

# Industrial Relations and the struggle to build in Victoria

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## Overview

Politics in Victoria revolves heavily around impressions about which political party and leader is better at ‘getting things done’. Jeff Kennett established his reputation as a ‘doer’, whereas the previous Cain and Kirner Labor Governments were denigrated for being controlled by unions who blocked development projects. This benchmark of apparent political capacity to ‘get things done’ applies, in particular, to major infrastructure construction projects.

Victorian unions are a dominant factor in determining whether construction projects in Victoria are completed on time and on budget. The unions that hold sway are the Construction, Forestry, Mining and Energy Union (CFMEU), the Electrical Trades Union (ETU) and, to a lesser extent, the Australian Metal Workers Union (AMWU) and the Australian Workers Union (AWU).

It is well recognised and commented upon that the Cain/Kirner ALP Government was destroyed because of Victorian unions. The Bracks/Brumby ALP Government has been determined not to allow Victorian unions to destroy its period in office.

This briefing paper looks at the success (or otherwise) of the Bracks/Brumby efforts to have major public and private projects completed on time and on budget. The focus of this paper is the impact of industrial relations on those two measures. It case studies, in particular, the largest construction project ever undertaken in Victoria—the EastLink Tollway.

## Relevant Timeline

Late 1999	Bracks/Brumby Government elected: Does not control Upper House of Parliament. Federal Workplace Relations Act (WRA) governs Victorian industrial relations.
Apr. 2001	Saizeriya plant begins construction. Melton. Completion target: February 2002.
2002-03	Cole Royal Commission inquiry into the construction sector. Finds that Victorian commercial construction is 20 per cent plus more expensive than housing construction because of industrial relations factors.
Oct. 2002	Federal Building Industry Taskforce begins.
Nov. 2002	Bracks/Brumby Government re-elected. Gains control of Upper House.
Feb. 2003	Saizeriya plant remains uncompleted.
2003-04	Commonwealth Games construction starts/occurring. MCG, Games Village. Southern Cross Railway Station development. Contract for EastLink let (November 2004).
2004	Howard Government strengthens its Building Code. (This is a federal code applied to all new federally funded or part-funded construction projects. Any builder/contractor who wishes to undertake federally funded construction must have industrial agreements and practices consistent with the code on all government work.)
Oct. 2004	Howard Government re-elected. Controls Senate.
Nov. 2004	EastLink construction begins.
Sept. 2005	Federal legislation passed creating the Australian Building and Construction Commission (ABCC) with the task of policing industrial activity in the commercial construction sector. ABCC also empowered to police the Federal Building Code.
2005	Building code strengthened further with requirement to comply on private-sector work.
Dec. 2005	Federal WorkChoices legislation passed.

## The Bracks/Brumby period

The Bracks/Brumby period in government began badly as far as important infrastructure projects were concerned.

The first major problem which occurred entirely within their period of government was the Saizeriya food manufacturing plant in Melton. Saizeriya is a giant restaurant chain in Japan serving Italian food. Like the McDonald's chain, Saizeriya manufactures its food externally to its restaurants. Saizeriya had decided to consolidate all its food production in one giant plant in Victoria. Plans were drawn up for an eight-factory complex costing some \$400 million on a massive site in Melton which would eventually employ some 500 people directly. All the food produced was to be exported to Saizeriya's restaurants. The additional infrastructure investment required to support and supply the plant with raw ingredients was projected to be over a billion dollars in new abattoirs and vegetable gardens. It was the largest planned food manufacturing investment in Australia's history. The first phase of the manufacturing complex involved one factory at a projected cost of some \$40 million.

The Bracks/Brumby Government inherited the Saizeriya project plans from the Kennett Government. Saizeriya was the first major project in which the Bracks/Brumby Government had total input into the industrial relations arrangements. They guided and advised Saizeriya. It was a problem from start to finish. The Government advised Saizeriya to sign an industrial agreement for operations with the National Union of Workers. This infuriated the AMWU, which asserted that it had rights to control labour at Saizeriya's manufacturing operations. The AMWU teamed up with the CFMEU during construction. The CFMEU delayed the construction phase and the AMWU delayed the machinery installation phase. The construction project ran more than 18 months over time. Saizeriya's restaurant expansion plans in Japan were heavily disrupted and Saizeriya's share price dropped. The Victorian Government advised Saizeriya in Japan that the problems lay with Saizeriya's Melbourne-based management team. The reality, however, was that a factional union war was the cause. This was linked to broader factional disputes inside the Victorian ALP. The facts were revealed in the Cole Commission Inquiry into the construction industry.

The outcome of the entire sorry situation was that Saizeriya was caught up in a union-ALP factional battle over which Saizeriya had no control. The first factory was eventually completed, but Saizeriya then announced that the rest of the project would not proceed. Saizeriya subsequently sued the Victorian Government for \$42 million

in damages. An out-of-court confidential settlement was reached.

Not only did this industrial relations fiasco cost Victoria the largest food investment project in Australia's history but it has done untold damage to Victoria's and Australia's investment reputation throughout Asia. There are apparently several Saizeriya-type businesses in Asia that might well have considered investing in Australia—in Victoria, in particular. That possible investment has now been shelved.

The Saizeriya scenario has been repeated in Victoria during the Bracks/Brumby period on many occasions. The dynamics of each situation are always different and specific to the projects in question, but industrial relations are always a key factor.

- **The Holden engine plant upgrade** ran over time and significantly over budget as a result of industrial relations problems.
- **The redevelopment of Federation Square** was an industrial relations fiasco resulting in extra costs and significant delays.
- **The redevelopment of the MCG** had such high-profile industrial relations problems that the Federal Government refused to contribute \$80 million to the project because of an unacceptable industrial situation.
- **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 normal housing costs. This is consistent with comparative estimates arising from the Cole Commission inquiry into the construction sector.
- **The Geelong Freeway upgrade** was afflicted with cost overruns and delays due to industrial relations issues.
- **The Austin/Mercy Hospital development** was badly affected by industrial relations problems. The Government has not made financial data available that would indicate the consequent cost overruns.

- **The redevelopment of the Southern Cross Railway station** was also a cost and delay scandal attributable to access difficulties, design issues and industrial relations problems. Although it opened in time for the Commonwealth Games, it is in fact still unfinished. The original contracted price for the job was \$286 million, but it actually cost \$341 million. The construction company announced a loss on the job of \$122 million and sued the Victorian Government. The claim was settled for \$32 million to compensate for contract variations and other related issues. Industrial relations problems with the project were particularly severe and reported widely. On the foregoing figures, it could be estimated that delays due to industrial relations problems cost the construction company up to \$90 million. This figure is again consistent with the findings of the Cole Commission Inquiry into the construction sector. This amount would be in addition to industrial relations contingencies which the company would have factored into its original contract price.
- **The Commonwealth Games swimming pool upgrade** was known to have suffered from significant industrial relations delays and cost overruns. The budget blew out from \$50 million to \$60 million. It could conservatively be assumed that \$5 million was attributed to industrial relations issues.

The projects mentioned above were started, committed to or wholly undertaken with industrial arrangements that pre-dated the WorkChoices and ABCC legislation.

In each of these cases, the full costs of the budget overruns is unknown because of government and private company secrecy about relevant information. However, there is enough information in the public domain to indicate that the cost overruns are in the many hundreds of millions of dollars and could even approach half a billion dollars just on these identified projects. A conservative estimate, however, would be as follows:

#### Private additional costs

##### **Saizeriya**

Estimate \$30 million

##### **Holden Plant**

Estimate \$ 4 million

##### **Southern Cross Station**

Estimate \$90 million

#### Public costs

##### **Federation Square**

Estimate \$40 million

##### **MCG**

Estimate \$100 million

##### **Austin/Mercy Hospital**

Not sufficient information to assess.

##### **Games Village**

Estimate \$20 million

##### **Geelong Freeway upgrade**

Estimate \$15 million

##### **Games pool**

Estimate \$5 million

#### Total probable cost: \$304 million

In each of these cases, project redesign and other technical issues will have been contributing factors to the costs being greater than the original planned estimates. This is common to many large construction projects. But what has been by far the biggest contributor to cost overruns and delays is the nature of the industrial relations situation in Victoria. Further, the foregoing figures are for areas of known delay and overruns. That is, they do not take into account the fact that standard construction budgets in Victoria build into the cost estimates a significant allowance for anticipated industrial relations problems. This is normally estimated to contribute at least an additional 15 per cent and is added to budgets.

The principal unions involved in this have been the CFMEU and the ETU, with the AMWU involved in manufacturing developments and anywhere significant metals fabrication is required. The scale of these costs can be better appreciated by looking at the EastLink project in some detail.

## Eastlink case study

The EastLink project is the largest single infrastructure project ever undertaken in Victoria. It is a 40-kilometre road construction project linking Mitcham and Frankston and the Eastern, Monash and Mornington Peninsula Freeways. A \$2.5 billion project (2004 figures), it is expected to take four years to complete. This compares with the CityLink construction which cost \$1.8 billion.

It is a project that is a good case to comparative costs of different industrial relations approaches:

- It is a physically and financially large project and therefore any costs differentials associated with industrial relations issues come into stark relief.
- A comparison can be drawn between CityLink and EastLink. CityLink was constructed entirely before the federal reforms to industrial relations occurred with the passage of the WorkChoices and the ABCC legislation. EastLink, on the other hand, is being constructed under an IR regime heavily influenced by those federal industrial relations reforms. In other words, CityLink was constructed using industrial agreements under the old WRA. EastLink is being constructed using industrial agreements and laws arising from, or influenced by, WorkChoices together with the enforcement agency of the ABCC. It is the first major project in which industrial relations differentials can thus be highlighted.
- Several of the companies involved in the consortium that won the EastLink tender were heavily involved in the CityLink project. The technical, engineering and management competencies involved with EastLink are similar to those used on CityLink.
- As of July 2006, EastLink construction is reported as running a year ahead of schedule substantially as a result of industrial relations peace. (The Age, 11/7/06) CityLink was known to have suffered significant industrial relations problems, particularly as a result of spurious OHS campaigning by unions. This was reported in the Cole Commission Inquiry.

The IPA Work Reform Unit has undertaken a general analysis of CityLink's industrial relations arrangements and compared them with EastLink's industrial relations arrangements. This has been possible because:

- The Cole Royal Commission into the Building and Construction Industry placed significant details in the public domain on CityLink's industrial relations issues.
- The IPA has developed considerable knowledge about industrial relations agreements as a conse-

quence of its Capacity to Manage Index project (CMI). This project ran for over four years, during which it studied and rated the impact of pre-WorkChoices industrial agreements on managerial capacity. The CMI project analysed some 315 industrial agreements and awards. In particular, it examined some 40 agreements and awards from the construction sector, including agreements entered into by companies involved in the EastLink and CityLink projects.

- Further, the IPA collected data from operators in the construction industry.

This combined knowledge has been used in this assessment.

The core of this assessment can be posed as the following central questions:

If EastLink had been constructed under industrial agreements that were outside of the WorkChoices and the ABCC environment, would there have been additional costs to the project? If so, what would those costs be?

Significant cost differentials have been found, amounting to \$295 million on very conservative scenarios and estimates.

The estimate of \$295 million was arrived at by considering the industrial relations costs that were imposed on CityLink which do not appear to have been imposed on EastLink. In other words, if EastLink had been forced to be constructed under CityLink-type industrial arrangements, EastLink would cost at least \$295 million more to construct. This figure comprises direct costs and toll revenue losses by not opening on time.

## The nature of the industrial agreements

The major agreement at Eastlink is one involving both the AWU and the CFMEU. The way in which this agreement was reached is important to understanding the productivity and cost benefits delivered to Eastlink.

The AWU has limited presence on Victorian construction projects, which are normally dominated by the CFMEU. The Cole Commission revealed that the bulk of industrial militancy in Victoria related to the CFMEU. Originally, the Eastlink construction consortium entered an agreement with the AWU. When this became public, the CFMEU became highly agitated and would have used their industrial muscle on other sites in protest at being locked out of the agreement. A settlement was ultimately reached in which the key enterprise agreement involved both the AWU and the CFMEU.

## Some basic EastLink facts

**Total contracted cost of EastLink:** \$2.5 billion.

Federal Government was to contribute \$540 million if the road were toll-free.

**Cost to Victorian budget if built toll-free:** \$1.96 billion.

Anticipated traffic per day is 250,000 vehicles.

Toll charges are capped at \$4.33 per car. Heavy vehicle charges are higher.

Revenue for Eastlink when opened will 'comfortably' be \$20 million a month—\$4.6 million a week. (*The Age*, 11/7/06)

Monthly construction expenditure is around \$50 million, peaking at \$100 million, with the largest cost being labour, involving a workforce of around 1,600 to 2,000 (*The Age*, 11/7/06)

### Wage cost estimates

(from AWU/CFMEU Agreement : rounded)

<b>Full-time weekly employee</b>	\$900
Add 19 per cent for hols/leave	\$170
Add site allowance	\$ 5
Add Incolink redundancy fund	\$ 63
Add other allowances	\$ 5
Add superannuation	\$140
<b>Base benefit to F/T employee</b>	<b>\$1,283</b>
	<b>per week</b>

This does not include double-time on Saturdays and other shift allowances of 50 per cent.

Average packaged value of each full-time job would ex-

ceed \$70,000 per year.

Add payroll tax of around 5 per cent and workers' compensation (of around 11 per cent in the construction sector).

**Total cost per year for each full-time employee:** around \$82,000 plus.

Not all 2,000 employees will work full-time for the full project. But assuming that construction will involve the equivalent of about 1,000 full-time enterprise agreement paid people (excluding managers/engineers, etc.), the cost of labour for the project would be about \$328 million. (\$82,000 x 1,000 x 4 years.)

This gives **average weekly labour costs of around \$1.56 million.**

On the same assumptions, the total number of working days required for the project from a costs' perspective would be about 880,000 (1,000 people x 220 available working days x 4 years). (NB: 'Working days excludes weekends, holidays etc.)

**Number of working hours required:** around 6.3 million (880,000 days x 7.2 hrs).

Note: The CFMEU/AWU Agreement allows for 26 rostered days off [RDOs], with half of those days at times to be decided in discussions with management, and half at the discretion of individual employees in consultation with management. This is very different from normal Victorian construction, where RDOs are set days requiring total construction close down. The Eastlink project allows for flexible RDOs thereby avoiding construction close down.

**Weekly site overheads:** If work stops on any project, the construction company has locked-in site cost overheads which continue to accrue. This is a significant cost factor in assessing the impact of lost construction due to industrial action. The weekly site overheads for the Eastlink project are unknown but can be assumed to be high.

This time, unlike the Saizeriya situation, the inter-factional war between unions was played to the advantage of the consortium's construction needs. In addition, the agreement was reached in a political environment where the Federal Government's labour reforms were looming large both before, and after, the 2004 Federal election.

The outcome was an agreement which was a marked improvement upon standard industrial agreements for construction projects in Victoria.

## Union delegates employed but not working

Standard commercial construction agreements before the introduction of WorkChoices and the ABCC required construction companies to employ union delegates who did no work on sites. This was particularly so in Victoria under industry-enforced pattern enterprise agreements. The delegates simply oversaw the industrial agreements to enforce compliance. They were the unions' eyes and ears on worksites. They organised industrial activity against companies and were the instigators and organisers of industrial disputes. Oddly, these people, whose job it was to work against the interests of companies, were on

companies' payrolls. The CityLink consortium partners typically had such requirements for non-working union delegates.

It is not clear if the Eastlink industrial undertakings require non-working union delegates. However, the likely cost impact of such delegates can be assessed.

The number of non-working delegates that could have been expected on EastLink would have been fifteen or more. The cost of these delegates' direct wages and benefits is estimated at \$5 million plus. This assumes wages, benefits and on-costs of at least \$82,000 per union delegate per year over four years.

With non-working delegates on site, Victorian construction companies normally factor a disruption cost into their budgets. That is, based on experience, it is assumed that the project will take longer than might otherwise be the case because of industrial disputes. From the Cole Commission Inquiry a figure of around 5 per cent more work time could have been expected from industrial relations problems if non-working unions delegates had worked on EastLink.

This would have added somewhere near 315,000 work hours to the project's cost, which equates to around 8.7 additional weeks to complete the project. This would create substantial additional site overheads which cannot be estimated. Eight weeks plus of delay would cost around \$40 million in lost toll revenue. A further \$13.5 million would be incurred in direct labour costs of the working workforce.

#### Probable additional costs

Union delegates' direct wages	\$5 million
Additional employees' direct wages	\$13.5 million
Site overheads	not estimated
Toll revenue forgone	\$40 million
<b>Total</b>	<b>\$58.5 million</b>

## Non-working and non-productive days

In 2004, standard industry practice enforced through union industrial agreements prohibited overtime being scheduled on certain days. The Victorian industry had an organised calendar with which everyone was supposed to comply. These lock-down weekends were linked to holidays and Rostered Days Off to effectively extend days on which work on sites was stopped or restricted.

The days rostered as non-working days and/or restricted working days in the industry included:

Public Holidays	10 days
Union picnic days	1 day
Christmas close down	9 days
RDOs	26 days
Lock-down days	12 days
<b>Total</b>	<b>58 days</b>

These unproductive days, imposed on the industry through industrial agreements, delayed project completion times, thus escalating costs considerably. Since Work-Choices came into effect, these restrictions have been largely removed. The ABCC has been particularly active in policing Federal Building Code compliance in this area. Further, these restrictions were largely eliminated in the AWU/CFMEU agreement. In particular, RDOs are not set on prescribed days but can be arranged by the construction consortium to fit in with construction schedules.

This creates significant advantage to the construction job. It means that construction activity on EastLink can theoretically occur 365 days a year (assuming rostering arrangements can be put in place and the contractors are willing to pay loadings, etc).

Over the four years of the project, this 365-day-a-year potential operation probably adds an additional 242 days of potential productive work days when compared with standard 2004 arrangements. (50 Sats, 1 union picnic, 9 Xmas close down, 26 RDOs, 12 lock-downs) This should enable the project to finish and open some 40 weeks or more earlier than under the 2004 arrangements. The fact that the construction timetable is reportedly already 12 months ahead of schedule (*The Age*, 11/7/06) after less than two years of construction tends to validate this assumption. In fact, the speed with which the project is progressing is almost unheard of in the history of construction in Victoria over the last 20–30 years.

Multiply this by an estimated toll revenue of \$4.6 million per week and the additional potential revenue available to the operators of EastLink is **\$184 million**. Early completion of the work would create significant overheads' savings to the contractors—certainly in the tens of millions of dollars, although this figure cannot be estimated with accuracy.

Assuming continuous construction, **the total estimated differential advantage to EastLink is at least \$184 million.**

## Disruption to agreements during project

Before WorkChoices, the ABCC and Federal Building Code came into effect, Victoria had an unregistered industry agreement, the Victorian Building Industry Agreement (VBIA), which was in force and to which all builders were expected to adhere. The VBIA was the principal agreement by which Victorian unions were able to secure their control of worksites. Non-adherence to the VBIA by any builder would result in builders' sites being closed down by unions. The VBIA was due to be renewed around November 2005, that is, a year into the EastLink construction. Under WorkChoices/ABCC, the VBIA has effectively been neutered—some would argue outlawed.

If EastLink had been required to operate under pre-WorkChoices/ABCC arrangements, it would have found itself in new enterprise agreement negotiations with unions in 2005 (VBIA renewal) in spite of the fact that it had project-specific agreements through until 2008.

It is standard practice in the construction industry to budget for significant industrial disruptions during agreement renewals. Renewal of the VBIA has a long history of creating industrial turmoil in the Victorian construction sector. EastLink would have been faced with this problem under pre-WorkChoices/ABCC laws.

When agreements are renewed, it is common practice in Victorian construction to assume at least five weeks of production disruption and productivity decreases during negotiations. This could have delayed the opening of EastLink by, say, two weeks. This would create a loss to revenue of \$9.2 million (\$4.6m x 2) and additional unknown overheads.

**Total estimated differential: \$9.2 million plus.** This does not take into account additional labour costs as a result of wage increases under the agreements.

## Spurious OHS claims

The Cole Commission analysed the incidence of sham OHS claims and disputes on the CityLink project. It was found that OHS excuses were used extensively by unions to conduct what were, in reality, industrial relations campaigns. Significant delays to CityLink arose as a result. The Commission's data suggest that the OHS shams may have contributed as much as 10 per cent to the total programme hours of CityLink.

If WorkChoices/ABCC had not been implemented, it could be reasonably assumed that EastLink would have suffered from at least a 3 per cent increase in programme

working hours (and that is a conservative estimate). This would add an additional 190,000 working hours to the project, with an additional (say) \$8.3 million in direct labour costs. The delay in completion would be around 5 weeks, leading to an unknown increase in overheads and a loss of toll revenue of \$23 million.

**Cost differential: \$31 million.**

## Bad Weather

The industry standard before WorkChoices was to 'down tools' on entire sites for even the smallest amount of rain. Melbourne has a rainfall pattern which is not consistent across the city. Rain frequently falls in one part of the city but misses suburbs quite close by. With EastLink being a 40-kilometre project, small amounts of rain could routinely be expected somewhere along the route but not on other sections. Industrial practices in place before WorkChoices would have caused work to stop on the whole route. The CityLink project was known to suffer from this problem.

Assuming that misuse of allegations of inclement weather added just 1 per cent to programmed working time, this would equate to 63,000 labour hours, delaying the project's completion by two weeks. This would add an unknown amount in overheads, cost \$9.2 million in forgone revenue and cost (say) \$3.1 million in additional labour costs.

**Cost differential for 'bad' weather: \$12.3 million.**

## Total cost differential

Adding all these factors together, the size of the possible cost differential between CityLink (that is, before Building Code/WorkChoices/ABCC) and EastLink (with Building Code/WorkChoices/ABCC environment) can be given a likely figure.

Non-working union delegates	\$58.5 million
Unproductive days	\$184 million
VBIA Agreement disruption	\$9.2 million
Sham OHS disputes	\$31 million
Sham weather disputes	\$12.3 million
<b>Total</b>	<b>\$295 million</b>

This figure is meant only to demonstrate how the industrial arrangements and behaviours that preceded the WorkChoices/ABCC environment adversely impacted on construction in Victoria. The figure demonstrates

a scenario applying to EastLink and the possible scale of advantage to EastLink by operating under the post-WorkChoices/ABCC environments.

The figure of \$295 million could be too high or low, but on Victorian experience, is likely to be conservative. The Cole Commission indicated that industrial behaviour and industrial agreements in Victoria pushed up the costs of construction by at least 20 per cent compared with housing construction costs. The \$295 million advantage to EastLink posited above, however, represents only 11.8 per cent of the total construction cost. The picture painted here should, therefore, be considered at the mid-range of possible scenarios.

## Eastlink: a toll-free possibility?

If the EastLink scenario is combined with the projects discussed in the historical overview at the beginning of this paper, the total difference in Victorian construction costs between the pre-Building Code/WorkChoices/ABCC regime and that which replaced it would come in somewhere around the \$500 million mark.

EastLink	\$295 million
Discussed projects	\$304 million
<b>Total</b>	<b>\$599 million</b>

This cost differential covers a six-year period and is conservative. It only covers some major projects and does not include any medium or minor ones, such as schools, hospitals and police station construction to name just a few.

In July 2005, the Bracks Government announced that it had spent \$10 billion on capital works in the previous five years and planned to spend \$20 billion in the following five years. (Media Release, Treasurer, 21 July 2005) This \$30 billion of spending over a decade is significant. Giving the scenarios contained in this briefing paper, the cost differential could quite conceivably reach well into the several billions of dollars. Adding private-sector costs into the figure would make it much larger.

This starts to give an idea of the scale of the benefit of the Building Code/WorkChoices/ABCC reforms to the State of Victoria and to the Victorian Government. If Eastlink had been built without tolls, the cost to the Bracks/Brumby Government would have been \$1.96 billion after Federal contributions.

It is more than likely possible that if Building Code/WorkChoices/ABCC had been in place at the beginning of the Bracks/Brumby period, the net benefit to Victoria could have enabled the Bracks/Brumby Government to build EastLink as a toll-free project.