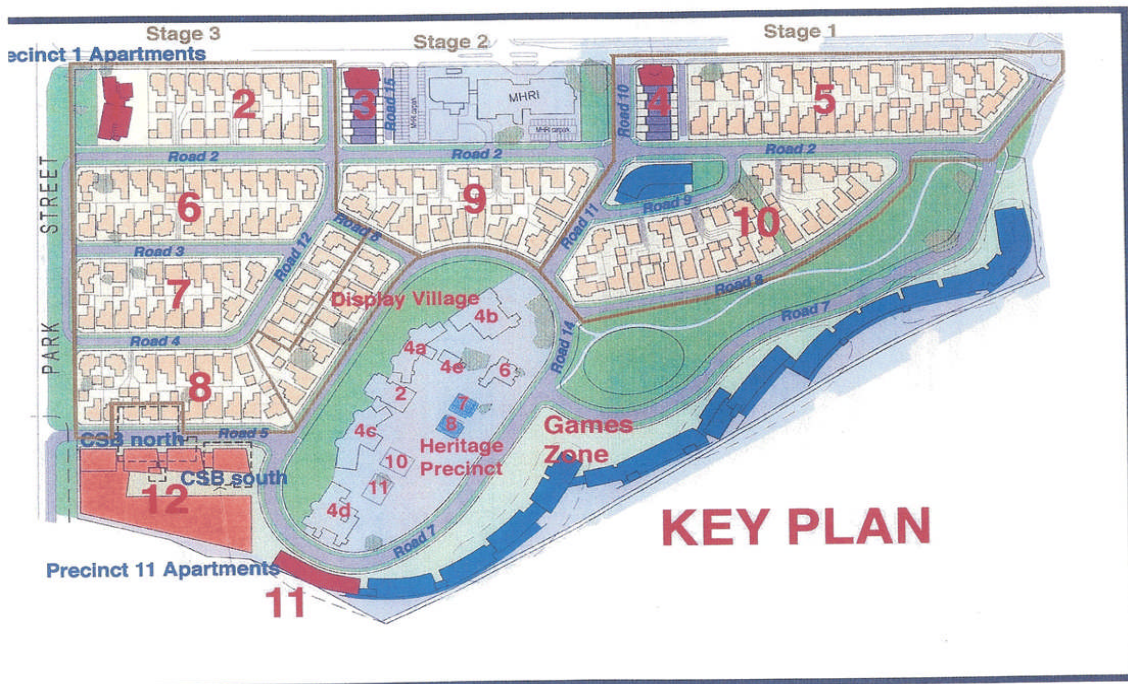
This analysis focuses on the cost of construction of the Commonwealth Games Village. Our 2006 report stated the following:

- The Commonwealth Games village was built with CFMEU workers and industrial agreements instead of using standard housing construction work arrangements which involve neither unions nor industrial relations agreements. The Games Village, consisting of 115 permanent and 115 temporary housing units, was essentially no different from a standard housing development that would occur in Victoria, except for the temporary security and other Games-related requirements. The 2002 budgeted cost for the project was \$144 million. The Government has not released comparative data but estimates indicate that the additional cost of the housing construction at the Games village was in the order of 25 to 30 per cent over and above normal housing costs. This is consistent with comparative estimates arising from the Cole Commission inquiry into the construction sector.

This report reveals that contractual arrangements put in place by the Government of Victoria inflated the cost of the Games Village construction by 34 per cent as a result of industrial arrangements with construction unions. In other words, if the Games Village had been built using normal housing contractors, the evidence indicates that the cost of the Games Village would have been 34 per cent less than the actual cost paid for by the taxpayers of Victoria. The extra cost was around \$50 million on the \$144 million project.

The Contractual Evidence

The Games Village construction consisted of two distinct contractual undertakings. There was the major sector of the Village itself and an additional sector called the Heritage Precinct (see map). The Heritage Precinct was required over and above the Village proper to accommodate more athletes and officials than had been originally planned.



Normal domestic housing was to be built to house the athletes in the Heritage Precinct. This housing was to be sold by the developer/builder after the Games and the developer was to retain the proceeds from the housing sale. The State of Victoria was to have access to the use of the housing accommodation during the Games at comparatively low cost.

The developer was a large Australian concern with construction activity in two markets: the domestic housing market and the commercial construction market.

- The domestic housing market constructs housing using what is called a ‘cottage industry’ process. That is, large numbers of self-employed carpenters, plumbers, brick layers and so on subcontract to builders and developers to build houses. The sector is large, well organized, does not have a union presence and does not operate under industrial agreements. It delivers quality - housing at affordable prices to Australians.
- The commercial construction sector builds anything more than two storeys in height, including apartments, commercial buildings and so on. The sector is controlled by construction unions and is governed by industrial agreements which specify how construction is to occur.

Because the developer operated in both sectors, it was well aware of the cost differential between the two, and was accustomed to pricing jobs differently.

To get the Games Village built, the Victorian Government entered a Memorandum of Understanding with construction unions that the village would be built using a union workforce with construction union industrial agreements and practices in place.

Up until recently, it has been difficult to secure hard evidence about the exact cost differential the Victorian Government was prepared to accept for using union arrangements to build the domestic housing when compared with standard cottage industry arrangements. That hard evidence is now available.

The IPA has obtained a copy of the Heritage Precinct contract between the Government and the developer under the Freedom of Information Act. The contract is complex but the analysis is as follows:

- a) The Victorian Government contracted with the developer and, in effect, lent the developer the full amount of the contracted price.
- b) Once the Commonwealth Games were finished, the builder was to sell the houses.
- c) The developer was to repay the loan to the government.

However

- d) The developer was only to repay 65.8 per cent of the loan.
- e) The 34.2 per cent of the loan not repaid was to be retained by the developer as compensation for the additional costs the developer would incur over and above normal domestic housing (cottage industry) construction costs. In the terminology of the contract these are called “compression costs”.
- f) The contract makes it clear that the additional costs are related to industrial relations undertakings and disputes as a consequence of the Government’s requirement that the developer use union industrial relations arrangements. Other costs were identified, but the IPA’s analysis is that, other than some minor legal and design costs, all costs were tied to industrial relations issues.

The outcome was that, in its contract with the developer, the Victorian Government accepted that the use of construction union industrial arrangements added 34 per cent to the cost of the Heritage Precinct. It is reasonable to assume that this cost escalation benchmark applied across the entire Games Village. Hence the additional cost of the Games Village is 34 percent of \$144 million; around \$50 million.

The following pages from the Heritage Precinct contract show

- Page 10: Clause 6.2.2 (iii): the requirement to pay back only 65.8 per cent.
- Page 7: Clause 3.3: “compression costs”. Particular attention should be given to clause (vi).

Contract cover page

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21 NOV 2007
DEPARTMENT OF INFRASTRUCTURE

Secretary to the Department of Infrastructure
Citta Village Park Pty Ltd and Bayslore Pty Limited
Australand Holdings Limited
Babcock and Brown Pty Ltd *Assoc. Holders*

**Supplemental Agreement –
Athlete Accommodation and
Heritage Precinct**

Melbourne 2006 Commonwealth
Games Village

Ref: MKT OFFICE P20 20041025A
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Page 10 of the contract:

6.2.2 Revised Arrangements

(a) Payment for the refurbishment works

- (i) Under the revised arrangements as set out in this Agreement, the Developer will progressively pay the first \$2,621,314 million of the refurbishment costs for the Retained Buildings and infrastructure costs in the Heritage Precinct;
- (ii) the State agreed to fund all other costs required to complete the build-out of the Heritage Precinct to Games Mode, subject to paragraph (iii);
- (iii) the Developer will reimburse to the State the amount of 65.8% of the net of:

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- (A) those costs incurred in the build-out of the Heritage Precinct which are shown as reimbursable in Table (A); less
- (B) the amounts referred to in Clauses 3.3(i), (ii), (v), (vi) and (vii); and
- (iv) for the avoidance of doubt, the State and the Developer agree that the following items are Table (A) costs referred to in paragraph (iii)(A), and are not included in the reimbursable costs paid to the State by the Developer:
 - (A) the cost of Environmental Enhancements;
 - (B) the cost of temporary landscape works (required for Games Mode);
 - (C) the cost of the installation and removal (and making good) of the Overlay Works;
 - (D) the cost of works constructed in Buildings 4d and 6 beyond "shell & core" works, which are to be funded by the Developer under its shell and core obligations; and

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Compression costs incurred (whether originally forecast or not) in order to complete the works in the Heritage Precinct by the Date for Heritage Precinct Practical Completion. The Developer must include in the particulars provided by the State a comparison of the Heritage Precinct Construction Programme showing the effect of the Compression against the Construction Programme before it became necessary for Compression. The Developer must act reasonably to mitigate any Compression costs. Compression costs will include, but not be limited to, the following:

- (i) additional design costs under Clause 6.2.2(d);
- (ii) additional management and supervision costs (subject to resources noted in Table (C)) incurred by the Developer being the amounts noted in items D3 and D4 of Table (C);
- (iii) contractors and suppliers pricing premiums;
- (iv) commercial labour rates and conditions experienced at the time;
- (v) acceleration costs, including costs incurred in working outside of normal working hours;
- (vi) costs resulting from the timely resolution of industrial relations and OH & S issues or disputes, arising from the construction of works in the Heritage Precinct (and for the avoidance of doubt the Developer acknowledges that the resolution of the industrial relations and OH&S issues or disputes remains the responsibility of the Developer); and
- (vii) all legal costs and Independent Certifier costs relating to the acceleration of works in the Heritage Precinct, including the preparation of this document.

The Developer, in agreeing to proceed with the works in the Heritage Precinct, would not be liable for these or any other Compression costs. The amount of the Compression costs payable by the State were to be determined and certified as payable by the Independent Certifier in relation to items (v) and (vi) above. For the avoidance of doubt, items (iii) and (iv) are included in the non-reimbursable amounts provided for under Clause 6.2.2(a)(iii).

Notwithstanding the foregoing provisions of this Clause 3.3, the Developer would only be entitled to recover Compression costs for Retained Buildings 10 and 11 under items (i), (ii), (v), (vi) and (vii).

The nature of the additional industrial relations costs

When it comes to explaining why industrial relations agreements and construction union activity created greater costs it might be thought that it was simply because construction workers were paid more than housing (cottage industry) subbies. This is not the case. The cost differential is because of unnecessary inefficiencies in the construction sector that are, in effect, a roting of the processes of work. Examples of what happened on the Games Village explain how the additional costs arose.

Wet weather disputes:

The approach to wet weather days in the construction sector is not based on common sense. Rather, the construction unions apply a very technical approach to what is a wet weather day and require work to stop and construction workers to go home. The Games Village was plagued by disputes over wet weather days.

Industry 'rules' state that if it rains to a certain extent between 7 am and 11 am, the site is to be closed for the day. At the Games Village, tools were often downed while site managers and unions engaged in deep 'analysis' about whether or not the site was "wet". While analysis occurred, no work occurred. On many occasions the debate over "wet days" resulted in formal dispute procedures coming before the Victorian Building Industry Disputes Board. Such formal disputes occurred repeatedly during July 2005. Several of these disputes involved the tendering of evidence from the Bureau of Meteorology about the actual amounts and times of rainfall.

The pictures below show some such discussions and were used as evidence as to what constituted “wet” days.



Scaffolding Dispute

In November 2005, the scaffolding contractor, Boral, notified building sites about safety concerns with some of its scaffolding which required checks on all of its scaffolding. Scaffolding-related work at the Games Village was immediately halted pending the required checks being completed. However, the construction unions banned *all* work on the site—including work where no scaffolding was required. The site had plenty of non-scaffolding work available that could have kept the workforce productive.

The ‘dispute’, allegedly over safety, resulted in formal dispute hearings in the Australian Industrial Relations Commission. In all, 18 days of lost production occurred on the site as a result of this dispute.

‘Union safety officers’

In August 2004, a dispute occurred over the provision of a fully paid union safety official to be placed in the Heritage Precinct. The site’s employees were gathered by the union during a morning smoko and told that the site was closed and they were to go home. The developer was not informed by the union about the demand before the site was closed. The matter became protracted and became formalised as a dispute in the Australian Industrial Relations Commission.

Catering

At least one site closure occurred because the union objected to the quality of the steaks being supplied in the site canteen.

Pressure was applied to employ the wives of unionists in the canteen.

End of job union shop stewards

When the Games Village was completed, two union shop stewards refused to leave the site and insisted on being given continuing work—even though there was none available. A union official arrived and for around half a day parked his car across the driveway of the site, thus preventing movement of goods into the site. The State Government eventually agreed to employ the two shop stewards through a labour hire company undertaking other work.

It all accumulates! It's not about wages

The key to understanding the industrial relations inefficiencies witnessed at the Games Village, which were common and systemic across the construction sector, is that the cost is cumulative. The formal identification of strikes does not give the full picture. The greater cost lies with the constant creation of disputes about seemingly simple things that could easily be resolved with goodwill and common sense. There is no reason for most of the disputes. But they are applied as a constant pressure mechanism against the managers of construction sites. This is what creates the inefficiencies and the additional costs.

The Victorian Government recognizes the cost

It is instructive that the Victorian Government recognizes the cost and, in relation to the Games Village, was prepared to accept and pay the additional and unnecessary cost. But the Government was also mindful that if these sorts of costs flowed on to the general housing industry, housing costs in Victoria would skyrocket. In the Memorandum of Understanding for the Commonwealth Games between the government and the unions, the following clause exists:

The parties recognize and agree that, wherever the Village is built, the application of the VBIA (Victorian Building Industry Agreement) is not and will not be used as a precedent for the application of the VBIA to large scale urban development projects or housing unit developments constructed by the cottage housing sector of the Victorian building industry.