The Role of accounting in legitimising the culture of the Australian construction industry

Rada Kosa Massingham
University of Wollongong

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The Role of Accounting in Legitimising the Culture of the Australian Construction Industry

A thesis submitted in fulfilment of the requirements for the award of the degree DOCTOR OF PHILOSOPHY from UNIVERSITY OF WOLLONGONG

by Rada Kosa Massingham, B.Com (Merit), MBA

School of Accounting, Economics and Finance, Faculty of Business

2017
CERTIFICATION

I, Rada Kosa Massingham, declare that this thesis, submitted in partial fulfilment of the requirements for the award of Doctor of Philosophy, in the School of Accounting, Economics and Finance, University of Wollongong, is wholly my own work unless otherwise referenced or acknowledged. The document has not been submitted for qualifications at any other academic institution.

Rada Kosa Massingham
ABSTRACT

Purpose: The purpose of this study was to examine the underlying conflict between a lawless culture and accounting practices within the context of the Australian Construction Industry. This provided an opportunity to examine accounting’s role as a legitimising process, within the context of the Critical Accounting perspective of whether accounting practice is objective or subjective. In doing so, the aim was to examine the social system that accountants work within this industry. The thesis explores the role of accounting within this complex industry at a period of time, the 2003 Royal Commission, where its lawlessness had become such that society recognised its social contract was breached and told the industry that this behavior would no longer be tolerated.

Design/Methodology/Approach: The methodology is a historical narrative embedded case study which uses content analysis and critical discourse analysis to find meaning in the reports written about the Royal Commission into Building and Construction Industry by Commissioner Cole. The research is in the period 2003-2011, with a primary focus of the period surrounding the Royal Commission into the industry and its immediate aftermath (2003-2005). The thesis has adopted a critical accounting approach based on using ‘new history’ narrative to examine the role of accounting from a socio-metric rather than econometric lens. Therefore, it has been interested in people, the industry’s stakeholders, and understanding their behaviours. The data collection, analysis and reporting uses Content Analysis as well as Critical Discourse Analysis. Critical discourse analysis was used to examine the societal and political themes emerging from the content analysis coding categories. The outcomes of the critical discourse analysis were examined from a
critical accounting perspective, with a particular emphasis on public interest theory, and stakeholder and legitimacy theories.

**Conclusions (or findings):** First, this study shows that accountants in the construction industry acted subjectively. They did this because accounting practice allows scope for what is called creative accounting. Chapter 6 explains the pressure placed on accountants by other stakeholders and how accountants responded. Second, the study provides regulators with information about the social practice of accounting which might be used to improve regulation of the industry. Given much of the industry’s unlawful behaviour occurs due to poor or inappropriate financial management, improved accounting practice in the industry could help restore public confidence and repair legitimation. This could be done by empowering accountants to act as internal regulators. Third, there are practical outcomes in terms of opportunity for accounting bodies to take action to improve accounting practice within the construction industry, addressing accounting standards, and a community of action research. Chapters 5 and 6 examine the complex social systems within the construction industry, and how practical solutions to structural and cultural reform must embrace a systems thinking approach. Fourth, there are several theoretical outcomes. The study contributes to critical accounting theory by advancing our understanding of organisational power and politics, and its impact on the role of accounting. The findings examined how accounting may serve a useful social purpose and how its practice may be continually improved. The analysis concludes with recommendations about how accounting practice may be improved to repair legitimisation in an industry that appears to ignore public interest.
**Research contributions:** (Theoretical) The study contributes to critical accounting theory by expounding how accounting practice was influenced by stakeholder interests within the construction industry’s political economy. By examining the reasons why regulation of the construction industry was so difficult and suggesting how this may be improved the study contributes to public interest theory. In consideration of the importance of the role of accounting in legitimising an industry with a long history of unlawfulness, the study contributes to the political economy theories of regulation reflecting broader cultural and societal values. The study contributes to legitimacy theory by defining the nature of the social contract breach between the construction industry and Australian society, and strategies to repair legitimacy. By exploring how the constructs of relationships, impact and expectations help us understand the social practice of accounting within the context of a social contract breach, the study contributes to stakeholder theory from the managerial perspective. The contribution lies in the empirical evidence of the socio-political power inequities defining the social interaction between industry stakeholders which have breached their social contract. Contributions to stakeholder theory include using social network analysis theory’s construct of density to enhance our understanding of the relationships concept; using the social network analysis constructs of heterogeneity and homogeneity to examine stakeholder behaviour, focusing on harmony and cohesion, furthering our understanding of the ethical perspective; using types and causes of power to explain political behavior, improving our understanding of the impact concept; and identifying four societal expectations to explain the social contract breach, contributing to our understanding of the expectation concept.
(Methodological) The study contributes to the debate between traditional accounting history and new accounting history in two ways. First, it examines the existence of multiple stakeholders within an industry and not just the political or social elites, in this case owners/managers within the construction industry. Whereas traditional accounting history might have written this thesis from the perspective of those with economic power, that is, owners/managers; the new history approach adopted allows for exploration of stakeholders with little power, including accountants, and how this has influenced accounting as social practice in this industry. Second, it questions the role of facts and truth in accounting history. Whereas traditional accounting history has had a pursuit of truth, evidence, and objective knowledge; new accounting history questions the need for such a rigorous approach. New accounting history has a more subjective perspective about events, allowing for multiple truths and even facts, depending upon the lens from which the events are written.

(Substantive) The study makes a substantive contribution by advancing our knowledge of accounting practice based on the social network analysis constructs of interaction, cohesion, and harmony. This produced four types of accounting social practice: trust, regulate, isolated, and hostile. It identifies the unlawful activities and the involvement of accountants in these activities. It defines the accounting processes where unlawful behaviour existed. The study provides guidelines for improving the social practice of accounting.

**Research limitations:** The research is limited in several ways. First, there are methodological limitations. Critics of historical narrative argue that they provide an incomplete story and therefore a weak form of history. This is addressed by embracing the
new history accounting method, which explores the historical narrative of the role of accounting in the construction industry from a social practice perspective. Second, there are theoretical limitations. Critical accounting theory may be seen as a controversial field because it aims to develop a more self-reflexive and contextualized perspective on accounting. While there are several perspectives on critical accounting, this study focuses on the role of sectional interests, for example stakeholders in accounting practice, particularly exploring the role of socio-political power inequities using stakeholder theory.

**Future research:** The historical narrative in this thesis is broad, encompassing a complex industry, substantial data, activities, social networks, and social practice. Future research might involve interviews with individuals involved in the construction industry representing the various stakeholders, to gain further knowledge about motivation, behaviours, and culture. Future research might also consider how accounting might improve its role in this industry by implementing some of the ideas presented in chapter 7.
ACKNOWLEDGEMENTS

This research has been conducted with the support of the Australian Government Research Training Program Scholarship.

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My devoted Mother and Father, thank you for your continuous care, support, and interest.

My darling daughter, Jana, thank you for your enormous encouragement and the sacrifices you have made during your childhood throughout this thesis. Thank you for being interested in my work. I hope I have made you proud.

My wonderful husband, Peter, thank you for coaching me to be resilient and supporting me through this long and arduous journey. Thank you for being my tower of strength and
encouraging me to achieve my goals. I could not have completed this thesis without your unconditional support.
DEDICATION

This thesis is dedicated to my darling daughter, JANA

and wonderful husband, PETER.

Thank you for your love and support.
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<td>AASB</td>
<td>Australian Accounting Standards Board</td>
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<td>Australian Broadcasting Corporation</td>
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<td>Australian Building and Construction Commissioner</td>
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<td>Australian Taxation Office</td>
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<td>Queensland Building Services Authority</td>
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<td>Building Workers' Industrial Union of Australia</td>
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<td>Construction, Forestry, Mining and Energy Union</td>
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<td>Corporate Law Economic Reform Program</td>
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<td>Council of Small Business Australia</td>
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<td>Code of Practice for the Construction Industry</td>
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<td>Deed of company arrangement</td>
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<td>Fair Work Building Industry</td>
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<td>Fair Work Commission</td>
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<td>Fair Work Ombudsman</td>
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<td>GAAP</td>
<td>Generally Accepted Accounting Principles</td>
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<td>GDP</td>
<td>Gross Domestic Product</td>
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<td>GEERS</td>
<td>General Employee Entitlements and Redundancy Scheme</td>
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<td>National Commission on Fraudulent Financial Reporting</td>
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<td>NECA</td>
<td>National Electrical and Communications Association</td>
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<td>NPV</td>
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<td>Acronym</td>
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<td>OSR</td>
<td>Office of State Revenue</td>
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<td>PAYG</td>
<td>Pay-as-you-go</td>
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<td>PC</td>
<td>Productivity Commission</td>
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<td>Political Economy Theory</td>
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CHAPTER 1: INTRODUCTION

The building and construction industry in Australia requires significant cultural change. Such change is necessary if the rule of law is to be reintroduced to conduct and activities within the industry, if individuals’ freedoms are to be maintained, and if the industry is to achieve its economic potential. Change is required in the attitudes of all sectors of the industry, including governments, clients, head (contractors) or subcontractors, industrial organisations and employees. (Cole 2003, vol. 11, p. 3)

1.1 Introduction

Accounting can play an important role in ensuring industry behaviour meets societal expectations by ensuring industry actors operate lawfully and in the public interest. These issues are especially important in relation to the Australian construction industry (hereinafter referred to as the construction industry). This industry is important to Australia due to its economic and social contribution but it has a history of unlawful behaviour. The primary objective of this study is to examine the underlying conflict between a lawless culture and accounting practices within the construction industry. It provides an opportunity to examine the role of accounting as a legitimising process, within the context of critical accounting, to appraise whether accounting practice is objective or subjective.

Construction is one of Australia’s largest industries. An industry analyst report found that the industry generates $285 billion of revenue annually (Dunn 2010, p.3), and represents 6.2% of Australia’s Gross Domestic Product (GDP) (Dunn 2010, p.35). The construction...
industry has a history of behaviour which society has considered unacceptable. In August 2001, the Australian Prime Minister (PM) announced the Royal Commission into the Building and Construction Industry (hereinafter referred to as the Royal Commission (RC)). A royal commission is a major government inquiry into a controversial issue of public importance. The Royal Commissions Act 1902, section 1A, defines a commission as an “inquiry into and report upon any matter specified in the Letters Patent, and which relates to or is connected with the peace, order, and good government of the Commonwealth, or any public purpose”. Gilligan (2002, p. 22) notes that the pragmatic function of a public inquiry, such as a royal commission, is to “investigate an issue for a government, collect information, submit a report and make recommendations”. Gilligan (2002, p. 23) argues that public inquiries such as royal commissions have a “broader political, or ideological, function as a management strategy, in particular that of crisis management”.

On 29 August 2001, the Governor-General issued a commission to The Honourable Terence Rhoderic Hudson Cole RFD QC (hereinafter referred to as Commissioner Cole) to “conduct inquiries into the unlawful or otherwise inappropriate practice and conduct in the building and construction industry” (DEWR 2003, p. 11). The Terms of Reference (TOR) asked Commissioner Cole to make recommendations to “improve the state of the industry” (DEWR 2003, p. 11). Clearly, the DEWR saw the RC as tasked to identify inappropriate conduct, the social contract breach, and to fix it, by repairing legitimacy.

There are several reasons why governments appoint public inquiries such as royal commissions, including: (1) to provide a perceived independent response to a crisis situation and (2) to investigate allegations of impropriety (Prasser 2006). Launching a royal
commission is a serious matter and a clear message from the government that an industry’s behaviour has breached society’s expectations of acceptable conduct. There have been numerous Australian Royal Commissions including the coal industry (Davidson 1929), wheat flour and bread industries (Gepp 1936); however, the only industry subject to a Royal Commission in Australia during the twenty-first century is the construction industry (Prasser 2006). This illustrates the significance of an industry royal commission. The Commissioner Cole completed his report in 2003, and it is known as the Royal Commission Report (RCR). It was an important event in Australia’s history, and a substantial intervention by the government as regulator of the construction industry.

There were two main reasons for the PM to launch the RC. First, the perception that the construction industry’s behaviour had become unacceptable. This established that there was a social contract breach. The industry had a long history of unlawful and inappropriate behaviour. However, society was no longer willing to tolerate this behaviour. The impetus for the RC was a report on the Australian Broadcasting Corporation (ABC) television program Four Corners which exposed a culture of corruption within the trade unions associated with the construction industry (Neighbour 2001). The industry had an unsavory reputation and even had links to organized crime which attracted significant negative media and other coverage. While there was a tendency to blame trade unions for illegal and unsatisfactory conduct, there were suggestions that management and other industry stakeholders were involved, at least to the extent that they did not act to stop unlawful behaviour. The Four Corners report highlighted growing alarms about the extent of unlawful behaviour within the industry, and forced the government to investigate whether it was acting in the public interest.
Second, the perception that society would benefit if the construction industry unlawful and inappropriate behaviour was addressed. This established that the legitimisation of the construction industry was necessary. The RCR argued that all sectors of the Australian economy would benefit if the structural and cultural reforms recommended for the construction industry were successfully implemented (Cole 2003, vol. 1, pp. 3-4). The societal contract between the construction industry and Australian society in the period following the RC was that it will achieve its economic potential by successfully implementing the recommended reforms.

The PM’s statement explaining the need for the RC made it clear that it was a criminal investigation with the use of the word ‘unlawful’ or otherwise inappropriate conduct. The TOR asked the RC to find evidence of this unlawful behaviour and solutions. The statement explained that the regulator felt the social contract with the construction industry had been breached and wanted the legitimacy gap closed so that the industry could once again be considered legitimate.

The structural and cultural issues highlighted by the RC in 2003 had developed over many years. Much of the cultural behaviour was historically caused by the industry’s industrial relations structure. The cost of industrial relations breakdown in the construction industry was highlighted a decade before the RC (Aiyewalehinmi, Oluwoye, & Lenard 1994). The industry’s structural issues were created by power imbalances between industry stakeholders; particularly the widespread use of very small businesses, known as sub-contractors (Toner 2006). The construction industry’s unsatisfactory behaviour was caused by industrial relations activity which exploited the structural imbalances within the
industry. The RC found that the industry has a proven predisposition to manipulation and non-compliance embedded in its culture (Cole 2003).

This study examines the role of accountants within the construction industry from two perspectives: how accounting may have dealt with the business practices that led to the RC (up to 2003), and then how accounting may have assisted structural and cultural reform (after 2003). Construction firms employ accountants to analyse and report on financial information to explain current performance and future prospects (Palepu, Healy, Bernard & Peek 2007). In the construction industry, there are large firms, known as head contractors, and small firms, known as sub-contractors. Head contractors employ accountants to provide management and financial accounting information for internal decision making involving management, external reporting involving stakeholders such as owners and investors, and regulation involving auditors. However, sub-contractors are different. While there are larger sub-contractors who employ accountants, most firms outsource this function to an accounting firm which is paid to provide professional services. Sub-contractors typically employ five staff or less (Toner 2006). These are very small business which would not be able to afford a full-time accountant. Their accountant would be an outsider, who may not be aware of the day-to-day operations of the business.

The unlawful and inappropriate behaviour of the construction industry leads to questions about the role of accounting within the businesses of head contractors and sub-contractors. While accountants may have had different employment relationships with these firms, they are still bound by the professional and ethical standards adopted by the profession. Researchers disagree over whether accounting is as an objective rule-based system which supports legitimisation processes, or a subjective construction based on satisficing (Deegan
2009). Given the unlawful and inappropriate behaviour in other functional areas within the construction industry, such as management, project management, procurement, and human resources (Cole 2003); it leads to questions regarding the role of accounting. Given employees involved in these other activities were involved in unlawful behaviours; accountants, in all likelihood, would have also been involved. In recent years, white collar crime, for example Enron, including insurance claims, credit cards, money laundering, and cyber-crime has been highlighted as an increasing problem for society (Yallapragada, Roe & Toma 2012). Accounting has been implicated in these scandals with suggestions that accountants and auditors had “unethical standards, unscrupulous and cooperating” behaviours (Yallapragada, Roe & Toma 2012). This study does not make accusations regarding the behaviour of any of the construction industry’s stakeholders, including trade unions or accountants. Instead it examines the role of accounting within this environment based on publicly available information and sources, but in doing so, does not infer illegal activity regarding any individual or firm.

This study provides an opportunity to test accounting’s role as a legitimising process in terms of whether accounting was able to address the social contract breach. In this way, this study examines whether accounting was part of the unlawful behaviour that led to the RC in 2003. Accountants are employed by the firm and their livelihood depends upon maintaining this employment relationship with the firm. Under these circumstances, this study will explore how accountants responded to pressures for inappropriate conduct, which seemed to have involved staff in other functional areas, with similar employment relationships. This provides an opportunity to engage in the Critical Accounting Theory (CAT) debate about whether accounting is an objective or subjective practice. If it is
objective, then this study should find that accountants were able to withstand the pressures exerted by stakeholders such as owners/managers, and apply accounting practices, such as the standards, in all circumstances. If it is subjective, the study should find that accountants were unable to withstand these pressures, and applied creative accounting or other practices which applied individual judgment.

The purpose of the thesis, and the underlying research objectives and broad research themes, is to examine underlying conflict between an unlawful culture and regulated accounting practices within the context of the construction industry. The thesis has a sociological perspective in the sense that it focuses on the behaviour of accountants within the broader social context of the organisations and the industry they work in. The outcome is a social reconstructed reality of accounting within this economic and socially important industry, which advances our understanding of the role of accountants, and their legitimation of cultural behaviours within the broader objective of protecting the public interest.

1.2 The Importance of the Construction Industry

1.2.1 Importance of the Study

Studying the conduct of the construction industry is important from at least three considerations. The industry is important to Australia’s economy, contributing 6.2% of Australia’s GDP. The RC described it as “critical to welfare and prosperity in Australia” (Cole 2003, vol. 1, p. 3). The industry is a major source of employment for Australians in industries such as building material suppliers and associated service providers; in particular
it provides an important service for society in terms of shelter and infrastructure. Thus Australian society desires a strong and competitive construction industry, which behaves lawfully. The RC argued that the whole of Australian society would benefit if the construction industry addressed its unlawful behaviour. The study helps us understand the role accountants can play in meeting this societal expectation.

Implementation of industry cultural change necessary to satisfy societal expectations is an important measure of effective government policy. As chapter 4 will show, the construction industry has been heavily regulated for decades. The Australian federal government acted as the industry regulator on behalf of Australian society which expected the industry to meet its social contract. Many attempts at regulation had little success. Indeed, the construction industry unlawful and inappropriate behaviour appeared to worsen in years leading up to the RC in 2003. The government made a significant investment in conducting a RC and the Australian society would expect a return on that investment in the form of successful implementation of the cultural change reforms. The government had run out of patience with the industry and its previous attempts at reform and now wanted the industry to change its business practices. The Commissioner Cole stated that cultural reform of the construction industry would have widespread direct and indirect benefits (Cole 2003). This study helps us understand the role accountants might play in industry cultural reform and achieving these benefits.

The construction industry provides a unique context for examining whether accounting is an objective rule-based system or a subjective process influenced by stakeholder demands. In this way, the study presents an opportunity for examining the role of accounting in a business environment moving towards increased focus on good corporate governance,
ethical behaviour, and social responsibility (Lusher 2012). Society expects accounting to assist in compliance with the social contract between itself and organisations or even industries. This study also provides a historical context by tracking changes from 2003 till 2012, thereby enabling an opportunity to examine whether accounting helped the industry towards legitimisation.

The study makes important contributions in measuring changes in the behaviour of the construction industry, the role of accounting, and accounting’s value to society. The study is grounded in a critical accounting theoretical perspective, which views accounting as a process that occurs within the social construct of organisations. This study contributes to our understanding of the social reality of accounting within the research context of this economic and socially significant industry.

1.2.2 Australian Construction Industry Societal Reputation

The construction industry has a long history of propensity towards unlawful or rebellious behaviour, and the industry’s history is strongly associated with the birth and growth of the trade union movement in Australia. The workers in the construction industry are mainly laborers or tradespeople and their employers are wealthy landowners or property developers, which has created socio-political inequities which manifested in the working class wealth divide. This led to the formation of some of the strongest and most militant trade unions in Australia. The unions have a history of conflict with employers, which has led to government intervention and ultimately the deregistering of several unions (CFMEU Victoria 2010). The construction industry has a reputation of industrial relations conflict and practices requiring intervention by the regulator, the Federal Government.
The RC contained 23 volumes. Volume 23 is confidential and not open to the public. Volume 3 was a particularly important volume as it addressed cultural change, which was seen as a major factor in the construction industry’s unlawful behaviour. Commissioner Cole makes this comment at the beginning of volume 3:

The nature and extent of the unlawful and inappropriate conduct disclosed in the hearings before me and recorded in this report should not continue uncorrected (Cole 2003, vol. 11, p. 3).

The RC, which described the industry as having a “culture of disregard for the law” (Cole 2003, vol. 1, p. 13), was scathing in its criticism of the trade unions and union officials associated with the industry. Much of the blame for the unlawful culture in the industry was placed with the unions. However, there is evidence in the RCR that the other industry stakeholders, most especially employers and management, complied with the demands of the unions and participated in unlawful behaviour. This behaviour most commonly created unfair or unsafe workplace practices. There was also abundant evidence of fraudulent activity including misuse of funds, bribery, and corruption. As explained in the RCR, this unlawful behaviour was “fostered because of the short term project profitability focus of all those in the industry” (Cole 2003, vol. 1, p. 13). This implicates all industry stakeholders. Accountants are involved in the pursuit of profitability because they analyse and report on profitability measures and as discussed earlier profit manipulation is an activity of unlawful and inappropriate behaviour that would involve accountants.

The pressures caused by competition encouraged people to break the rules in the pursuit of profit. At this stage, it is important to note that while many of the cultural problems were blamed on trade unions, which led to widespread intimidation, harassment, coercion, and
fear, the RC infers that management (and others) were to blame for complying with union demands. Management contributed to the cultural problems in pursuit of profit for, if they did not comply, projects would be delayed and profits lost. If activities involved financial management, management may have involved their accountants in complying with the demands of trade unions. If money was involved in the interaction between management and trade unions, accountants should have been aware and perhaps involved.

### 1.2.3 Public Interest Theory

There is significant public interest in the construction industry because it is important economically, socially, and politically. Public Interest Theory (PIT) claims regulation is introduced to protect the public and that regulators seek to maximize the overall welfare of the community. Regulation is a trade-off between the cost of regulation and the social benefits of regulation (Scott 2003, p. 448). PIT assumes that the regulator, which is usually the government, is a neutral arbiter of the public interest and does not let its self-interest impact on the regulatory process. From a financial reporting perspective, investors need “protection from fraudulent organisations that may produce misleading information which, due to information asymmetries, cannot be known to be fraudulent when used” (Deegan 2006, p. 41).

The regulation of accounting or the absence of regulation can have many economic and social consequences (Deegan 2006, p. 43). Researchers make the distinction between public and private interest theory of regulation. Public interest is often described as investor protection regulation because it aims to protect investors from unlawful behaviour. PIT
“holds that regulation is supplied in response to the demand of the public for the correction of inefficient or inequitable market practices” (Posner 1974, p. 335), which suggest it is in the public’s interest for firms to operate their business efficiently and equitably. Private interest theory argues that regulation is driven by the needs of powerful lobby groups, and while this definitely happens in Australia, for example the powerful mining industry successfully over-turned the Resources Super Profits Tax, an unpopular government tax, in 2010, this was not the case with the construction industry in 2003. The RCR suggested that the government believed that the industry was ‘under-performing’, largely due to inefficient work practices caused by unlawful behaviour, and that the resulting lack of productivity was hurting the Australian economy. In this respect, the RC was driven by genuine public interest by the regulator with a sincere desire to force the industry to comply with society’s expectations.

Political Economy Theory (PET) (Gray, Owens & Adams 1996, p. 47) provides the social, political and economic framework for this thesis. Legitimacy Theory (LT) and Stakeholder Theory (ST) both derive from the broader theory of PET (Deegan 2009, p. 321). LT will be used to define the social contract between the construction industry and the society within which it operates. (Deegan 2009, p. 325) The industry value system is incongruent with the value system of the larger social system. This incongruence results in a disparity that is a threat to the legitimacy (Lindblom 1994, p. 2). ST will be used to identify key stakeholders, individual social contracts and industry’s responsibility to stakeholders, both managerially and ethically. Gray, Kouhy, and Lavers (1995) explain that there are similarities and overlap between LT and ST as both address the issues underlying PET. However, the two
are distinguished by using LT to consider the construction industry’s interactions with society as a whole, and ST to focus on the interactions between the industry’s stakeholders.

The basis of an industry’s social contract is explained by PIT. PIT claims regulation is introduced to protect the public and that regulators seek to maximize the overall welfare of the community. From an accounting perspective, regulators, such as the government, primarily aim to protect investors from fraudulent activity, but also aim to protect against non-productivity and other poor performance which will have significant direct, such as loss of employment, and indirect, such as non-competitiveness of supporting industries, impact on the economy.

LT provides further insight into the social contract between the industry and Australian society. “Legitimacy theory asserts that organisations continually seek to ensure that they are perceived as operating within the bounds and norms of their respective societies - that is, they attempt to ensure that their activities are perceived by outside parties as being ‘legitimate’” (Deegan 2009, p. 323). Traditionally, accounting theory has been situated within the goal of profit maximization as the optimal measure of corporate performance (Patten 1991). Under this notion, a firm’s profits were viewed as an all-inclusive measure of organisational legitimacy (Ramanathan 1976) because this increased societal wealth. This perspective addresses the non-productivity and poor performance aspects of the RCR. However, an increase in corporate disasters (for example, Enron) and unethical behaviour has led to a shift in focus. Social contracts expect organisations to react and “attend to human, environmental, and other social consequences” of their activities (Heard & Bolce 1981, p.247). This perspective addresses the unlawful behaviour aspects of the RCR.
The RCR sets out society’s expectations of the industry, and the extent to which it complies with the social contract (Deegan 2009, p. 325). In this sense, the RC represents a gap analysis, measuring the difference between current practice and desired practice, and was a significant trigger for change. This defines the ‘legitimacy gap’ in the industry’s social contract (Deegan 2009, p. 329). The legitimacy gap is the difference between how an organisation should act and how it is perceived that the organisation has acted (Deegan 2009, p. 329).

Seven unlawful behaviours were selected as the focus of the thesis. These behaviours were identified from the analysis of the RC findings. They were selected because they were dominant themes in the RC and were associated with financial matters and, therefore, might involve accountants. The seven unlawful behaviours are:

1. Tax evasion
2. Employee entitlements
3. Phoenix company activity
4. Security of payments
5. Profit reporting
6. Inappropriate payments
7. Payroll tax

The process for selecting these behaviours was as follows. Volume 1 of the RCR presents Commissioner Cole’s main findings (Cole 2003, vol. 1). There were three key findings which were used in the selection of these behaviours:

2. On pages 6-10, section 19: The types of inappropriate conduct which exist throughout the building and construction, listed 87 behaviours (Cole 2003, vol. 1, p.6-10).


While profit reporting was not specifically mentioned in the three sections outlined in table 1.1, it was mentioned numerous times in the volume 1 report (and elsewhere in the other volumes). An example is discussion of the short term project driven profit process (Cole 2003, vol. 1, p.13), which reveals Commissioner Cole’s concerns with how the construction industry’s structural and cultural problems created pressure to manipulate reporting. Profit reporting involved profit manipulation. This was done for several purposes and for different audiences. Owners/managers might seek to manipulate profit reporting to falsify the company’s financial position to persuade other companies of financial viability when tendering for work, or to mislead regulators and evade tax, or even to avoid the threshold for payroll tax. The RC provides several detailed case studies which shed light on how employers engaged in inappropriate behaviours associated with profit reporting (see section 6.2.5). Table 1.1 provides details.
<table>
<thead>
<tr>
<th>Unlawful Behaviour</th>
<th>Section 15</th>
<th>Section 19</th>
<th>Section 36</th>
</tr>
</thead>
<tbody>
<tr>
<td>Tax evasion</td>
<td>(v) avoidance and evasion of taxation obligations</td>
<td>N/a</td>
<td>(p) Taxation obligations – avoidance and evasion</td>
</tr>
<tr>
<td>Employee entitlements</td>
<td>(c) underpayment of employees’ entitlements</td>
<td>N/a</td>
<td>(w) Workers’ entitlements</td>
</tr>
<tr>
<td>Phoenix company activity</td>
<td>N/a</td>
<td>N/a</td>
<td>(l) Phoenix companies</td>
</tr>
<tr>
<td>Security of payments</td>
<td>(u) absence of adequate security of payment for subcontractors</td>
<td>N/a</td>
<td>(n) Security of payments</td>
</tr>
<tr>
<td>Profit reporting</td>
<td>N/a</td>
<td>N/a</td>
<td>N/a</td>
</tr>
<tr>
<td>Inappropriate payments</td>
<td>(j) widespread making of, and receipt of, inappropriate payments</td>
<td>• Unions insisting on the payment of a travel allowance to workers who did not travel in their work</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>• Payment by a head contractor of unpaid debts of its subcontractor, pursuant to an implicit or explicit union demand</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>• A practice within the industry that the response to the unlawful or inappropriate exercise of power by a union is the payment of money or a ‘commercial solution’ rather than resort to the law</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>• The disguising of payments of money by contractors to a union</td>
<td>(u) Unlawful and inappropriate payments</td>
</tr>
<tr>
<td>Payroll tax</td>
<td>N/a</td>
<td>N/a</td>
<td>(k) Payroll tax obligations – compliance</td>
</tr>
</tbody>
</table>
“Legitimacy theory proposes a relationship between corporate disclosures and community expectations, the view being that management reacts to community concerns and makes necessary changes” (Deegan 2009, p. 340). Researchers tend to use media reports as an indication of public satisfaction or dissatisfaction with an organisation’s activities (see Ader 1995, p. 300; Brown & Deegan 1998). Organisations can also use customer surveys to gauge satisfaction levels. Neuman (1990) distinguishes between “obtrusive” and “non-obtrusive” issues, which defines public awareness levels, and enables organisations to prioritise issues for action. For example, interest rate increases are highly visible and would be an obtrusive issue for banks; while industrial relations practices or accounting procedures would be invisible to most and, therefore, classified as non-obtrusive. In this study, the RC made societal expectations very explicit for all industry stakeholders. In addition, chapter 5 will show that the construction industry had a history of regulation prior to the RC. Society, through the regulator the Federal Government, had made its dissatisfaction with the industry’s behaviour explicit. Therefore, the industry’s managers should have known what society expected of them and that they were in breach of this expectation. Managers did not need to carry out their own research, analysis, or guess what society expected from them. The RCR clearly specified the nature of the social contract. Therefore the societal contract and the nature of the breach was made explicit both before the RC, through the various efforts to regulate the industry before 2003, and then by the RC.

Based on the above discussion of the theoretical definitions, the main conceptual development will lie in understanding the interaction of stakeholders in complying or not complying with the construction industry’s social contract. This discussion will focus on
the role of accounting. This examines the reasons that led the various stakeholders, including accountants, to accept or reject society’s expectations.

The social contract and the importance of pursuing legitimacy is explained in three ways: Pragmatic: based on audience self-interest, Moral: based on normative approval, and Cognitive: based on comprehensibility and taken-for-grantedness (Suchman 1995, p. 1). Legitimacy is a relative concept in the sense that it is relative to the social system in which the organisation operates at a particular time and place (Deegan 2009, p. 324). Legitimacy motives help us understand its relativity. Pragmatism is focused on the stakeholder doing what is right for them, morality is the sense of doing the right thing, and cognitive is ‘doing things the way we do it around here’. The legitimacy motives of the various stakeholders within the construction industry will be distinguished. This will then explain the industry’s motives for compliance or non-compliance with the social contract.

Stakeholders motivated with pragmatism will be more likely to breach the social contract than stakeholders motivated by cognitive or morality motives. In terms of ST, there are various groups with a vested interest in the construction industry, but they also have different expectations of accounting practice, manifested as multiple social contracts. The inappropriate behaviour associated with other construction industry activities suggests that the industry tended to adopt a managerial rather than ethical perspective on stakeholder expectations. Clearly, not all stakeholder groups are equal in the Industry. This may have affected accountants employed by the industry due to differences in power within these groups creating conflict over accounting practice. This suggests the need for enquiry into who amongst these stakeholder groups was in control and what their expectations of accounting were. ST allows an opportunity to further examine the tension between
accounting as an objective rule based system versus a subjective reality. This raises the question of whether accounting is based on a sense of responsibility, doing the right thing, or demand, meeting the interests of the most powerful stakeholders. There are three stakeholder constructs: relationships, impact, and expectations (Gray, Owens & Adams 1996, p. 45). Relationships measures the importance of the stakeholder to the organisation, impact measures which stakeholders the organisation’s activities will have the greatest effect on, and expectations measures stakeholders in terms of their vested interest in the organisation. This framework is used to differentiate the political economy of construction industry stakeholders. The political economy will be stronger if there are differences between stakeholders in these three stakeholder constructs. On the other hand, homogeneity within the stakeholders will create a weak political economy. A strong political economy will be dysfunctional, manifesting in social contract breach, and create pressures on accounting practice. Alternatively, a weak political economy will lead to more compliance with the social contract and less pressure on accounting practice. Organisations that treat stakeholder groups as more equal are more likely to follow the social contract.

1.3 Accounting and Regulation

The accounting “profession’s social obligation to serve the public is paralleled by enhanced occupational status. In return for this enhanced status, members of the profession agree to undertake their work with the public interest in mind” (Carey 1965, p. 376). Accounting has high occupational status, largely because it deals with money and has a reputation for integrity and objectivity, which is reinforced by the audit process. Accounting and
accountants are afforded trust by society with the understanding that they will act in the public interest. Members of the Accounting Professional and Ethical Standards Board Limited (APESB) are required to comply with APES 110 Code of Ethics for Professional Accountants, when acting in the public interest (Section 100.1). Further guidance on the application of the fundamental principles contained within Part A and Part C of the code are provided to Members in Business in APES GN 40 Ethical Conflicts in the Workplace – Considerations for Members in Business.

The societal contract agreed to by accountants is embodied in the accounting standards. The standards represent the set of rules that accountants agree to follow in carrying out their work. The public interest is served by accountants doing their work according to the accounting standards. In the construction industry, one of the main standards issued by the Australian Accounting Standards Board (AASB) is Australian Accounting Standards Board (AASB) 111 Construction Contracts, which establishes that “the primary issue in accounting for construction contracts is the allocation of contract revenue and contract costs to the reporting periods in which construction work is performed”. Distortions in profit may result from misstated revenue. It is important that “contract revenue is matched with the contract costs incurred in reaching the stage of completion, resulting in the reporting of revenue, expenses and profit which can be attributed to the proportion of work completed” (AASB 111, para. 25). If this standard is not followed, then inappropriate behaviour such as profit manipulation may occur. AASB 111 is to be superseded by AASB 15 Revenue from Contracts with Customers as of 1 January 2018.

A construction firm must determine how and when to recognise contract revenue and contract costs. The accounting standard prescribes the accounting treatment of revenue and
costs associated with construction contracts. The standard, in essence, requires that contract revenue and contract costs be recognised by applying the stage of completion method and that specific information be disclosed about construction contracts in the financial reports of contractors. The accounting standard requires the entity to disclose:

a. Amount of contract revenue recognised as revenue in the period; and
b. The methods used to determine the contract revenue recognised in the period; and

c. The methods used to determine the stage of completion of contracts in progress (AASB 111, para. 39).

According to the accounting standard, the stage of completion of a contract may be determined using the following methods:

1. The proportion of contract costs incurred for work performed to date bear to the estimated total contract costs; or
2. Survey of work performed; or
3. Completion of physical proportion of the contract work (AASB 111, para. 30).

Australian accounting standard AASB 111 is highly subjective and allows a high degree of choice in the recognition of revenues and expenses with reference to the stage of completion method. The broadness of the standard allows the industry to ensure they are perceived as operating within the boundaries of generally accepted accounting principles (GAAP).

Using the critical accounting premise that problems in accounting are potential problems in and of society (Cooper & Sherer 1984, p. 222), potential problems in and of society are problems in accounting. In doing so, it is acknowledged that accounting is more than calculative, in that it is a social practice involved in political struggles (Burchell, Clubb,
Hopwood, Hughes & Naphapiet, 1980, p. 13). As outlined above, the RC found the construction industry was lawless in its conduct of industrial relations. It exhibited cultural norms of non-compliance and regulatory antipathy. This study examines whether the practice of accounting was also influenced by these cultural norms.

Critical accounting researchers attempt to understand those who practice accounting by investigating the practice of accounting. This involves explaining the actions of accountants in terms of their meanings. Researchers argue that “practitioners do not see accounting as a purely technical activity: objective, factual and neutral. Instead, they see it as a social activity and draw on many meanings objective, subjective, inter-subjective, positional in explaining how they construct practice within specific social contexts” (Jones 1992, p. 225). It is this which constitutes accounting rationality in practice. From a critical accounting perspective, there is a need to understand this rationality in order to explain, and change, accounting.

Accountants often see themselves as engaged in an objective, value-free, technical enterprise, representing reality "as is"; when the reality is that “they are subjective ‘constructors of reality’, presenting and representing the situations in limited and one-sided ways” (Morgan 1988, p. 477). Critical accounting theorists argue that accountants “are not just technicians practicing a technical craft, they are part of a much broader process of reality construction, producing partial and rather one sided views of reality, exactly as an artist is obliged to produce a partial view of the reality he or she wishes to represent” (Morgan 1988, p. 477). The following quote argues that accounting is subjective.

By appreciating and exploring this dimension of the accounting process, accountants have a means of developing a new epistemology of accounting that will
emphasize the interpretive as opposed to the supposedly ‘objective’ aspects of the discipline, perhaps in a way that will help broaden and deepen the accountants' contributions to economic and social life (Morgan 1988, p. 477).

Accountants are social beings who work within a social system involving complex behaviours and attitudes. This is particularly apparent in the construction industry which demonstrated evidence of non-compliance with government regulation. If management and other stakeholders could reject government directives associated with work practices it leads to questions about whether they would also reject regulation from accountants and their regulation, that is, auditors and the accounting standards. As individuals, accountants in the construction industry operated under workplace pressures very different from their colleagues in other industries, but with the same needs to maintain employment relationships. The reality of accounting practice, in this sense, was different for construction industry accountants compared with accountants from most other industries in Australia at the time of the RC in 2003.

Accounting choice theory (Watts & Zimmerman 1986; 1990) considers the implications of not only the nature of the firm but also the role accounting plays within the firm for accounting choice of GAAP (Watts 1992). Hunt and Hogler (1990) stated that:

There is a growing awareness that generally accepted accounting principles (GAAP) have become highly politicized and manipulable. As a result, not only have authoritative accounting bodies (e.g. the FASB) lost some of their credibility, but the situation also allows managers to construct a portfolio of accounting choices that are in their own best interests and not necessarily in the best interests of other parties (e.g. shareholders, creditors, employees). Indeed, "In the acquisition of capital and in the managerial labor market (hiring, remuneration and retention) (Fama, 1980), it is to managers' advantage to have the discretion either to disclose or to fail to disclose information to investors, in order to put themselves in the best possible light" (Gaa, 1986, p. 442). Furthermore, as long as managers' accounting choices are in compliance with GAAP, they will be sanctioned by professional accountants through the audit attest function (p. 56).
This sociological perspective of accounting choice theory suggests that the flexibility allowed under GAAP results in a range of factors, such as ownership structure of the firm, as having influence on the way accountants legitimise accounting activities.

This section has explained that the role of accounting has traditionally been to protect the public interest, manifested by following accounting standards, which represent the accounting profession’s societal contract. CAT challenges the view that accounting is an objective rule based practice and accounting choice theory adds weight to the argument that the pursuit of standards is a subjective choice made by individual accountants who perhaps seek to serve their own interest first and the public interest second. Given the widespread unlawfulness in other areas of the construction industry, this presents an excellent opportunity to investigate the reality of accounting in an environment where individuals are under constant pressure to bend the rules. Given this operating context, this study will examine whether accountants allowed themselves to be influenced by those engaging in unlawful behaviour or whether they were able to resist these pressures and not become involved. Accountants are, after all, only human.

1.4 The Role of Accounting

The RC found the industry was characterised by widespread disregard for the law, recording over one hundred types of unlawful behavior (Cole 2003). While the majority of these acts were related to industrial behaviour, such as unfair workplace practices, there were behaviours relevant to accounting. More specifically, the RC found tax evasion, widespread inappropriate payments, underpayment of employee entitlements, absence of
adequate security of payments for sub-contractors, non-compliance with payroll tax and the creation of phoenix companies amongst other breaches in regulation. Thus accounting practices were involved in the construction industry’s unlawfulness. This indicates that the accounting profession operates to support the views of business (Sikka & Wilmott 2005), and is a subjective process.

A major cause for the escalating unlawfulness leading up to RC was that the existing regulatory bodies had insufficient power and resources to enforce the law (Cole 2003). As chapter 4 will show, regulation up to the time of the RC failed to ensure that the industry carried out its work not just in the interests of those most immediately involved, that is the owners and employers, but society generally. The RCR claimed that trade union officials, in particular, felt above the law in the sense that unlawful behaviour seemed to go unpunished. The failure of the Federal government to regulate behaviour in the construction industry suggests that other regulatory bodies, such as auditors and the AASB, would have also struggled to impose order. If the construction industry ignored the Federal Government, they may also have ignored accounting regulators. Therefore, the key themes considered in this thesis are:

1. The way in which the structural and cultural factors that led to the RC in 2003 affect accounting practice in the construction industry.

2. The role of accounting in the construction industry firms’ social contract.

In considering the first theme, there is a range of key social actors in the construction industry: owners, general managers, project managers, accountants, general staff, construction workers, subcontractors, suppliers, government, regulators, unions and...
investors. There are social tensions between accounting regulation and these social actors. This theme reconstructs the social reality of accounting within this industry and addresses the theoretical issue of whether accounting is objective or subjective.

In relation to the second theme, the RC confirmed breaches in the “social contract”, that is, the expectation that society had about how the industry should conduct its business (Deegan 2009, p. 325). This explores the reaction of the wider social system. There were a number of government intervention strategies. First, the Building Industry Taskforce (BIT) was established as an interim measure on 1 October 2002 in direct response to the core findings of the RC, until the establishment of a national agency. The BIT was created due to the “continuation of unlawful and inappropriate behaviour in the industry” (Hadgkiss 2004, p. ii; 2005, p. i) and “the overwhelming requirement for greater powers in order to fulfil the Government’s objective of securing the rule of law” (Hadgkiss 2004, p. ii). Second, the passing of the Building and Construction Industry Improvement Act 2005(C’wth) (BCII Act 2005) to establish the Office of Australian Building and Construction Commissioner (ABCC) on 1 October 2005. The primary responsibility of the ABCC was to ensure workplace laws were upheld in the construction industry to ensure building work was carried out fairly, effectively and productively for benefit of all industry participants and Australian economy as a whole. Third, the Building and Construction Industry Forum (BCIF) was established to ensure compliance with tax laws. This theme examines the role of accounting as a legitimising system.
1.5 Research Method

1.5.1 Overview

The research epistemology is constructivist. The aim is to reconstruct the reality or truth of the role of accounting practice in repairing or legitimising the breach of the societal contract within the construction industry. The research design is a single descriptive case study using historical narrative. The unit of analysis adopts an embedded design, which is multiple units of analysis within a single case study because, while the primary focus is on the construction industry as a whole, this study examines differences between stakeholders in terms of their compliance with the societal contract. Two main sources of evidence are used: documents from the construction industry and archival records. The analytical technique is explanation building by using Content Analysis (CA) guided by Critical Discourse Analysis (CDA). CA and CDA are appropriate because the main source of evidence is text, the RCR, and the best way to examine the research themes is via the communication within this text.

Figure 1.1 presents the overall framework for this study. On the left hand side it identifies the theoretical frameworks used to interpret the data. Next is theme 1 which covers the period up to and including the RCR in 2003. It examines the nature of the social contract breach and accounting’s role. Next is theme 2 which covers the period after the RC. It examines the legitimisation process and accounting’s role in helping the industry find legitimacy, that is, fill the legitimacy gap. On the right side is the data analysis methods and the specific accounting work practices examined by this study. The list of activities is taken directly from the findings of the RC. In reconstructing the social reality of accounting in the
construction industry, this study examines how each of these activities were undertaken and the role accountants played. Given that the RC found these activities to be evidence of unlawfulness by the industry, it is then possible to assess accountants’ degree of cooperation with this behaviour by establishing their level of involvement in these activities.
Figure 1.1: Overall Thesis Framework: Accounting’s Role in Legitimisation of the Australian construction industry
1.5.2 Research Setting

The subject of this study is the construction industry; more specifically firms engaged in residential and non-residential construction. Chapter 3 provides an analysis of this industry. The principle research data will be gathered from extensive secondary sources, most especially the 23 volumes of the RCR. This study is a reconstruction of reality based on the publicly information available. It is a historical recount. It does not promise to discover the truth of accounting practice in the construction industry in the period under review. This is not a study of forensic accounting. It is an historical narrative examining the role of accounting. Given the nature of the focus of this study, there has been no attempt to include contributions from those who worked in the industry, other than the evidence they provided to the RC. Human nature suggests it would be very unlikely individuals would admit to inappropriate conduct and, therefore, non-compliance with the social contract would be impossible based on an interview method. Fortunately, the RC was a major public enquiry and produced a very significant volume of data, and the industry’s social contract breach has meant it has been heavily regulated since the RC. This means that the research strategy will focus on ways to extract the most accurate representation of the truth, measured by the accuracy of the social construction of the reality of behaviour from the industry’s social actors, from these secondary sources.

The large amount of data which is publicly available provides the detail necessary for such a thick description of the social reality of behaviour within the construction industry. There are 23 volumes of the RCR, company annual reports, industry regulator reports, and industry analyst reports. CA was chosen to examine “words, meanings, pictures, symbols,
ideas, themes or any message that can be communicated” (Neuman 2006, p. 322). The data available for this study contains hundreds of thousands of pieces of content.

1.5.3 Data Analysis

Given the significant amount of textual data, for example, in the RCR, it was decided to use CA because it is appropriate for analysing the content of text. CA lets a researcher identify the messages and meanings in a source of communication, for example, reports (Neuman 2006, p. 323). CA enables content to be compared and analysed using coding techniques. It can also reveal aspects of the text’s content that are non-obvious or difficult to see (Neuman 2006, p. 323). The question then is to determine what you are trying to analyse and reveal. CA generally tries to measure frequency, direction, and intensity of communication (Neuman 2006, p. 325). This can be extended to consider the source (who), encoding (why), channel (how), message (what), recipient (to whom), and the decoding process (to what effect) (Holsti 1968). To further reconstruct the reality of the construction industry, CDA is used to code the meaning in the messages within the RC text. CDA aims to uncover the embedded meanings in everyday rhetorical discourses that point to beliefs, ideologies, and values of a social community (Brummett 2008). CDA provides additional meaning within a text.

CA and CDA are used explicitly in chapters 3 and 4 to show the nature of the construction industry’s breach of the social contract and the regulator’s response. An example is table 4.2: Critical Discourse Analysis of Selected Themes from the ABC Four Corners Transcript (see chapter 4). The coding used to apply CDA to texts (such as in table 4.2) was developed from Gee (2011). Gee (2011) recommended using the following codes to reconstruct social
reality based on text analysis, in other words, to discover what the social context in the documents really means. The codes were: significance, practices (activities), identities, relationships, politics, connections, and sign systems and knowledge. The coding in table 4.2, for example, used Gee’s (2011) definition of these codes to apply to the text of the ABC Four Corners Transcript to classify meaning within each theme. For example, under the theme Explicit Social Contract Expectations and the topic of industrial relations, the CDA coding describes the identity of union leaders as villains and relationships based on collusion.

The study also uses Social Network Analysis (SNA) to examine the nature of the construction industry’s political economy. SNA is a technique used in the social sciences to analyse social interaction at work. Given the importance of understanding cultural behaviour in this study, SNA provides a framework for analysing how the construction industry stakeholders interacted. It also allows us to understand the role of accountants in terms of their social interactions with other stakeholders. A recent article identified research opportunities opened by SNA’s perspective on accounting and auditing regulation (Richardson 2009). Therefore, SNA is used in this study to apply ST to understand the pressures placed on accountants by other construction industry stakeholders.

SNA is used explicitly in chapters 5 and 6. First, SNA is used to classify social behaviours into broad themes. Each of the unlawful activities identified by the RC were analysed and coded into broad themes. These are listed in table 5.1 in the middle column (see chapter 5). The themes are descriptions of the main types of unlawful behaviour found after analysis of each of the seven unlawful activities (listed in the first column). Each theme was then coded into one of the three theoretical lenses used in chapter 5, that is relationships, impact,
or expectations. Coding was done by assessing each theme and the type of social behaviour it describes, against the definition of the construct. This method is an example of grounded theory, which is ‘a qualitative research method that uses a systematic set of procedures to develop an inductively derived theory about a phenomenon’ (Neuman, 2006, p. 60). The codes, therefore, were induced from analysis of the data presented in this chapter. The procedure was to look for similarities, that is, themes, across ‘unlike phenomena’ (Neuman, 2006, p. 60), which in this case was the thesis data which was based on numerous sources, for example the RC volumes and other documents, and often different case studies and contexts. This grounded theory approach enabled theory to emerge from the data, in this case it was themes of unlawful behaviours (middle column) associated with activities (left column) and explained by one of the three ST constructs used in this analysis. The table illustrates the range of social behaviours associated with each activity. The outcome of this analysis was then used to organise the historical narrative in the rest of this chapter. The method enables generalizations by making comparisons across social situations. These are later linked to accountants’ behaviour in section 5.3. The activities and themes were combined into their relevant lens.

Second, SNA was used to examine three dimensions of ST, (1) relationships, (2) impact, and (3) expectations (Gray, Owens & Adams 1996, p. 45). The objective with this operationalisation is to test whether these ST constructs may help predict stakeholder behaviour in terms of willingness to meet the social contract. The first operationalisation is relationships. Relationships may be defined by SNA. SNA allows us to measure interaction between stakeholder groups in terms of network quality (depth of contact) and network structure (number of contacts and frequency of contact) (for example, Stone 2001). The
second operationalisation is impact. Impact may be defined in terms of management’s willingness to listen to various stakeholder groups and adjust their behaviour accordingly. It measures the power or level of influence of each group. The third operationalisation is expectations. Expectations may be defined in terms of the social contract for each stakeholder group. It answers questions about what each of the groups listed in figure 2.1 (see chapter 2) expect of accounting, and how these expectations differ. The central theme with ST for this study is that the construction industry’s stakeholder groups will have different social contracts with the industry in terms of its accounting. This will be manifested in differences compared with the overall social contract, the RC, and between the expectations of the various groups.

To assist this analysis, the seven unlawful activities were examined to identify their business processes (see appendix 1). This method is a further example of grounded theory, which is ‘a qualitative research method that uses a systematic set of procedures to develop an inductively derived theory about a phenomenon’ (Neuman, 2006, p. 60) (see section 5.1 in chapter 5 for further explanation). Each process was then analysed in terms of:

1. Interaction. This is to identify the density of accountants’ social networks in each process. High density means frequent interaction with other stakeholders involved in the unlawful activity. Low density means infrequent or no interaction. This asks, how much were accountants invited to participate in this process? Codes were developed to describe the level of density:
   a. Lead: where the accountant interacts with others;
   b. Follow: where the accountant responds to requests for help from others; and
   c. Alone: where the accountant does the activity largely in isolation from others.
2. Harmony. This is to identify the heterogeneous (inclusiveness) accountants’ social networks in each process. Heterogeneity means accountants’ views were welcomed by other stakeholders. Homogeneity means accountants’ views were unwelcome. This asks, how much were accountants asked for their opinion in this process? Codes were developed to describe the level of heterogeneity as follows:
   a. Respect: where accountants were valued; and
   b. Tolerance: where the accountant was entitled to participate.

Codes were developed to describe the level of homogeneity, as follows:
   a. Outsider: where secrets are held from the accountant; and
   b. Enemy: where the accountant is denied any contact with other stakeholders.

3. Cohesion. This is to identify the democracy of accountants’ social networks in each process. High cohesion means shared control with other stakeholders involved in the unlawful activity. Low cohesion means no shared control. This is to examine how much were accountants’ opinions listened to. Codes were developed to describe the level of democracy, as follows:
   a. Expert: where the accountant’s opinion matters more than any others; and
   b. Advisor: where the accountant only offers advice

Codes were developed to describe the level of non-democracy, as follows:
   a. Challenged: where the accountants views would be disputed; and
   b. Ignored: where the accountant has no influence at all.

The codes were induced from the data using a grounded theory method. The procedure was to look for similarities across the behaviours to enable generalizations about the social behaviours. The code descriptors are based on the macro-level explanation of the micro-
level events (Neuman, 2006, p. 60) described in the historical narrative which follows. The descriptors were guided by SNA theory of interaction, harmony and cohesion (see section 5.2.3.1). Further explanation is provided below.

Interaction: density is used to examine the interconnectedness of social networks; individuals with high density scores are connected with more than one social network (Stone 2001; Anklam 2005). Density is a positive factor in social networks because it measures frequency of interaction. The more density, the more opportunity to build and maintain relationships, which results in increased communication, trust, and social dependency. In contrast, low density indicates separateness, which results in isolation, mistrust, and conflict. The analysis identified the network density, that is, the connectivity between stakeholder groups. It also highlights differences in density amongst stakeholders, that is, which groups were well connected and which were not.

The interaction codes developed to describe accountants’ social behaviour were lead, follow, and alone. They describe levels of interaction with other construction industry stakeholders in terms of decreasing density. ‘Lead’ describes accountants playing a pro-active role where they seek interaction with others and, therefore, assume a principal role in the social network associated with that activity; often because they are the employee most responsible for performing the activity or the subject matter expert. ‘Follow’ describes accountants playing a reactive role where they respond to requests from others to interact and, therefore, assume a subservient role in the social network associated with that activity; often because others are decision makers and only involve accountants to provide advice or when otherwise necessary. ‘Alone’ describes accountants as being excluded either voluntarily or involuntarily from the social network associated with that activity; usually
because decision makers do not want accountants to be involved (perhaps hiding something) or the accountant prefers to do a part of the activity in isolation from other associated work (perhaps because they do not want to know what is happening).

Harmony: indicates tolerance and respect between stakeholder groups. If inclusive (heterogeneous), the social network welcomes different types of members and is tolerant of different views, if exclusive (homogenous), it allows membership only to people who are similar (Stone, 2001). Heterogeneity is a positive factor in social networks because it identifies the subjective nature of diversity in opinions. The more heterogeneity, the more tolerance and respect for different stakeholders. This results in ethical behaviour in terms of harmony. However, if relationships were characterized by fragmentation and discord, generated by inequality, repression, and exclusion, then the industry would demonstrate unethical social behaviour. This unethical behaviour will be explained by Managerial perspective of ST.

The harmony codes developed to describe accountants’ social behaviour were respect, tolerance, outsider, and enemy. The first two codes were heterogenous themes. This illustrates positive social behaviour where accountants were respected or at least tolerated by the social networks associated with the activity. This behaviour is about the role of the accountant and their right, as subject matter experts, to be involved. They are levels of inclusion; with respect being the most positive, and tolerance is still being included but less positive. This supports ST’s ethical perspective. On the other hand, the latter two codes were homogenous themes. This was negative social behaviour where accountants were seen as outsiders or even the enemy. This behaviour is about the accountant being seen as a threat or a barrier to conducting a work activity they may not approve of. They are levels of
exclusion; with enemy being the most negative, and outsider still negative but less so. This supports the Managerial perspective of ST.

Cohesion: indicate efficient teamwork. This analysis is looking for the extent to which a network membership is democratic; if democratic, decisions will be taken horizontally; if non-democratic, decisions will be taken vertically (Anklam 2005). Democracy is a positive factor in social networks because it helps in controlling the activities. The more shared control within the network, the more efficient the group is because it allows divergent thought, creativity, and innovation; which ultimately results in ethical behaviour in terms of cohesion.

The cohesion codes developed to describe accountants’ social behaviour were expert, advisor, challenged, and ignored. The first two codes were examples of democracy. This illustrates positive social behaviour where accountants assumed high socio-political status within the social networks associated with the activity. This behaviour is about the power of accountants and their capacity to control the behaviour of others within the network. They are levels of participation; with expert being the most positive, and advisor is still being a major role but with less influence. This supports equality and gives accountants the opportunity to have a strong influence on the network’s behaviour. On the other hand, the latter two codes were non-democratic themes. This illustrates negative social behaviour where accountants assumed low socio-political status within the social networks associated with the activity. This behaviour is about the lack of power of accountants and their inability to control the behaviour of others within the network. They are levels of non-participation; with ignored being the most negative, and challenged is still being a weak participant but slightly more influential. This encourages inequality and denies accountants
the opportunity to influence the network’s behaviour. The coding in table 5.2: Accountants’ Behaviour in Construction Industry Social Networks, is an example of the results of this coding method.

1.6 Contribution of the Study

The study makes several contributions. In reconstructing the reality of accounting practice in the construction industry the study provides an historical narrative regarding whether accounting’s role is objective and rule-based or subjective and open to interpretation. This contribution is grounded within critical accounting perspectives.

The social reconstruction of accounting in this industry also provides an opportunity to contribute to the existing body of literature in several areas. It includes SNA theory to extend our understanding of ST. SNA is used to examine the industry culture which was the cause of the construction industry’s unlawfulness. Organisational culture theory was identified by Dent (1991) as a new field of enquiry enabling the construction of a new reality of accounting practice. Gaffikin (2008, p. 128) states that “there is little doubt that accounting practices, as socially defined activities, are greatly affected by culture”. However, he is critical of definitions of culture, particularly Hofstede’s measures of national culture (see Gaffikin 2008, pp. 217-218), and he argues that “it is not possible to prescribe fixed dimensions as to how culture impacts on those (accounting) practices”. Gaffikin (2008) argues that we cannot rely on extant simplistic cultural dimensions and that to understand the impact of culture on accounting practice, we need a “much broader compass”. Deegan (2003, p. 520) agrees that “determining the validity of decision making
across different cultures would be an important area for future accounting research”. While this discussion is of national culture rather than industry culture, the same opportunities exist given accounting operates within a socially constructed context. Organisational culture is the set of shared values and norms that control organisational members’ interactions with each other and with customers’ suppliers, customers, and other people outside the organisation (Jones 2004, p. 195). Little is known about the way in which accounting is implicated in the culture of organisations (Dent 1991). SNA theory provides a lens to examine this topic.

The thesis also addresses the nature of the legitimacy gap, and particularly the difference between actual and desired cultural behaviours. The RCR found that the construction industry had a deeply embedded organisational culture based on coercion, intimidation, and bending the rules, which meant that many industry activities did not follow accepted standards; for example fair work practices, workplace relations, occupational health and safety, and recruitment. The RC establishes the legitimacy gap in the construction industry; in terms of actual and desired behaviour. The study also tracks the response to the RC in 2003 to look at the legitimisation process in terms of how the legitimacy gap was addressed. This connects with the main contribution, the role of accountants, by examining whether accounting played a role in the legitimisation of this industry.
1.7 Chapter Summary

This chapter has introduced the thesis. Chapter 2 discusses the methodology, literature and public interest. Chapter 3 examines the nature of the construction industry, while chapter 4 describes the history of the regulation of the construction Industry. Chapter 5 assesses the relationships between the construction industry’s stakeholders, and chapter 6 looks at the impact of power and politics on the relationships between stakeholders and how the expectations of society were affected. Chapter 7 provides suggestions for changing the construction industry’s unlawful behaviours based on the research findings, and chapter 8 describes conclusions.
CHAPTER 2: METHODOLOGY AND THEORETICAL FRAMEWORK

2.1 Introduction

This chapter explains the research methodology used to conduct this study and its theoretical framework. The research is an historical narrative of the construction industry in the period 2003-2011, with a primary focus on the period surrounding the RC into the industry and its immediate aftermath (2003-2005). The data collection, analysis, and reporting uses CA; as well as CDA. CA is a “technique for compressing many words of text into fewer content categories based on explicit rules of coding” (Stemler 2001, p. 55). The study focuses mainly on the text contained in the Construction Industry RC (Cole 2003) and the BIT Reports (2004; 2005); along with other publicly available information on the industry and its behaviour. CDA is used to examine the societal and political themes emerging from the CA coding categories. The outcomes of the CDA will be examined from a critical accounting perspective, with a particular emphasis on PIT, and stakeholder and LT.

2.2 Research Methodology

2.2.1 Introduction

The selection of a research methodology involves a number of steps. The first step is to decide whether to adopt a qualitative or quantitative approach. Silverman (1993) makes the
important distinction that social sciences research has two schools: one oriented towards the quantitative testing of theories, and the other directed at qualitatively developing theories. This study aims to contribute to CAT; more specifically the social reconstruction of the role of accounting. Therefore, a qualitative approach is justified.

The second step in the selection of methodology is to decide on the research philosophy or epistemology. Some organisational behaviour is so complex that one cannot find objective knowledge of reality, one can only represent it, that is, construct it (Girod-Seville & Perret 2001, p. 17). The complexity is caused by the nature of the social world under study whose reality is defined by interpretations of the social actors of their interactions to create a shared meaning, which is at the root of the “social construction of reality” (Berger & Luckman 1966, p. 17). Following the principles of a qualitative social construction of reality, it is accepted that discovering the truth behind the construction industry’s behaviour which led to the RC would be very difficult. Although, respondents can be asked in an interview to explain why their behaviour was non-compliant or perhaps unlawful, it is unlikely a respondent will provide a response or a truthful response. Given the nature of this study, therefore, it can only seek to reconstruct the reality of the industry’s behaviour via information which may be publicly accessed.

Fortunately, the RC was a major public enquiry and produced a very significant volume of data, and the industry’s breach of the social contract has meant it has been heavily regulated since the RC. This means that the research strategy will focus on ways to extract the most accurate representation of accounting practice, measured by the accuracy of the social construction of the reality of behaviour from the industry’s social actors, from these secondary sources. Critical accounting researchers have argued the need for a constructing
of accounting reality as a subjective rather than objective process (for example, see Morgan 1988). Therefore, a constructivist epistemology has been chosen.

2.2.2 Research Design

The third step in the selection of research methodology is to decide on research strategy. The research design is a case study based on historical narrative. Case study research “is an in-depth examination of an extensive amount of information about very few units or cases for one period or across multiple periods of time” (Neuman 2006, p. 40). Case study methodology is used as the research design because it is suitable for studying complex social phenomena within a single industry. The study includes characteristics suitable for case study enquiry, namely: many variables of interest including whether accounting is objective or subjective, the nature of the legitimacy gap, and accounting work practices (see figure 1.1 in chapter 1); multiple sources of evidence (multiple government and industry reports); and theoretical propositions (themes in this study) to guide the collection and analysis of data (Yin 1988).

2.2.3 Research Technique

The case study was analysed using the broad framework presented by figure 1.1 in chapter 1. There are two general analytic strategies used to analyse case study data:

1. Relying on theoretical propositions: theoretical orientation guiding the analysis; following theoretical propositions that have formed the design of the case study. This helps to focus attention on certain data and to ignore other data

2. Developing a case description: a descriptive framework for organizing the case study; analysis organized on the basis of description of the general
characteristics and relations of the phenomenon in question (Yin 1994, pp. 103-105).

This study adopts the first analytical strategy to provide theoretical direction. The RCR and the other documents contain a very significant volume of information. In order to find explanatory meaning in this data and for research efficiency purposes, the theoretical frameworks outlined in figure 1.1 in chapter 1 act as a lens to focus on the most relevant information in the reports. More specifically: PIT establishes the nature of the social contract; ST guides examination of the nature of the legitimacy gap; and LT helps identify the process of changing behaviour after the RC in 2003.

Given the case study happened in the past, it lends itself to historical analysis. Historical research plays an important role in developing general explanations and can substantiate the emergence and evolution of tendencies over time (Neuman 2006, p. 433). However, social science researchers can be critical of historical research. There seems to be three main criticisms:


2. Cognitive bias. Historians do not use all of the information available to them; rather they select evidence which suits their purpose. This means that the reader cannot know what information was excluded which might have been relevant (Neuman 2006, p. 434). Similarly, historians tend to focus on people rather than events, which focuses the research on micro-level issues rather than macro-level (Neuman 2006, p. 434).
3. Evidence. Historians organize evidence in a sequential manner, that is, a historical narrative, to tell a story. “This compounds problems of undefined concepts and the selection of evidence” (Neuman 2006, p. 434).

Narrative is the “pattern and structure of life where events occurred not just in succession but with the order of events giving meaning to those which were previous and those subsequent” (Funnell 1998, p. 143). In this way, narrative should not just tell a story by explaining what happened and what happened next, rather it should provide meaning to those events by using analysis to examine the sequential connections. In contrast, critics see narrative as more myth than historical fact due to the focus on individuals and the focus on ‘interesting’ events to the exclusion of the normal. The debate appears to focus on the need to reconstruct an objective social reality or truth rather than a subjective version of reality.

The criticisms of historical narrative in accounting research can be quite controversial. Funnell (1998) was one of the most influential proponents of the new accounting history method as an alternative to traditional accounting history. The debate appears to centre on the messages or meaning which may be gained from interpreting a body of text. Deconstructionists argue the need to be sensitive to the text’s content and context, or the method of presentation (Funnell 1998). Neuman (2006, p. 435) summarises this debate in terms of the characteristics of the narrative form and its strengths and weaknesses. Table 2.1 presents Neuman’s summary with comments on how these issues are addressed in this study.
### Table 2.1: Historical Narrative - Critique of Methodology

<table>
<thead>
<tr>
<th>Characteristics</th>
<th>Critique</th>
<th>Response</th>
</tr>
</thead>
<tbody>
<tr>
<td>1.</td>
<td>It tells a story, with a plot, climaxes</td>
<td>This gives the study a natural structure but the main focus is on<em>explaining</em> what happened, rather than describing what happened</td>
</tr>
<tr>
<td>2.</td>
<td>It follows a chronological order and sequence of events</td>
<td>This is used by looking at what happened prior to the RC, the RCR, and the response after the release of the reports</td>
</tr>
<tr>
<td>3.</td>
<td>It focuses on specific individuals, not on structures or abstract ideas</td>
<td>Here a different approach is adopted, rather the focus is on conceptual structures, the breach of social contract.</td>
</tr>
<tr>
<td>4.</td>
<td>It is primarily particular and descriptive, not analytic and general.</td>
<td>Here a different approach is also used. The aim is not to tell the story of the construction industry, rather the focus is on a very specific analytical lens, that is, the role of accounting in legitimising the industry.</td>
</tr>
<tr>
<td>5.</td>
<td>It presents its events as unique, unpredictable, and contingent.</td>
<td>The study does have these characteristics. While there have been other industries involved in royal commissions, it is uncommon and the level of unlawful behaviour in the construction industry was unique.</td>
</tr>
</tbody>
</table>

**Strengths**

1. It is colorful, interesting, and entertaining  
The unlawfulness of the construction industry is a fascinating story. For accounting, it represents an excellent opportunity to examine the objective versus subjective role debate.

2. It gives a sense of life in a different era  
While the RC was not long ago, a little more than a decade, the cultural behaviours which created the industry-wide unlawfulness evolved over many decades. It created a sense of ‘this is the way we do things’ which is fascinating in itself. Why was there such widespread acceptance of unlawfulness? And how did accountants respond to that culture? It leads us to question whether the level of unlawful and inappropriate behaviour would be tolerated today.
### Table 2.1: Historical Narrative - Critique of Methodology

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<th>Critique</th>
<th>Response</th>
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<tbody>
<tr>
<td>3. It communicates the way people in the past experienced reality and connects emotionally with these people</td>
<td>From an accounting perspective, it creates an empathy with the pressures these people must have been placed under by the various stakeholders. It makes us question how we would respond to these pressures ourselves. Given the employment relationship accountants had with stakeholders who misbehaved, it forces us to consider what lengths people will go to in order to protect their job: an emotional issue which connects with all of us.</td>
</tr>
<tr>
<td>4. It surrounds individuals and events with a mix of social reality</td>
<td>While the focus is not on individuals, they are grouped as stakeholder groups to reconstruct the social reality of their interactions.</td>
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</table>

**Weaknesses**

<table>
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<tr>
<th>Weakness</th>
<th>Response</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. It hides causal theories or concepts or leaves them implicit.</td>
<td>This is not done. Rather, theoretical concepts are explicitly used to reconstruct the social reality of the industry. The historical narrative is framed by the concepts. The analysis gives structure to the narrative.</td>
</tr>
<tr>
<td>2. It uses rhetoric to persuade and is subject to logical fallacies.</td>
<td>The use of CA and CDA adds depth to the analysis and the presentation of the findings, thereby avoiding logical fallacies.</td>
</tr>
<tr>
<td>3. It tends to ignore the normal for the unique or dramatic.</td>
<td>There is so much information in the documents being investigated by this study that it must be selective in what is analysed and reported. The structure provided by the conceptual framework and the rigor of the research techniques, that is, CA and CDA, ensures the focus is on the material with most relevance to the study.</td>
</tr>
<tr>
<td>4. It rarely builds on previous knowledge and does little to create general knowledge.</td>
<td>The theoretical framework (see figure 1.1 in chapter 1) ensures that the study remains focused on advancing our knowledge about the role of accounting practice, with a particular emphasis on legitimacy. This ensures that the study does not degenerate into a story of what happened.</td>
</tr>
<tr>
<td>5. It tends to focus on individuals and their ability to shape events.</td>
<td>This is not done. Rather the focus is on groups of individuals, that is, stakeholder groups.</td>
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</table>
The table shows that the study has adopted in particular three of the five characteristics of historical narratives: first, it tells a story, with a plot, climaxes, secondly, it follows a chronological order and sequence of events, and thirdly, it presents its events as unique, unpredictable, and contingent. In addressing the debate over historical narrative, proponents of new accounting argue that the ‘counter-narrative’ is a means to generate meaning and convince, thereby advancing the body of knowledge on the topic under investigation (Funnell 1998). It does this by connecting the phenomena under investigation, in this case accounting practice, with the wider social, economic, and institutional contexts, in this case the construction industry’s breach of the social contract. In making these ideas operational, translating them into action, Loft’s (1986) position that accounting must be considered as an activity which is both social and political in itself is adopted. This means that the ways that accountants practice and produce outcomes, for example accounting reports, allows them to engage with others, in this case stakeholders. Accountants have an impact on others in terms of the ways in which the accounting information is used. Therefore, this discussion about counter-narrative may be translated into research technique by examining the interactions between accountants and stakeholders from the historical content of the RCR and the other documents investigated by this study.

This study uses the counter-narrative method broadly by applying CAT as the main theoretical lens, analysing the documents via this lens, and using CA and CDA to reconstruct the social reality of the construction industry’s behaviour.
2.2.4 Analytical Techniques

The study adopts two techniques to analyse the research data gathered: CA and SNA. CA is supported by a further technique called CDA. CA is used to make sense of the text data analysed for this study. SNA is used to examine the social interactions of the industry stakeholders.

CA is a methodology for gathering and analysing the content of text (Neuman 2006, p. 322). The methodology allows a researcher uncover the messages and meanings in a source of communication, such as a book, article, movie, and perceive content in a different way to the ordinary way of reading or watching (Neuman 2006, p. 323). CA has been used for more than a century and across many fields (Neuman 2006, p. 322), including in recent accounting research (for example, see Dellaportas, Senarath Yapa & Sivanantham 2008; Breton 2009; Brandau & Hoffjan 2010; Crofts & Bisman 2010; Vafaei, Taylor & Ahmed 2011). Structured observation of text, using written rules, is enabled by CA. These rules provide the structure to the measurement and coding of the content. By following the CA rules, the researcher ensures they are using the method properly. This also gives the reader confidence in the validity and reliability of the results. The CA rules are:

1. Frequency: counting how many times a word or code is mentioned.
2. Direction: message is positive versus negative, supporting or opposing.
3. Intensity: the strength or power of a message.
The following table shows fifteen general purpose uses of CA, the element of the communication paradigm to which they apply, and the question they are intended to answer.
<table>
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<th>Purpose</th>
<th>Element</th>
<th>Question</th>
<th>Use</th>
</tr>
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<tbody>
<tr>
<td>Make inferences about the antecedents of communications</td>
<td>Source</td>
<td>Who?</td>
<td>• Answer questions of disputed authorship (authorship analysis)</td>
</tr>
</tbody>
</table>
| Encoding process | Why? | • Secure political & military intelligence  
• Analyse traits of individuals  
• Infer cultural aspects & change  
• Provide legal & evaluative evidence |
| Describe & make inferences about the characteristics of communications | Channel | How? | • Analyse techniques of persuasion  
• Analyse style |
| Message | What? | • Describe trends in communication content  
• Relate known characteristics of sources to messages they produce  
• Compare communication content to standards |
| Recipient | To Whom? | • Relate known characteristics of audiences to messages produced for them  
• Describe patterns of communication |
| Make inferences about the consequences of communications | Decoding process | With what effect? | • Measure readability  
• Analyse the flow of information  
• Assess responses to communications |

(Source: Purpose, communication element, and question from Holsti (1968). Uses primarily from Berelson (1952) as adapted by Holsti (1968))
According to Krippendorff (2004), six questions must be addressed in every CA:

1. Texts: Which data are analysed and how is this rearticulated? Texts occur in the analyst’s world but their origins in the world of others must be acknowledged.
2. Research questions: the targets of the analyst’s inferences from available texts. By starting content analysis with research questions before making any enquiries, efficiency and empirical grounding is enabled.
3. Context: specifies the world in which texts can be related to the analyst’s research questions. The analyst needs to make their context explicit, and it is usually their theoretical perspective.
4. Analytical constructs: operationalize what the analyst knows about the context; specifically the explanations of how the texts are connected to possible answers to the research questions, and the conditions under which these connections might change.
5. Inferences: these emerge in the analysts coding the texts, the analytical procedures, and sometimes after the analysis has been applied. There are deductive inferences: logical generalizations, inductive inferences: are generalizations from smaller samples to similar kinds of larger populations; and abductive inferences: applying from one set of particulars to another. This is the type most relevant to content analysis.
6. Validating evidence: while content analysis can be difficult to replicate, it is helpful if a content analysis can be validated in principle. The aim is to give a sense of reliability and repeatability within the constraints of abductive inferences (pp. 29-40).

The assumption is that words and phrases frequently mentioned are those reflecting important concerns in every communication. Quantitative CA begins with word frequencies, space measurements, time counts and keyword frequencies. “Content analysis is a research technique for making replicable and valid inferences from texts (or other meaningful matter) to the contexts of their use” (Krippendorff 2004, p.18). To extend CA, CDA is used to provide additional structure to the analysis of the meaning in the document text under investigation in the thesis.

CDA was first developed by the Lancaster school of linguists of which Norman Fairclough was the most prominent figure. Fairclough developed a three-dimensional framework for
studying discourse, where the aim is to map three separate forms of analysis onto one another. This involved analysis of (spoken or written) language texts, analysis of discourse practice (processes of text production, distribution and consumption) and analysis of discursive events as instances of sociocultural practice (Fairclough 1995). The analysis is at the micro, meso and macro-level of interpretation. At the micro-level, the researcher considers the text’s syntax and metaphoric structure. The meso-level involves studying the text’s production and consumption, focusing on how power relations are enacted. At the macro-level, the researcher is concerned with inter-textual understanding, trying to understand the broad, societal currents that are affecting the text being studied (Fairclough 1995). In this way, this study is able to code the text in the RCR which is associated with cultural dimensions asking who, why, what type questions. This will elevate the analysis from descriptive to explanatory case study analysis as the CA framework is used to reconstruct the reality of cultural behaviour within the construction industry. The following CDA framework adapted from Gee (2011, pp. 121-122) is used to complete the reconstructions:

1. **Significance**: language may be used to signal that something is more or less significant or important. This is used to code node attributes by asking this CDA question: how is this language being used to make certain things significant or not?

2. **Practices (activities)**: language may be used to get things done. This is used to code node attributes by asking this CDA question: what practice or activity is this language being used to enact?

3. **Identities**: language may be used to explain roles, which is particularly important in this thesis from a ST perspective. This is used to code node attributes by asking this
CDA question: what identity or role is this language trying to get others to recognise?

4. Relationships: language explains the relationship we have, want to have, or are trying to have with others. It is another very important concept for the thesis’s stakeholder analysis. It introduces the notion of deference and of power differentials in relationships. This is used to code node attributes by asking this CDA question: what sort of relationship is this language trying to create with others?

5. Politics: language may be used to assign value judgments about others which allocates them status. This is used to code node attributes by asking this CDA question: who or what is being assigned values of being normal, right, good, correct, proper, appropriate, valuable, the way things ought to be, high status – and the inverse of each of these labels.

6. Connections: language may be used to link things that are not normally connected. This is used to code node attributes by asking this CDA question: how does this language connect or disconnect things or make something relevant or irrelevant?

7. Sign systems and knowledge: language may also be abstract and include symbols or jargon. This is used to code node attributes by asking this CDA question: does this language privilege or disprivilege certain technical or jargon groups?

SNA was introduced by Granovetter (1973) who used it as a tool to link macro and micro levels of sociology theory. Granovetter felt that existing network analysis focused mainly on interactions within well-defined small groups, that is, micro level analysis. However, there was a need to examine interactions ‘between’ groups, that is, macro level analysis, as well as ‘within’ groups (micro level). He differentiated this in terms of strong ties and weak
ties. One of the criticisms of network analysis has been that it lacks sufficient measurement tools (see Granovetter 1973). Granovetter pioneered the notion that SNA, at the macro level, can identify political organisation and social cohesion, themes which are particularly relevant to this study.

Where SNA can enhance ST and make an important contribution in this study is in providing contextual and systemic understanding of the interaction between the construction industry’s stakeholders. Borgatti and Foster (2003, p. 991) explain that SNA has evolved to include more predictive power “including direction of causality, levels of analysis, explanatory goals, and explanatory mechanisms”. They explain how recent SNA studies have focused on network consequences and have classified the literature into “four canonical types: structural social capital, social access to resources, contagion, and environmental shaping” (Borgatti & Foster 2003 p. 991). Social access to resources connects with LT in terms of organisations being granted access to resources in exchange for legitimate behaviour. Similarly, environmental shaping connects with LT in terms of legitimacy tactics, the actions and interactions of stakeholders to repair legitimacy.

Therefore, SNA might help the explanatory power of ST analysis by mapping the interactions of the construction industry’s stakeholder groups and connecting these interactions with their motives; social access to resources, contagion, and environmental shaping. However, an obvious problem for this study in using SNA is that it commonly uses statistical analysis, largely based on survey data. The study does not have access to survey data and, therefore, must infer SNA data based on qualitative interpretation of stakeholder relationships using publicly available data. The ways that this study applies a
theory usually requiring quantitative data to qualitative data is a further methodological contribution.

SNA allows measures of social quality and social structure. The first SNA construct is network structure. It is measured by four factors: network size, having lots of contacts and that are well connected; density, access to multiple social networks; heterogeneity, willing to accept different people and views into their group; and constraints, group decision making is democratic and effective (see Stone 2001; Anklam 2005). The structural measures are based on measuring connections. Survey respondents are typically asked whom they connect or interact with, that is, nominate their “ties”. In this way, network structure measures social relationships in terms of an individual’s connectivity and frequency of interaction: how many people do they know and how often do they talk.

The second construct is network quality. It is measured by six factors:

- tie importance, know important people and have a strong network position or even power as a result;
- corporate leadership, have a degree of influence within social networks or seen as a politician or activist;
- volunteering, have a degree of popularity within social networks or seen as a generous person;
- mentoring, have leadership status within social networks or seen as a wise person;
- social dependence: have durability within social networks or seen as a necessary person; and
- reciprocity or willing to give and receive from others (Stone 2001; Anklam 2005).
The quality measures are based on measuring the strength of relations. Survey respondents are typically asked about the nature of their relationship with others and also about how others’ perceive them. In this way, network quality measures social relationships in terms of an individual’s social influence and status: do they know the ‘right’ people and are they seen as a networker.

This discussion shows how SNA cannot be used in this study at a micro level because individuals cannot be surveyed to measure their social capital in terms of network structure or quality at the time of the RC. However, inferences may be made at the macro level interaction, the strength of weak ties, using some of the conceptual frameworks outlined above. While interactions cannot be analysed in statistical terms, conclusions may be drawn about the strength of the relationships between the stakeholder groups, as opposed to individuals, using network structure and network quality as guiding ideas. The results will be presented in chapter 5. For example, conclusions may be drawn about network structure measurements such as (a) heterogeneity: willing to accept different people and views into their group; and (b) constraints: group decision making is democratic and effective, from the document text using CDA to find meaning and interpretation from the language used. This broad way may be used to identify macro level political-social differences between the stakeholder groups. As Borgatti and Foster (2003, p. 991) explain, this approach is validated by fields which use SNA to analyse document text, such as “literary criticism, in which consideration of literary works as self-contained immutable objects has given way to seeing texts as embedded in a system of meaning references decoded by myriad interacting readers” (for example, see Kristeva 1980). The study will use SNA to draw qualitative
conclusions about the social interaction of accountants with other industry stakeholders, particularly in terms of their social network structure and network quality.

Given the large volume of data analysed by this study, CA and CDA are used explicitly in chapters 3 and 4 to show the nature of the construction industry’s breach of the social contract and the regulator’s response. Chapters 5 and 6 then apply SNA to three dimensions of ST, (1) relationships, (2) impact, and (3) expectations; and CA and CDA are used more implicitly, otherwise the narrative would have become too mechanical and the analytical technique would have got in the way of the story being told.

2.3 Theoretical Framework

2.3.1 Critical Accounting

The main theoretical lens for this thesis is CAT. This theoretical lens seeks to find the reality or truth about how accounting is practised within the context of its organisational setting. CAT views accounting as a social practice and its reality is found in the interactions between its various stakeholders. Yet as, Hopwood (1983, p. 287) stated “With accounting so intertwined with organisational functioning it is surprising that so little is known of the organisational nature of accounting practice”. A framework to examine this social reality is provided by CAT (Hines 1988). In the mid-1970s CAT emerged by researchers adopting a “critical perspective” about accounting practice. CAT is cross-disciplinary and has been influenced by a range of intellectual sources, particularly sociology. Some researchers have drawn on labour process theory or on political economy in the Marxist tradition (for
example, Cooper & Sherer 1984). Other researchers have been influenced by interpretative and interactionist sociology (for example, Tomkins, Groves, Abdel-Khalik, Ajinkya, Morgan & Willmott 1983). CAT has two themes that are particularly relevant for this study. The first is whether accounting can enact change leading to a better society (Laughlin 1999). The second is the debate over whether accounting is objective or subjective. Each theme is now examined.

The importance of social culture for the practice of accounting is widely acknowledged (Dillard, Rigsby & Goodman, 2004, p. 507). To change accounting practice requires not only social awareness but ultimately social change (Cooper & Sherer 1984, p. 222). CAT links understanding and change through the philosophy of praxis, whereby theory informs practice and existing practice informs theory (Roslender 2006, p. 264). This is achieved with the evaluation of existing practice aimed at changing and shaping accounting conceptually, institutionally, practically and politically (Tinker 2005, p. 101). Laughlin’s work on critical theory is used to solve real life accounting problems and examines accounting systems in organisations (Gaffikin 2006, p. 10). Laughlin (1999, p. 73) argues that there are four characteristics of critical accounting. First, critical accounting is always contextual and recognises accounting has social, political and economic consequences. Second, critical accounting seeks engagement to change or improve practice of the accounting profession. Third, CAT is concerned with micro (individuals and organisations) and macro (societal and professional) levels. Fourth, critical accounting is inter-disciplinary and engages and borrows from other disciplines. This study meets each of these criteria. On the inter-disciplinary criteria, the study uses SNA as a research method from the sociological discipline.
CAT can identify theories for changing the way accounting is practiced in industry and ultimately lead to reforms in how business and society operate (Deegan 2009, p. 530). CAT aims to identify the prevailing social arrangements within a community, such as an industry, within the broader context of the society in which it exists (Roslender 2006, p. 250). CAT aims to promote self-awareness of both “what is” and “what might be”, and how the former might be transformed to install the latter (Roslender 2006, p. 250). It is concerned with the promotion of a better society, and understanding the change processes necessary to achieve this goal. Therefore, it lends itself to examining the role of accounting in legitimising the construction industry.

CAT examines the social praxis involved in organisational change (Tinker 2005, p. 101). Social praxis envisages a broad understanding of both “theory” and “practice”, involving a two-way and perhaps circular relationship between the two, whereby theory influences practice and vice versa (Deegan 2009, p. 530). One implication of social praxis within the context of CAT is that theories need to change in response to changing social conditions. Well developed and empirically grounded theories may create impetus for changing the way accounting is practiced and ultimately lead to reforms in how business and society operate (Deegan 2009, p. 530). In this study, the aim is to understand the social reality of the interaction between the various social actors in the construction industry. By understanding how these actors or stakeholders behave and why, a theory of the antecedents associated with social contract breach at an industry level may be developed. This is the main explanatory dimension of this study, explaining why the breach happened.

In understanding the social interaction between the industry’s groups, it is necessary to distinguish between the traditional ‘partisan’ perspective, which views accounting as
objective or neutral, and critical accounting, where accounting is seen as a means of constructing or legitimising particular social structures (Deegan 2009, p. 531). In order to understand the social reality of accounting from a critical theory perspective, PET is used. This theory explains that the strategic outcomes of accounting practices favour specific interests in society and disadvantage others (Cooper & Sherer 1984, p. 208). The social praxis underlying the behaviour leading to the construction industry’s legitimacy gap may be explained by the differing interests of the social actors.

Traditionally, researchers have argued that accounting is objective and that it stands above all other organisational activity and acts as a type of guardian of the public interest. Accounting practice, therefore, is able to withstand the pressures exerted by the various stakeholders, for example owners, management, and maintains its integrity through application of accounting standards. On the other hand, critical accounting researchers argue that accounting practice is subjective because it is influenced by the social interactions within its organisational setting. In this sense, the thesis explores the objectivity versus subjectivity debate within CAT. It questions whether accounting acted as a watchdog over the construction industry, providing a sense of regulation within an otherwise unlawful culture. If it was not a watchdog, it suggests that accountants were unable to withstand the pressure of the organisational context and were dragged towards the industry’s culture of inappropriate and unlawful conduct, such as bending and even breaking the rules.

Traditional accounting researchers view accounting as “technical”. In Hopwood’s (1985, pp. 362 - 372) discussion, “technical” is variously linked with the terms “calculative”, “neutral”, “professional”, “uncritical” and the belief in “progress” and “efficiency”. 
Accountants in practice are presented as seeing the setting of accounting standards as a purely technical activity and claiming objectivity. Conventional academics are seen as viewing accounting as a factual and “objective form of knowledge” (Loft 1986, p.137). Textbooks are found to portray accounting as “a technical and neutral information service for decision making” (Hopper, Storey & Willmott 1987, p. 442). “Thus, a theme which runs through critical accounting is that conventional accounting espouses a technical perspective which typically stresses objectivity, factuality and neutrality” (Jones 1992, p.229).

Some researchers argue that the idea of objectivity in accounting is largely a myth, and propose “an alternative perspective on the nature of the accounting process, building on insights regarding the interpretive and metaphorical nature of accounting, and arguing that accounting should be approached as a form of “dialogue” through which accountants can construct, “read” and probe situations in a variety of ways” (Morgan 1988, p. 477).

The critical perspective of accounting and the theory of accounting rationality (see Jones 1992) view is supported by Hopper, Storey and Willmott (1987, p. 438), who sees accounting as “fully social practice [that is] both the medium and the outcome of the politico-economic context in which accounting is embedded”. The theme is echoed by many other critical accounting writers (for example, Cooper & Sherer 1984; Knights 1987; Loft 1986). “Thus, critical accountants have created a dichotomous model which offers the possibility of examining different perspectives on accounting” (Jones 1992, p. 229). These different perspectives have arisen from the social practice of accounting, whereby it was stated that:
In identifying accounting as “social”, stress is variously placed on: subjectivity; the cultural or ideological nature of knowledge; and the political nature of accounting in relation to interests. Despite the critical accounting view that accounting is a social activity, this perspective is not seen as shaping the meanings that accounting practitioners attach to accounting (Jones 1992, p. 229).

This creates a dichotomy in the interpretation of accounting practice between those who study accounting, for example researchers, and those who practice it. The conventional view of accounting as objective and rule based is contrasted with the social reality of practicing accountants. As Jones describes, “management accountants include subjectivity, uncertainty/estimation and purposefulness in their explanations of accounting and, in doing so, come closer to the critical perspective than to its image of conventional accounting” (Jones 1992, p. 230). Therefore, the conventional perspective cannot provide an adequate conceptual framework for this study of accounting in practice. “The conventional perspective captures only one aspect of practitioners’ views, or only those views expressed in particular contexts at particular moments” (Jones 1992, p. 230). The critical accounting perspective adopted by this thesis provides an opportunity to examine all aspects of accounting practice in the construction industry at the time of the RC.

“The work of critical accountants in debunking the myth of conventional accounting has presented a strong challenge to the image of accounting as a narrow technical activity” (Jones 1992, p. 230). There is a danger that management accountants see their activities as objective, factual and neutral, which is a perspective of accounting as objective practice. This may be one element of an accountants’ self-image but it does not recognise the “subjectivity, estimation/uncertainty and purposefulness which they recognise in ‘professional judgement’” (Jones 1992, p. 230), which is a perspective of accounting as subjective practice.
Some critical accounting researchers may be sceptical of the use of ST in this thesis. Some researchers believe that the “critical-theory approach is essentially a critique of the stakeholder-accountability approach” (see Brown & Fraser 2004, p. 27). This suggests a conflict which may make some feel uncomfortable in the analysis which follows. This conflict has been debated “during the 1930s, 1950s and 1970s” (Brown & Fraser 2004, p. 27). Therefore, it is an ongoing difference of research opinion. It appears to be based on two issues. First, critical theorists suggest that the stakeholder approach is unrealistic. ST proposes accountability and transparency necessary for a democratic society (Brown & Fraser 2004, p. 28). For accounting this means full disclosure based on satisfying stakeholders’ needs for information. Critical accounting argues that this approach denies the “exploitative aspects of the capitalist system, and the inherent social inequities which exist” (Brown & Fraser 2004, p. 28). In other words, ST’s idea of including all stakeholders is nice in theory but does not reflect reality. Second, critical theorists suggest the stakeholder approach is unachievable. ST proposes that stakeholders “have information rights which must be acknowledged for decision-making purposes and to protect against potential abuses of corporate power” (Brown & Fraser 2004, p. 28). For accounting this means that all stakeholders should have equal power and equal access to financial information. Critical accounting is “sceptical about the potential for real accountability in the absence of radical change in capitalist society” (Brown & Fraser 2004, p. 28). In other words, we cannot act as if we live in a pluralist society because those with power and financial strength dominate other stakeholders and will deny them information rights.

These differences are also apparent in the treatment of regulation, which emerges as an important theme in this thesis, and is highlighted in chapter 7. ST proposes that “regulation
is necessary to ensure balanced reporting for accountability, monitoring and decision-making purposes” (Brown & Fraser 2004, p. 28). For accounting this means objectivity and regulation aims to ensure this. Critical accounting accepts this, to some degree, by acknowledging that “legislation is important in securing information rights” (Brown & Fraser 2004, p. 28). However, critical accounting is still “wary of opportunities elite groups have to emasculate regulatory processes through agenda setting” (Brown & Fraser 2004, p. 28). This means that regulation must address the socio-power inequities in the business world.

This apparent conflict between critical accounting and ST may be reconciled. The way forward is tolerance for different perspectives. Critical accounting researchers themselves call for tolerance, and “a more self-reflexive and contextualized perspective on accounting which sees the connections between society, history, organisations, accounting theory, and accounting practice” (Lodh & Gaffikin 2005, p. 156). Critical accounting has challenged the traditional view of accounting from a financial or economic perspective and, in doing so, it has required tolerance from researchers who prefer this view.

Critical accounting encourages different perspectives on accounting research. This thesis embraces this thinking in several ways. First, it adopts the new history of accounting and “explores the reflexive relationships between accounting and the socio-political system in which it is embedded” (Funnell 2005, p. 144). New accounting history tends to have a sociological perspective, which explores accounting as social practice using social theory. The reflexivity of the thesis lies in its focus on the role of accounting within its social practice, which fits in the definition of critical accounting by Lodh and Gaffikin (2005) and Funnell (2005).
Second, the thesis focuses on the role of accounting in improving society through the social contract breach within the construction industry and the role accountants could play in repairing this breach and legitimising this industry. This provides a theoretical bridge connecting critical accounting and ST. Critical accounting attempts to comprehend the “social contexts within which accounting issues exist” (Gaffikin 2005b, p. xvii). This approach examines how accounting may serve a “useful social purpose and how its practice may be continually improved” (Gaffikin 2008, p. 5). The bridge is PIT, which connects critical accounting to LT and ST. The societal contract breach, which is defined by LT, identifies the opportunity for accounting to improve society, and ST enables us to understand why the legitimacy gap exists and how accountants might help close the gap.

Third, the thesis may address the concerns of critical accounting researchers who are skeptical about the claims of ST. Recent research from critical accounting researchers has discussed the important role of stakeholders. Anderson, Gaffikin and Singh (2014, p. 542) argues that accounting research needs to recognize the needs of multiple stakeholders and “from a reading of the corporate social and environmental literature, it seems that the stakeholder concept has been gaining prominence over the last two decades”. Gaffikin and Lindawati (2012), for example, argue the need to include the public as important stakeholders. They propose a code of ethics applicable not only to public accountants but which should be extended to “the business community and probably the public at large as potential stakeholders” (Gaffikin & Lindawati 2012, p.14). This supports PIT, and the stakeholder perspective, from critical accounting researchers. The following quote suggests the widespread acceptance and practice of stakeholder perspective:
these ideas] have been accepted in accounting education and practice. These include, for example, the idea of the social responsibility of the accounting profession and the stakeholder orientation of accounting reports. These topics are now included in most Australian accounting texts. The accounting profession, both the Institute and CPA Australia, has also embraced these ideas (Anderson et al. 2014, p. 546)

However, Anderson et al. (2014) acknowledge concerns about whether these ideals have been realised in practice. They highlight recent corporate scandals, such as Enron, and suggest that “the accounting profession has had problems in fulfilling its social responsibilities” (Anderson et al. 2014, p. 546). However, this criticism appears to focus more on Corporate Social Responsibility accounting rather than ST. The thesis contributes to this discussion by developing an operationalisation of ST, more specifically from the managerial perspective, by exploring how the constructs of relationships, impact and expectations help us understand the social practice of accounting within the context of a social contract breach. The application of such an approach might, for example, help better understand how scandals such as Enron occurred and how to avoid them in the future, therefore, realising in practice the goals of ST and satisfying critical accounting researchers. In doing so, this study extends critical accounting by operationalising ST and realising that whilst key stakeholders are part of the problem, they are also by necessity, part of any possible solution.

2.3.2 Public Interest Theory

The debate over whether accounting is objective or subjective practice is explored through PIT. This theory aims to correct inefficient or ineffective market practices (Posner 1974). In terms of accounting practice, the PIT of regulation proposes that regulation be introduced to
protect the public (Deegan 2009, p. 42). In most cases, the regulator, usually the
government, acts on behalf of the public to rectify inefficiencies. However, in some cases
the regulator is a private sector, as opposed to public sector, agency, as with accounting.
Whilst technical accounting standards are the responsibility of the AASB, ethical and
professional accounting standards are the subject of industry self-regulation (Wallace,
Ironfield & Orr 2000, p. 149). Questions then arise about whether private sector regulators
act in the interests of the public or their own constituents, in this case, accountants (Deegan
2009, p. 43).

The public interest is to ensure that in a capitalist society there is confidence that capital
markets are efficiently directing or allocating resources to productive assets (Deegan 2009,
p.74). There are arguments that government regulation is flawed due to ineffective
implementation caused by ineffective management or funding or the regulation is
ultimately controlled by those parties who it was supposed to control (Deegan 2009, p.74).
However, as highlighted in chapter 4, the Australian Government did not give in to pressure
exerted by the construction industry and it allocated hundreds of millions of dollars to
investigate and regulate the industry. The RC alone cost $60 million dollars (Senate
Standing Committee on Education and Employment 2014, p. 13). Therefore, typical
criticisms of regulation do not fit in this case. The government genuinely sought to correct
perceived social inequities in the construction interest with sincere motives to protect public
interest, and allocated resources appropriately.
2.3.3 Legitimacy Theory

The reasons why the government launched the RC are explored through LT. This theory asserts that “organisations continually seek to ensure that they are being perceived as operating within the bounds and norms of their respective societies, that is, they attempt to ensure that their activities are perceived by outside parties as being ‘legitimate’” (Deegan 2009, p. 323). LT is part of the broader PET (Gray, Owens & Adams 1996). PET explains how capitalism, as a social system, is shaped by economic and political interests (Gaffikin 2008, p. 82). In a capitalist society, such as Australia, there are many social inequalities amongst social classes brought about by their inequitable access to the use of resources. Economic forces serve to protect the interests of those with access to resources. Regulation is the political forces used to find more balance in the allocation of these resources.

LT fits within PIT because it explains how organisations obtain access to resources in return for acting within the broader public interests. In essence, responsible corporate citizenship is rewarded with approval by society and wealth. The measure of legitimacy expectations is the social contract. Historically, social contracts were measured by profit. Traditionally, accounting theory has been situated within the goal of profit maximization as the optimal measure of corporate performance (Patten 1991). Under this notion, a firm’s profits were viewed as an all-inclusive measure of organisational legitimacy (Ramanathan 1976) because this increased societal wealth. However, an increase in corporate disasters (for example, Enron) and unethical behaviour has led to a shift in focus. Social contracts now expect organisations to react and “attend to human, environmental, and other social consequences of business activities” (Heard & Bolce 1981, pp. 247-248).
Legitimacy, therefore, is the measure of societal perceptions of the adequacy of corporate behaviour (Suchman 1995). Legitimacy is commonly defined as the perception that the actions of an entity are within the norms of their society (Deegan 2002; Nasi, Nasi, Phillips & Zyglidopoulos 1997; Suchman 1995). Perception may differ from reality but the status of legitimacy is based on being adjudged legitimate (Lindblom 1994). Legitimacy is pursued primarily for one of two reasons. Legitimacy is either considered to be an operational resource (Dowling & Pfeffer 1975; O’Donovan 2002) or a set of constitutive beliefs (Zucker 1987). However, unlike many other resources, legitimacy is considered to be a resource that an organisation is able to affect or manipulate through various disclosure-related strategies (Woodward, Edwards & Birken 1996). In line with resource dependence theory (Pfeffer & Salancik 1978), organisations dependent on a resource will pursue strategies to ensure the continued supply of that resource (Deegan 2009, p. 324).

Legitimation is the process that leads to legitimacy (Deegan 2005; Lindblom 1994). “Researchers have proposed that legitimation tactics might differ depending upon whether the entity is trying to gain, maintain, or repair legitimacy” (Deegan 2009, p. 331). Deegan (2009) argues that theoretical development in this area remain weak. Given the historical context of this study, this represents an area within the literature where a significant contribution can be made. In examining the history of the construction industry, this study will begin by looking at how the industry tried to maintain legitimacy. It must be assumed that the industry had legitimacy status at one point; otherwise society would not have allowed it access to necessary resources. Maintaining legitimacy is considered easier than gaining or repairing (O’Donovan 2002). There are two strategies for maintaining legitimacy: predicting future changes and protecting past accomplishments (Deegan 2009,

This study will examine how the construction industry gained legitimacy in the first place. Organisations gain legitimacy by proactively seeking to persuade society that they deserve this status, and access to necessary resources (O’Donovan 2002). Gaining legitimacy involves similar strategies as when trying to repair legitimacy. The only real difference is that gaining is a proactive approach and repairing is a reactive approach. Repairing involves responding to a crisis. Lindblom (1994) recommends four strategies to gain or repair legitimacy:

1. Communicate to the public the organisation’s performance and activities which align with society’s expectations
2. Change perception of the public via disclosure of positive or desirable activities, without falsifying
3. Manipulate perception by deflecting attention from problem areas onto positive or desirable activities
4. Change social expectations, perhaps by arguing they are unreasonable.

In developing theories about the process of legitimisation, two approaches are adopted in this present study. It will examine what, if any, legitimisation tactics were employed by the industry before and after the RC to maintain, gain or repair legitimacy, and what disclosures the industry used to communicate with society. Deegan (2009, p. 332) explains
that there has been insufficient empirical research and theoretical development to connect specific legitimisation techniques with efforts to gain, maintain, or repair legitimacy. In other words, Lindblom’s recommendations are untested and it is not known whether they work or how to attain legitimacy. The only action known to work is disclosure.

To attain legitimacy status, the actual conduct of the organisation is somewhat irrelevant. Rather it is what society collectively knows or perceives that shapes legitimacy (Deegan 2009, p. 324). Information disclosure, therefore, is vital to establishing corporate legitimacy. Disclosure is important in influencing society’s perception of the organisation’s behaviour. Disclosure must then consider what type of information will influence society’s perception. LT emphasizes that the organisation must appear to consider the rights of the public at large, not just shareholders or investors (Deegan 2009, p. 325). It examines questions about the type of information that needs to be disclosed, and how organisations can persuade society that they are behaving legitimately.

Legitimacy is a theoretical concept in the sense that there is usually no clear statement from society about what it expects of an organisation. It is unlikely that an organisation can find a copy of their social contract and “negotiate” that with society (Deegan 2009, p. 326). However, it is possible to identify general guidelines of behaviour applicable to most organisations. Gray, Owens and Adams (1996) distinguish between explicit and implicit terms of the social contract. Explicit terms are legal requirements. These may be specified by legislation in areas such as industrial relations, environment, and safety. However, Dowling and Pfeffer (1975) point out that society may be unable or unwilling to have all desirable behaviours codified within the law. Implicit terms are areas outside the law but still deemed desirable by society. For example, Nike’s use of Asian ‘sweatshops’ outraged
many people in the community which Nike obviously did not foresee. Implicit terms are the area where managers have most discretion and seem to make the most mistakes.

As a society changes, so do its expectations of organisations. Therefore, organisations need to adapt and change in terms of their social contract. The analysis will identify the “legitimacy gap” in the industry’s social contract (Deegan 2009, p. 329). The difference between how an organisation should act and how it is perceived that the organisation has acted is the legitimacy gap (Deegan 2009, p. 329).

LT is used in this thesis to examine the social contract between the industry and Australian society. The RC issued a 23 volume report on 24 February 2003 (Cole 2003). The RCR presented the findings of the Commissioner Cole’s examination of the conduct of the industry. It sets out society’s expectations of the industry, and the extent to which it complies with the social contract (Deegan 2009, p. 325). In this sense, the RCR represents a gap analysis, measuring the difference between current practice and desired practice, and was a significant trigger for change.

Legitimacy gaps are created in two ways. Society’s expectations might change but the organisation or industry is still doing what it always did. The classic example is the tobacco companies; they carried on doing business as they always had, but suddenly came under increasing attack in the 1970s as society became more aware of the health problems associated with smoking (Nasi et al. 1997). The second manner in which legitimacy gaps are created is when previously unknown information about an organisation becomes known. Bowles (1991, p. 398) calls this the “organizational shadow”, which refers to information about the organisation unknown to the public. This usually becomes known.
through the media. This framework is used to explain the historical context of how the construction industry lost legitimacy in chapter 4. For example, the Four Corners Report was a catalyst for the RC; because while the Government was aware of the industry’s unlawful and inappropriate behaviour, the media report pushed it into the forefront of public consciousness and the Government had to respond.

LT proposes a relationship between corporate disclosures and community expectations; the view being that management reacts to community concerns and makes necessary changes (Deegan 2009, p. 340). Researchers tend to use media reports as an indication of public satisfaction or dissatisfaction with an organisation’s activities (for example, see Ader 1995, p. 300; Brown & Deegan, 1998). Organisations can also use customer surveys to gauge satisfaction levels. This enables management to distinguish what is important so that organisations can prioritize issues for action.

Neuman (1990) distinguishes between “obtrusive” and “non-obtrusive” issues which defines public awareness levels. For example, interest rate increases are highly visible and would be an obtrusive issue for banks; while industrial relations practices or accounting procedures would be invisible to most and, therefore, classified as non-obtrusive. Construction industry managers needed then to see the signs that their conduct was considered unacceptable by society and whether to act or ignore them.

LT explains that managers will adapt to community expectations if they are to be successful (Deegan 2009, p. 335). A number of papers have identified specific types of social responsibility disclosures that have appeared in annual reports (Deegan 2009, p. 336). These disclosures attempt to explain how management has responded to legitimacy gaps.
and tried to attain or maintain legitimacy. Questions then emerge about what type of public disclosures exist in the construction industry and how to assess their reliability and accuracy.

In summary, LT helps us understand the construction industry’s interaction with the broader society. It helps identify the economic forces which created social inequities leading to the breach of the social contract, as well as the political forces driving regulation and seeking to find balance amongst the industry’s social groups. It provides an interpretative framework to measure the social contract, the nature of the breach, that is the legitimacy gap, and its historical context, how the industry gained, maintained, and repaired its legitimacy.

2.3.4 Stakeholder Theory

ST and LT are similar, as both are part of the broader theory of PIT. The difference is that while LT discusses the expectations of society in general, manifested as the social contract, ST examines particular groups within society. These different groups, it is proposed by ST, will have different expectations and this is manifested in terms of various social contracts ‘negotiated’ with different stakeholder groups (Deegan 2009, p. 346). Therefore, ST has a very important role in this study, and is the main theory used. ST allows us to examine the difference between the government’s expectations of the industry and other groups with a vested interest in the industry. In this study, ST uses SNA to help understand the social interaction between the construction industry’s stakeholders.
Accounting’s role in the industry has implications for how stakeholder expectations are considered or managed. Firms’ compliance with the social contract will be influenced by their relationships within the industry. ST will enable the examination of the interaction of the following groups within the industry, their relative importance and influence over accounting, and the tension between responsibility, doing the right thing, and demand, meeting the interests of the various stakeholder groups. The following figure summarises the stakeholder groups within the construction industry:
ST has two themes: the Ethical (also referred to as moral or normative) perspective and the Managerial perspective. Each theme is now examined.

The Ethical perspective argues that all stakeholders should be treated equally and that the (economic) power of various groups should not allow them to have differential influence over the firm (Deegan 2009, p. 347). Decisions should be made based on the best interests of all stakeholders and not just the most powerful. The ethical perspective supports the position of the RC. The RC’s statement of social expectations of the industry argues that improved behaviour, manifested in structural and cultural reforms, would benefit all
Australians. Therefore, the Government is representing all of society in setting a social contract for the industry. From a SNA lens, the ethical perspective represents cohesion and harmony within the social network, generated by equality, democracy and participation amongst all stakeholders.

The Managerial perspective, on the other hand, argues that management will be likely to respond to the expectations of particular (typically powerful) stakeholders (Gray, Owens & Adams 1996, p. 45). A fundamental cause of the problems that led to the RC was that the industry’s management were influenced by the demands of different stakeholders, the unions in particular. However, the RC also found non-industrial relations issues such as tax evasion and unlawful acceptance and reporting of ‘commissions’. This raises the question of which stakeholder groups influenced these behaviours and why.

Three stakeholder constructs have been identified for operationalisation:

1. Relationships
2. Impact
3. Expectations (Gray, Owens & Adams 1996, p. 45)

The objective with this operationalisation is to test whether these ST constructs may help predict stakeholder behaviour in terms of willingness to meet the social contract. The first operationalisation is relationships. Relationships may be defined by SNA. SNA allows us to measure interaction between stakeholder groups in terms of network quality (depth of contact) and network structure (number of contacts and frequency of contact) (for example, Stone 2001). The second operationalisation is impact. Impact may be defined in terms of
management’s willingness to listen to various stakeholder groups and adjust their behaviour accordingly. It measures the power or level of influence of each group. The third operationalisation is expectations. Expectations may be defined in terms of the social contract for each stakeholder group. It answers questions about what each of the groups listed in figure 2.1 above expect of accounting, and how these expectations differ. The central theme with ST for this study is that the construction industry’s stakeholder groups will have different social contracts with the industry in terms of its accounting. This will be manifested in differences compared with the overall social contract, the RC, and between the expectations of the various groups.

In summary, ST identifies the various groups with a vested interest in the industry, but also their different expectations of accounting practice, manifested as multiple social contracts. The unlawfulness associated with other construction industry activities suggests that the industry tended to adopt a managerial rather than ethical perspective on stakeholder expectations. Clearly, not all stakeholder groups are equal in the construction industry. Questions raised include whether differences in power within these groups create conflict over accounting practice; if so, who was in control and what were their expectations of accounting within the industry. ST allows an opportunity to further examine the tension between accounting as an objective rule based system versus a subjective reality. It allows examination about whether accounting in the construction industry was based on a sense of responsibility, doing the right thing, or demand, meeting the interests of the most powerful stakeholders. SNA theory will be used to enhance ST by examining the macro level interactions of the stakeholder groups in some more theoretical detail.
2.4 Research Objectives

The study has two main themes, as outlined in section 1.4 of chapter 1:

1. How did the structural and cultural factors that led to the RC in 2003 affect accounting practice in the construction industry?

2. What was the role of accounting in the construction industry’s social contract?

In this section, these themes are expanded to identify specific research objectives, which are used to guide the data gathering, analysis, and reporting. This chapter’s theoretical framework is laid over the research objectives to show how the theory is used to examine the data.

As stated previously, the main theoretical lens used in this study is CAT. CAT aims to identify the prevailing social arrangements within a community, such as an industry, within the broader context of the society in which it exists (Roslender 2006, p. 250). In this study, CAT examines the interaction between the construction industry and its stakeholders. The societal context is that the industry is important to Australia but was not behaving in a way that met society’s expectations. The outcome was the RC 2003 to examine why the industry was misbehaving and how this might be addressed. CAT also aims to promote self-awareness of both “what is” and “what might be”, and how the former might be transformed to install the latter (Roslender 2006, p. 250). The difference between the desired and the actual behaviour of the construction industry is the legitimacy gap.
Theme 1 – What Led to the Royal Commission (up to 2003)

PIT explains why and how society intervenes in business activity. In this study, it is used to explain why the regulator, the Federal Government, felt it needed to take action to improve behaviour in the construction industry. It is also used to explain the types of regulation used by the Government and accounting bodies. In terms of this study, a number of questions emerge:

1. Why was the construction industry sufficiently important for the Australian Federal Government to launch a Royal Commission? (chapter 3)
2. Why did the Federal Government choose to conduct a Royal Commission into the construction industry? (chapter 4)
3. Did regulation of accounting practice in the construction industry act in the interests of the public or its constituents? (chapter 7)

LT explains how organisations seek to be perceived as ‘legitimate’ by their society in return for resources necessary for their survival (for example, see Dowling & Pfeffer 1975; O’Donovan 2002). Lindblom (1994) distinguishes between legitimacy and legitimation, where the former is a condition or status and the latter a process that leads to being adjudged legitimate. This raises a number of questions:

4. Why does the construction industry need to be perceived as legitimate? What resources are conferred as a result? (chapter 3)
5. What criteria does society set in adjudging legitimate status? How can it be known if the industry is legitimate? (chapter 4)
6. What processes does society expect of the industry to close the legitimacy gap?
LT helps us understand why and how organisations can be accepted as appropriate corporate citizens in their society. A number of questions emerge:

7. How did the construction industry perceive its role as corporate citizens? (chapter 4)
8. How did society perceive the industry’s role as corporate citizens? (chapter 4)
9. What was the nature of the social contract between the construction industry and Australian society? What did society expect from this industry? (chapter 4)

ST identifies the various groups with a vested interest in the construction industry, but also their different expectations of accounting practice, manifested as multiple social contracts. ST is used help explain or predict stakeholder behaviour in terms of willingness to meet the social contract. A number of questions emerge:

10. How did the construction industry’s stakeholders interact with accountants? (chapter 5)
11. What is the willingness of the construction industry’s management to listen to various stakeholder groups and adjust their behaviour accordingly? Who had the power in this industry? What power did accountants have? (chapter 6)
12. What is the social contract the construction industry’s stakeholders had with accountants? (chapter 6)

**Theme 2 – Post Royal Commission (after 2003)**

Non-compliance with the social contract can also have a negative impact on the organisation or industry’s market reputation or image (Deegan, Rankin & Voght 2000). The importance of societal perception is illustrated by a study showing positive correlations between media attention for certain social and environmental issues and the volume of disclosures on these issues (Deegan, Rankin & Tobin 2002). In other words, organisations
see compliance with their social contract important enough to take action. This leads to questions about the RC’s findings and how the construction industry reacted:

13. What measures of legitimacy were imposed by the RC on the construction industry? (chapter 4)

14. Did the construction industry’s non-compliance with the social contract have a negative impact on its market reputation/image? If so, how did this negative impact affect the industry? (chapter 7)

The role of accounting practice is then considered within the broader context of the social reconstruction of this industry. The specific activities identified by the RC as misbehaviour may then be examined in terms of the role of accountants. These activities are listed on the right hand side of figure 1.1 in chapter 1, and include profit manipulation, non-compliance with payroll tax, and so on. The response of accounting to the RC findings is explored by looking at how these activities are typically conducted in the construction industry and whether they could have been undertaken with or without accountants, prior to the RC, and afterwards. In this way, conclusions about the role of accounting in legitimising the construction industry can be drawn. A number of questions emerge:

15. What role did accountants play in activities identified as unlawful behaviour by the RC? (chapter 6)

16. Did accountants change their role in activities identified as misbehaviour by the RC after 2003? (chapter 7)

This section identified sixteen research questions aiming to reconstruct the social reality of behaviour explaining the legitimacy gap in the construction industry.
2.5 Chapter Summary

This chapter discussed the ‘what’, ‘why’, and ‘how’ of the study. It defined the ‘what’ as the construction industry, with a particular emphasis on the industry’s private and public stakeholders. The ‘why’ explained that the industry is socially and economically important to Australia and its conduct is in the public interest. The ‘how’ outlined the methodology and the theoretical framework used to examine accounting’s role in legitimising this industry. The methodology is an embedded case study which uses CA and CDA to find meaning in the reports written about the construction industry. The social reconstruction of the industry and its stakeholders mainly uses ST, with help from LT and PIT, and ideas from the discipline of sociology, SNA. The next chapter will explain the phenomena under investigation, the ‘what’ in this case study, in more detail, and also its significance, the ‘why’ in this case study.
CHAPTER 3: THE CONSTRUCTION INDUSTRY

3.1 Introduction

This chapter examines the nature of the construction industry. The purpose of this chapter is to provide context for the remaining chapters. The chapter examines the industry’s nature, history, structure, and culture. The chapter will show that the construction industry has had a long history in Australia, that it is important to society, its structure has created intense competition with small profit margins and a short-term profit focus, and the culture that these characteristics have produced has created a propensity towards unlawful behaviour.

The construction industry began in the earliest days of Australia’s settlement by white Europeans, that is the 1780s, and has remained important to society ever since. In the early days, much of Australia was characterised by vast distances between settlements. The industry provides fundamental benefits to society, that is, shelter and infrastructure such as roads and bridges. The industry is somewhat unique in Australia in terms of its industry structure. It is a highly fragmented industry divided between a small group of large companies, known as head contractors, and thousands of very small companies, known as sub-contractors. The sub-contractors are often dependent upon head contractors for work, creating important socio-power differentials within the industry. This is heightened by the wealth and status divide of landowners, entrepreneurs and business owners, and property developers, and trades people. Given the traditional working class nature of trades people and labourers, many industry employees have felt
powerless in terms of their relationship with their employers. This tension has found a powerful voice in the trade union movement in Australia, which has always been closely associated with the construction industry employees. This association has created a rebellious culture within the construction industry which evolved to the point in 2003 when the Federal Government launched a Royal Commission to investigate the industry’s conduct.

The main purpose in describing the industry’s history from a sociological perspective is to begin analysis of the behaviours leading to the social contract breach. Organisational behaviour can be a result of organisational culture which in turn is a result of underlying assumptions about the way business is done (Schein 2004, p. 26). The behaviours which led the RC to conclude that the industry was unlawful (Cole 2003, vol. 1, p. 8) did not suddenly emerge. These behaviours were embedded in organisational practices, systems, norms and values. By looking at the history of the industry from a sociological perspective, an understanding is gained as to why these unlawful behaviours became the norm. The turning point appears to be a change in political ideological, brought about by the emergence of communism and its adoption by union leaders, particularly from the 1950s onwards. The prosperity of the 1960s boosted union membership and strength. The 1970s saw a fundamental shift in the industry’s socio-political landscape with unions taking control and dictating the rules of stakeholder interaction. This landscape built upon the political ideologies of left wing union leadership with a natural animosity towards the ruling class, manifested by owners and managers, and a militant style. This evolved in the 1980s and 1990s into a culture that felt those in power could ignore the law and do things their way. It seems a long way from the sense of social justice and generosity of spirit that created the friendly societies in the early days of Australia’s white settlement.
3.2 Nature of the Australian Construction Industry

3.2.1 Introduction

Economists define an industry as a group of firms that supplies a particular market (Grant 2009, p. 86). The key to defining an industry is its market. The main problem with defining an industry in terms of its market is setting boundaries. In the case of the construction industry, it offers many products and services and has many different types of customers. Researchers overcome this problem by dividing it into supply and demand dimensions. On the demand side, an industry is defined as firms that provide the same product or service, and its customers are able to switch, or choose between suppliers, on the basis of price. On the supply side, an industry is composed of firms that are able to use their factors of production, including equipment, technology and labour, in the same way (see Grant 2013).

This approach to defining industry structure focuses on the key dimension of firm behaviour within an industry: competition. Competition is particularly important in the construction industry because it has created many of the structural problems identified by the RC in 2003. The construction industry is characterised by intense competition, leading to small profit margins, and a short term focus on profit. In order to understand the structural problems, we need to identify who is in competition.

3.2.2 Industry Sectors

Previous research uses the term construction generally to describe the activity of the creation of physical infrastructure, superstructure and related facilities (Wells 1985). Construction is also referred to as all types of activities associated with the erection and repair of immobile structures and facilities (Nam & Tatum 1988), in other words, things that are built for a purpose to last.
It is more helpful that the construction industry is typically defined as having three distinct industry sectors: engineering construction, non-residential building, and residential building (de Valence 2011). This approach is also adopted by the Australian Bureau of Statistics (ABS), a government body who collects and reports on information for the government and broader society. The ABS defines the construction industry in terms of the major industry segments, as follows:

The construction industry consists of those businesses mainly engaged in the construction of residential and non-residential buildings (including alterations and additions), engineering structures and related trade services classified under the Australian and New Zealand Standard Industrial Classification (ANZSIC) 2006 (ABS 2010, p. 3).

In terms of competition, competitors can be identified by asking whether the same firms operate in each of the three industry sectors. For example, do those firms offering engineering construction services also offer residential and non-residential buildings? From a demand perspective, would customers seeking to buy a road or a bridge be willing to buy a house instead if the price was lower? This would not occur because these products offer a different function for the customer. From a supply perspective, can an engineering construction firm use its expensive earth moving equipment to build a block of units? This is also unlikely to occur. This means that the engineering construction sector is different from residential and non-residential building. Therefore, from a competition perspective, the construction industry can be split into two distinct groups of competitors: engineering construction and residential and non-residential.

Consideration needs to be given as to whether firms competing in residential and non-residential constructing are the same. From a demand perspective, would customers seeking to buy a house be willing to buy an office, factory or shop if the price was lower? Given that the needs of the customer are very different this is most unlikely.
From a supply side perspective, would firms who can build a house also be able to build a factory with their existing resources such as equipment and labour? This is more likely. This means that firms are able to compete in both the residential and non-residential sectors. Therefore, this study adopts a definition of residential and non-residential building as its definition of the construction industry. It does this because this study focuses on the types of firms investigated by the RC and, from a competitors’ perspective, this was firms operating in the residential and non-residential sectors.

3.2.3 Industry Segments

Researchers also define industries in terms of the products and services they offer (Grant 2013). The construction industry has two classes product buildings and civil works (Chris 1998; Gould & Joyce 2008).

This approach also supports the decision made by this study to separate the industry into engineering construction and residential and non-residential building. In terms of market segmentation, researchers have mostly classified the industry in this way. First, engineering construction offers road and bridge construction, electrical generation, electrical transmission, water and sewerage, processing plants including oil and gas pipelines, and miscellaneous including railways, harbours, and recreational facilities (de Valence 2011). Residential building includes all dwellings. Non-residential building includes offices, hotels, factories, shops and other business premises, as well as warehouses, terminals, service stations, and car parks (de Valence 2011). This approach to industry segmentation is consistent with industry analysts who also define the industry in terms of the type of products and services offered, as shown by this extract:

The [industry] covers construction of buildings, roads, railroads, aerodromes, irrigation projects, harbour or river works, water, gas, sewerage, storm water drains, mains, electricity, other transmission lines or towers, pipelines, oil
refineries, civil engineering projects and on-site assembly of prefabricated buildings. It includes repairs and renovation, mine site preparation, demolitions or excavations and the installation of utilities. Construction services are also included (Dunn 2010, p. 2).

This industry analyst report extends the range of products and services typically used by researchers by including support services such as maintenance. For the purposes of this study, the industry analyst definition is too broad and would include too many firms that are not competing directly.

The only reason to use industry segments to analyse unlawful behaviour instead of industry sectors would be if competitors were different. Researchers have found that competitors in the construction industry are different across Australia, but for reasons not related to the products or services; namely size and geography. Therefore, this study will focus at the industry sector level, residential and non-residential construction, with an interest in differences in behaviour across firm size and geography.

3.2.4 Firm Size

The RCR defines the construction industry in terms of firm size: head contractors (large companies) and sub-contractors (small businesses). In general terms, these categories may be defined in terms of number of employees. The RCR defines most subcontractors as small businesses employing fewer than five employees (Cole 2003, vol. 1, p.13). The ABS defines small business as fewer than twenty employees, and five or less employees as micro businesses (ABS 2002, p. 1). For the purposes of consistency, the thesis adopts the RCR definition of small business, which may be used interchangeably with the ABS term micro business. All others are classified as large companies. In terms of competition, firm size does matter in the construction industry. Head contractors compete against other head contractors; while small contractors compete against other
small contractors. In most cases, big firms do not compete against small firms. There are exceptions to this rule. For example, there are very small firms who build houses who compete against the big housing construction firms. However, this competition is more indirect and customers are still most likely to be comparing small builders against other small builders, perhaps based on price or the opportunity to build a one-off design. Most large house builders have a set of standard designs that customers can choose from and they compete based on these designs. Differences in firm size are very important in creating the socio-power inequities which existed within the construction industry and this had a strong influence on the relationships between the industry’s stakeholders.

The government’s main concern from the social contract breach identified by the RC was the small firms who largely work for the head contractors. These firms employ only a few people each but when combined represent a large proportion of the industry workforce (36%) (Cole 2003). The Government’s concern about this industry structure is the powerlessness of the small businesses to address the industry’s unlawful behaviour, as shown in this extract from the RCR:

The subcontractors in the building and construction industry are typical of small business in Australia. Of the 692 800 people who are engaged in the industry, 248 100, or 36 per cent, are subcontractors or ‘own account workers’. Less than 25 per cent of the total workforce belongs to a union. These figures are indicative of an industry where more than three-quarters of the workforce do not wish to be involved with unions, and more than one-third have an attitude of independence and self-reliance. However, most subcontractors are small with 94 per cent employing fewer than five employees. They are frequently undercapitalised and depend upon continuous cash flow for their continued existence. They are thus immensely vulnerable to disruption to their work flow. They have no prospect of resisting union demands or, at present of recovering losses suffered from unlawful industrial action by unions (Cole 2003, vol. 1, p.13).
The extract shows why the Government chose to define the industry in this way. The phrase ‘immensely vulnerable’ is particularly useful in describing the power inequities within the industry, and how subcontractors had little power. For the purposes of this study it is helpful to split the industry sector grouping, residential and non-residential building; and then into head contractors and sub-contractors within each sector, because they are competing directly with one another. The issue of competition is important because it influences industry structural issues, which were highlighted as problems by the RC.

### 3.2.5 Geography

The construction industry is not mobile, in the sense that the final product is not readily transportable and the final service has to be delivered on site (Toner 2006). As a result, firms tend to operate within a geographic area that enables their workers to travel to and from site; perhaps one to one and a half hours travel by car or rail. Therefore, most small firms service their local area. Large firms can overcome this problem by opening branches in other areas and employing local staff.

The larger firms operate across all segments and Australian states (geographic locations) and include firms such as Lend Lease Corporation Limited, Leighton Holdings Limited, and Mirvac Group. However, the construction industry has very low mobility barriers, in the sense that there are no regulatory barriers to inter-state trade or mobility of equipment or labour, and minimal restraints on the acquisition of industry occupational skills (Toner 2006). This means that while a firm may be based in one state, such as Victoria, it might compete for business in another state, such as New South Wales, if it needed the work. This means it has the opportunity to grow and become a national firm.
In summary, the study defines the construction industry as firms competing in residential and non-residential building, with a particular focus on firm size, and an interest in differences by geography, that is, state. The study does not include firms offering engineering construction, and does not examine industry segments in the sense of product or service classifications.

3.3 History of the Australian Construction Industry

3.3.1 Sociological Background

The construction industry began when the tents of the first fleet were set up on arrival at Sydney Cove in 1788. The Aboriginal people who lived in Australia before the arrival of the English also engaged in construction in the sense of camp sites and other shelter. However, the beginnings of today’s construction industry began with white settlement in 1788. From the earliest days of the white settlement, construction works began with convict labour under the supervision of military authorities (Knight 1997). Sydney Cove quickly grew as temporary and then more permanent structures were built and roads and bridges were constructed. In the decades following the first fleet arrival, free convicts, as well as free and assisted immigrants began to engage in construction work (Knight 1997). As the number of skilled immigrants grew, their skills were diffused and groups of tradespeople emerged. As these groups grew, authorities felt a need to regulate their work practices to introduce consistent standards and quality about the way work was conducted. Carpenters and joiners were one of the first labour groups to become organized in this way (Turner & Sandercock 1983). Various associations surrounding the building trades, known as friendly societies, started to emerge in the 1830s (Mitchell 1996).
These friendly societies provide an insight into the culture of construction industry employees in the early decades of white settlement in Australia. They began as a benefit society in the sense of providing financial and other support for members who were sick, out-of-work, and sometimes provided funeral assistance (Hume 1960). This helped to create a sense of belonging and support that evolved into the national culture identity of ‘mateship’ that Australian is so proud of. Mateship has its roots in Australia from convict times; but the goldfields in the 19th century were the cultural incubators of the term (Dyrenfurth 2015). Trade unionists, labour party members, and radicals have used the term mateship to mean the same thing as unionism, and mateship was seen as the equivalent of socialism within the union movement (Dyrenfurth 2015). This sense of mateship created a strong identity for workers in the industry and a culture of supporting one another when things got tough. It also created a sense of ‘us’ and ‘them’.

In these early stages of the industry’s development, social networks began to establish clear roles and divisions. Hume (1960), for example, argues that the friendly societies were indeed trade unions because they excluded employers from their membership and recognized differences in worker status. Although the friendly societies began with a purpose of providing social welfare, this grew to include a focus on wages and conditions of employment. While initially these groups may have existed to help those “down on their luck”, they evolved to consider the needs of all members. They became unions of trades or trade unions.

Evidence of the sense of natural justice desired by these early trade unions emerged in industrial action which aimed to improve the economic interests of members. The carpenters and joiners went on strike at least once in 1840; plumbers also took industrial action in the 1840s; and stonemasons fought for and won the eight hour day in 1856 (Turner & Sandercock 1983). These actions reveal a culture of socio-power conflict.
between employers and employees. That workers felt the need to strike to communicate their dissatisfaction with their working conditions suggests they felt powerless and exploited by employers and that the only way to negotiate changes was to band together and take a stand. The sense of mateship had grown into an industrial movement by the 1850s. This shows that the culture which led to the RC in 2003 had its roots 150 years ago in the growing awareness of workers that they needed to act together to force employers to listen to their needs.

There was also a sense of pride in their skills and the quality of their work. The early trades unions imposed strict rules of entrance; if a tradesman’s work was not of satisfactory standard, they were not admitted as a member of the union (Mitchell 1996). This sense of pride and maintaining industry standards was formalized by the creation of the construction industry’s peak body, the Master Builders Association (MBA), in 1873. The MBA is Australia’s oldest industry association (Master Builders 2015). The formation of the MBA also “heralded a change in the industry, namely the widespread adoption of subcontracting” (Gyles 1992, vol. 7, p. 146).

The emergence of subcontracting was a watershed moment in the history of the construction industry as it changed the way work was organized. Most importantly for this study, it changed the employment relationship and had a significant impact on socio-political power inequities in the industry’s social networks. The emergence of the MBA changed the employment relationship away from single trades. For example a customer, such as someone wanting a house built, would seek people with necessary skills to complete the project such as a carpenter, plumber and other trades (Gyles 1992, vol. 7, p. 146). The master builders tendered for whole projects and then subcontracted work out to tradesmen (Knight 1997). This meant that the master builders were project managers who had a temporary relationship with the tradespeople they employed. The
temporary nature of this relationship created socio-political power inequities in the employment relationship. Tradespeople became subcontractors whose dependency on the masters builders to give them work meant that they were vulnerable. The master builders in essence were head contractors. This industry structure continues to today.

In 1899, the Government began to take an active role in the regulation of the construction industry. The New South Wales Minister for Works used the Public Works Department to improve the remuneration and working conditions of lower skilled labourers (Sheldon 1989). This resulted in growth in union membership. In the period up to 1920, union density continued to grow (Knight 1997), and the government took a more active interest in union activities and Federal registration of building unions (Gyles 1992, vol. 7, p. 148).

The construction industry had a cyclical boom-bust nature in the early part of the 20th century in response to changes in the economy and in government policy, which created fluctuations in spending on all industry sectors. World War One halved industry outputs, but the post war recovery increased demand, and the depression in the 1930s led to widespread unemployment in the industry (Sheldon 1993). During this period the adoption of the new political ideology of communism emerged and created important changes in Australian society. These changes would have a significant impact on the construction industry.

By 1945, communists led the major construction unions in Australia (Turner & Sandercock 1983). This was most noticeable in the Building Workers’ Industrial Union (BWIU), which was formed by workers with communist party associations (Mitchell 1996). Communist beliefs transformed employee groups into industrial unions rather than trade unions (Mitchell 1996) by changing the focus from individual trades such as
electricians to industries such as construction. This increased the size of the unions in terms of membership and more power. The transformation meant that the socio-political power inequities between employers and employees became aggressive and adversarial. Unions such as the BWIU sought benefits for their members, just like pre-communist unions, but the difference was in how they sought these benefits. Rather than pursuing benefits through the process set by government, that is industrial tribunals, the BWIU sought to deal directly with employers. Accordingly a new relationship emerged between the industry’s stakeholders. The BWIU introduced campaigns of “direct action” which saw the first attempts of different unions working together to coerce employers to comply with their demands (Knight 1997). This aggressive behaviour led the Federal Government to deregister the BWIU, essentially outlawing their behaviour.

In the 1950s, the construction industry socio-political power inequities changed again as two new dynamics emerged. Inter-union rivalry emerged as unions struggled to establish more power over other unions (Gyles 1992, vol. 7, p. 146). Employers, through the MBA, fought back by trying to get unions such as the BWIU deregistered. At the same time, the militant culture created by communist ideology created power struggles within the union movement. Whereas until the 1950s the battle had been between employers and employees, it now involved employees against employees as well. However, the battle was mainly restricted to union leadership and often did not involve the average union member. It was the 1950s where the construction industry established a reputation for violence and aggression (Frenkel & Coolican 1980), and thuggery and corruption (Mitchell 1996). Thus, it had changed considerably from the benevolence of the friendly societies 60 years before.

In the 1960s, the construction industry enjoyed a boom period with almost uninterrupted growth. During this period, changing technology, new building materials and techniques
changed the way labour was used (Mitchell 1996). Once again, the employment relationship in the industry changed. New pre-fabrication techniques meant the use of off-site construction, which was then transported to site (Mitchell 1996). This created a ‘manufacturing’ process for construction where off-site ‘factories’ prepared prefabricated structures for assembly on-site. These off-site production facilities enabled more specialisation of labour and more permanency in the employment relationship.

Booming demand for construction, particularly within the central business districts of major cities, meant employers wanted to avoid industrial disputes to ensure they did not miss out on opportunities (Mitchell 1996). In this way, the 1960s swung the balance of power towards the trade unions and their members. Employees in the construction industry experienced their best ever wages and working conditions, increased job security, and bargaining power over employers who wished to avoid industrial disputes.

In the 1970s, the unions started to flex their muscle. The final swing in the socio-political power inequities amongst construction industry stakeholders was noticeable during this time. During this period, the trade unions assumed control of the industry. The Builders Labourers Federation (BLF) led the way and attacked employers with aggressive tactics. The most visible was disputes over payment for accidents (Mitchell 1996). The dispute caused massive disruption to the industry with 30,000 union members attending meetings across New South Wales alone. Employers felt powerless to respond and had no choice but to grant the unions’ demands for accident pay (Mitchell 1996). The BLF was not satisfied and wanted the dispute to continue despite getting what they sought. However, the dispute is particularly important for this study because it showed how the unions had changed the rules of engagement in the adversarial relationship between the construction industry’s stakeholders. This dispute showed that the unions not only wanted to win, they wanted to define the nature of the
game, fight only along the rules they set, and to emerge victorious (Knight 1997). The new rules of engagement did not include ‘asking for an umpire’s decision’ (Knight 1997) which meant the unions did not involve society’s legal system, that is, courts or other arbitration. This shows that as early as the 1970s, 30 years before the RC in 2003, that the unions had decided they did not need to work within the legal processes established by society. They would go around the legal system and do things their way. While this may imply a negative impact on the construction industry, particularly for employers, industrial unrest did have a positive affect by improving the quality of employees’ lives.

In the 1980s, the construction industry moved towards becoming a truly national industry, whereas it had previously been restricted to geographic boundaries set by the states of Australia. The movement towards a national industry was generated at two levels: employers expanded to open business in other states, and the unions amalgamated and created Federal Branches, rather than state-based organisations. Both the employers and unions saw the benefits of size. Larger organisations had more bargaining power. In the 1990s, the decade leading up to the RC in 2003, the industry’s behaviour increasingly attracted the attention of the media, the public, and the Government.

3.3.2 Economic Background

Like any economy, the construction of residential and non-residential building, as well as infrastructure such as roads and bridges is essential. Given that Australia’s history of European settlement is little more than 200 years, and the rapid development of the towns and cities and associated infrastructure, it is clear that the industry became prosperous and influential. Australia has one of the highest rates of home ownership in
the world. Therefore, demand for housing construction has always been strong. On the other hand, Australia is a big country with vast distances separating the major towns and cities, fuelling demand for infrastructure. This strong demand may have created a perception within the industry of being an essential service, and one Australia could not do without.

The period prior to 1930 saw steady growth as Australia transformed from a colony to a nation. Villages transformed into towns and then into cities. Demand for dwellings grew as the population increased. The period between 1930 and 1944 was characterised by the depression and World War II, which meant an overall economic downturn and slow demand for construction activity. The period between 1945 and 1975 was defined by consistent and strong growth throughout the Australian economy. This was also the period where the construction industry enjoyed its strongest growth relative to the economy overall. The source of much of this post-war investment build up was the construction of buildings and the formation of infrastructure. Over this period the construction industry rose from 5% of Gross Domestic Product to a peak of 8.3% in the mid-1970s (Dunn 2010).

Since 1975, the construction industry has shown signs of maturity. The industry’s share of GDP has fallen gradually, despite sporadic boom periods such as 1988-89 where it reached 5.8% of GDP. There have been no major and widely used advances in technology, shifts of location or market, and the major long term driving force behind demand has been population growth (Dunn 2010, p. 36). Despite this, the construction industry’s overall revenues have grown steadily over the past few decades. The following table and graph presents a trend analysis since 1986-87 by industry sector. The annual data is presented for the year’s preceding the RC, and then compared with the most current data (2011-12).
### Table 3.1: Construction Industry Revenues in AUD$ Billion

<table>
<thead>
<tr>
<th>Year</th>
<th>Residential Building</th>
<th>Non-Residential Building</th>
<th>Total Building</th>
<th>Engineering Construction</th>
<th>Total Construction</th>
</tr>
</thead>
<tbody>
<tr>
<td>1986-87</td>
<td>12.6</td>
<td>13.4</td>
<td>26.0</td>
<td>12.5</td>
<td>38.5</td>
</tr>
<tr>
<td>1987-88</td>
<td>13.8</td>
<td>15.4</td>
<td>29.2</td>
<td>11.6</td>
<td>40.8</td>
</tr>
<tr>
<td>1988-89</td>
<td>17.7</td>
<td>16.1</td>
<td>33.8</td>
<td>11.4</td>
<td>45.2</td>
</tr>
<tr>
<td>1989-90</td>
<td>16.9</td>
<td>17.2</td>
<td>34.1</td>
<td>12.7</td>
<td>46.8</td>
</tr>
<tr>
<td>1990-91</td>
<td>14.7</td>
<td>15.4</td>
<td>30.1</td>
<td>12.9</td>
<td>43.0</td>
</tr>
<tr>
<td>1991-92</td>
<td>14.8</td>
<td>12.0</td>
<td>26.8</td>
<td>12.0</td>
<td>38.8</td>
</tr>
<tr>
<td>1992-93</td>
<td>17.3</td>
<td>10.8</td>
<td>28.1</td>
<td>12.4</td>
<td>40.5</td>
</tr>
<tr>
<td>1993-94</td>
<td>18.9</td>
<td>10.4</td>
<td>29.3</td>
<td>13.4</td>
<td>42.7</td>
</tr>
<tr>
<td>1994-95</td>
<td>19.7</td>
<td>11.3</td>
<td>31.0</td>
<td>13.7</td>
<td>44.7</td>
</tr>
<tr>
<td>1995-96</td>
<td>16.3</td>
<td>12.6</td>
<td>28.9</td>
<td>15.0</td>
<td>43.9</td>
</tr>
<tr>
<td>1996-97</td>
<td>16.1</td>
<td>13.8</td>
<td>29.9</td>
<td>15.5</td>
<td>45.4</td>
</tr>
<tr>
<td>1997-98</td>
<td>19.2</td>
<td>13.9</td>
<td>33.1</td>
<td>17.4</td>
<td>50.5</td>
</tr>
<tr>
<td>1998-99</td>
<td>20.8</td>
<td>14.5</td>
<td>35.3</td>
<td>19.2</td>
<td>54.5</td>
</tr>
<tr>
<td>1999-00</td>
<td>24.2</td>
<td>14.2</td>
<td>38.4</td>
<td>19.3</td>
<td>57.7</td>
</tr>
<tr>
<td>2011-2012</td>
<td>59.3</td>
<td>42.3</td>
<td>101.6</td>
<td>135.9</td>
<td>237.5</td>
</tr>
</tbody>
</table>

Source: Australian Bureau of Statistics
The graph shows how much the construction industry has grown over the past 20 years. While the increase in revenues is due to CPI changes in this period, for example the cost to purchase a house is much more in 2012 than in 1986; it also reflects growth in the economy and the population which both drive construction demand. The steep spike in 2011-2012 is also due to no data being available for the decade before. A search of the ABS archives could not locate this data. However, the point is made that in the decade prior to the RCR the industry revenues were relatively stable, but began to climb in 1999-2000 which was when momentum for an investigation into unlawful behaviour started to gather.

### 3.3.3 Propensity Towards Unlawful Behaviour

The construction industry did not always behave unlawfully. As section 3.3.2 explained, the industry began with a strong sense of social justice, and the friendly societies in the period 1790-1820 created a benevolent culture based on sharing and support for the less
fortunate. The industry’s culture changed in the 1900s as the friendly societies became trade unions. The relationship between employers and employees became more adversarial. World War II marked the most dramatic change in behaviour of the unions, as communism infiltrated the union movement, and people with communist ideology assumed leadership (Mitchell 1996). From this period, the unions became increasingly militant and aggressive in negotiating demands from employers on behalf of their members. Communist ideology bred an inherent animosity towards the wealthy class that is employers and their organisations such as the head contractors, and perceptions of being exploited. This created a rebellious culture within the industry where the unions saw authority as the enemy. This manifested in the 1970s where strong militant unions, such as the Builders Labourers Federation, engaged in coercive behaviour. The unions assumed control of the industry in the 1970s with a reputation for bullying rather than negotiation. It was at this time that rebellion turned into disregard for legal processes (Mitchell 1996). Rather than negotiate through arbitration, the unions preferred to by-pass the courts and deal directly with employers, and at times negotiations were sometimes unlawful (Mitchell 1996), creating a sense of anarchy within the industry.

Within this turmoil, unlawful practices emerged. This emerged in the form of collusive tendering, the making of special payments, and the distribution of unsuccessful tender fees amongst some employers (Knight 1997, p. 80). The Royal Commission into Productivity in the Building Industry in New South Wales 1992 found evidence of this unlawful activity inside the Master Builders’ Association from 1974 onwards (Gyles 1992, vol. 2, p. 25). The Royal Commissioner, The Honourable Justice Roger Vincent Gyles QC, commented that:
The evidence abounds with grounds for concluding that the agreements were made with dishonest intent (Gyles 1992, vol. 2, p. 161).

The phrase ‘dishonest intent’ suggests unlawful behaviour and that this was deliberate, that is, not accidental. Gyles (1992) added:

The agreements were made in private and kept private by deliberate lack of records, false invoicing and abstention from legal action if repudiation by a successful tender occurred (vol. 2, p. 161).

This suggests that this unlawful behaviour was organised in the sense that processes were put in place to cover up unlawful work practices. This infers that this unlawful behaviour was not a one-off event and that it was sufficiently regular as to require covering up by falsifying documentation. The activity, false invoicing, is particularly relevant for this study as invoicing is part of accounting work practices. Accountants were probably aware of practices such as false invoicing. Other Government investigations found that the construction industry’s work practices were “corrupt” and “widespread” (Knight 1997, p. 80).

Therefore, the construction industry did have a propensity towards unlawful behaviour prior to the RC in 2003. The industry has a long history of political activism, mainly via its strong trade union movement. Some of the unions have been deregistered by the Australian Government, and the unions have a history of rebellious and unlawful behaviour. This raises the question of whether the industry’s other stakeholders, the owners, management, staff, also had a propensity toward unlawful behaviour. The RCR and the BIT Reports (Hadgkiss 2004, 2005) were scathing in their criticism of the unions, and somewhat defensive of contractors and sub-contractors who were portrayed as the victims of bullying by the unions. However, guilt cannot be completely absolved from the other stakeholders. There was an industry-wide culture of unlawfulness created.
over many decades, and all stakeholders were involved to some degree. For example, a union official cannot accept unlawful payments from a contractor unless it was offered, irrespective of whether it was demanded by the official. Therefore, for the industry’s unlawful behaviour to be effective it had to involve various stakeholder groups.

3.3.4 The Breach of the Social Contract

PET explains how capitalism, as a social system, is shaped by economic and political interests (Gaffikin 2008, p. 82). In a capitalist society, such as Australia, there are many social inequalities amongst social classes brought about by their inequitable access to the use of resources. This is particularly evident in the construction industry which has a long history of conflict between those with access to resources, that is employers, and those without access, the working class. This has been manifest in the actions of the trade union movement, with strikes and other industrial action. Economic forces serve to protect the interests of those with access to resources. Regulation is the political force used to find more balance in the allocation of these resources. The more conflict between the industry stakeholders due to perceived inequity in the allocation of resources, the more need for regulation to find more equity for all stakeholders.

LT explains how organisations obtain access to resources in return for acting within the broader public interests. In essence, responsible corporate citizenship is rewarded with approval by society and wealth. Legitimacy expectations are defined by a social contract. Historically, social contracts were measured by profit. Companies that were profitable were considered to be meeting their obligations to society, their social contracts, because they use society’s resources appropriately. Traditionally, accounting theory has been situated within the goal of profit maximization as the optimal measure of corporate performance (Patten 1991). This introduces the work practice of profit
manipulation as a source of conflict for the Construction Industry in meeting its social contract. If profit is a measure of good corporate behaviour, meeting the social contract, then manipulation of profit is an illegal activity in response to regulation. Given accounting plays a lead role in the reporting of profit, questions must be raised about the role of accounting in profit manipulation in the construction industry.

PIT aims to correct inefficient or ineffective market practices (Posner 1974). In terms of accounting practice, the PIT of regulation proposes that regulation be introduced to protect the public (Deegan 2009, p. 42). In most cases the regulator, usually the government, acts on behalf of the public to rectify inefficiencies. This suggests that the regulator of the construction industry, the Australian federal government, perceived there were inequities in the industry’s market practices which were having a negative impact on the public interests.

“Legitimacy is a generalised perception or assumption that the actions of an entity are desirable, proper, or appropriate, within some socially constructed system of norms, values beliefs, and definitions” (Suchman 1995, p. 574). It is considered essential because it means society agrees to allow the organisation or industry access to necessary resources for survival. These resources could be any factor of production such as raw materials; land; office, retail or manufacturing space; and employees. Legitimacy is a status conferred upon by society; in other words it has to be earned.

The construction industry had legitimacy prior to the RC in 2003. This is known because society had conferred access to resources necessary for it to survive for more than 100 years. It had earned legitimacy status. This raises the question how the industry gained legitimacy in the first place. The answer lies in its desirability. In gaining legitimacy, the construction industry performs activities that are desirable. It is
clear that the construction industry is important to society. In only the second paragraph the RCR explained that the industry “is critical to welfare and prosperity in Australia” (Cole 2003, vol. 1, p. 3). It has very significant economic benefits for society but there are more fundamental reasons which explain its desirability. Construction is one of the oldest industries known to mankind, perhaps only agriculture is older. People need food to eat but also somewhere to live. For thousands of years, the ability to build housing has been of fundamentally important value to human communities. As societies became more complex, other buildings such as community meeting places such as halls, churches, castles, and monasteries became necessary, as well as roads, bridges, and other infrastructure. Maslow’s hierarchy of human needs shows that shelter is one of our fundamental desires (Maslow 1987). According to Maslow, there are five basic needs:

1. Physiological needs such as food, water
2. Safety needs such as shelter, security
3. Belonging, love and being part of a group
4. Esteem through feeling valued
5. Self-actualisation, the need to realise potential (Maslow 1987, pp. 2-6).

Central to Maslow’s theory is that the list is hierarchical in the sense that basic physiological needs must be met first before progressing to the safety needs and then onto belonging, and the higher level needs. Therefore, the service to society provided by the construction industry is at the second level and only preceded by basic physiological needs. This explains why its activities are desirable and it can attain legitimacy status in any society.
The construction industry not only provides shelter, it also contributes to society’s overall well-being via improved living standards. The construction industry plays a major and vital role in transforming the aspirations and needs of people into reality by physically implementing various construction development projects (Ibrahim, Roy, Ahmed, & Imtiaz, 2010). Construction projects cover infrastructure, such as roads, dams, airports, railways, and irrigation work, and buildings such as schools, houses, hospitals, factories (Ibrahim et al. 2010). Thus, the construction industry is essential to the growth of a nation and a key sector in the nation’s economy. A country cannot grow if there is no development and infrastructure built to spur the economy. The contributions of the industry are more than just economic; the products of construction mentioned above contribute extensively towards the creation of wealth and the quality of life of the population. The following quote illustrates the importance of the construction industry to the world’s fastest growing economy, China:

According to a survey conducted by China Statistics Press in 2000 and 2001, the construction industry in China accounts for approximately 7 percent of gross domestic product since mid-1990s and the employment in construction also accounts for about 7 percent of the total urban permanent employment in China. Furthermore, at the end of year 2003, there were totally 48,688 registered firms employing 37.8 million people working in the construction industry, creating a total output of 2,186.5 billion Yuan which is about 300 billion US $ (Shang et al., 2006). These figures clearly indicate the scale and importance of the construction industry sector in the economic development in China (Zou, Fang, Wang & Loosemore 2007, pp. 163-164).

Further evidence of the legitimacy of the construction industry is found in its reputation of conducting business in a proper or appropriate way. Construction is one of the oldest laboratories of the management sciences, particularly in the field of production management (Ibrahim et al. 2010). There are several important historical examples of the construction industry being used as an exemplar in management studies. In 400 BC, studies were carried out in Persia on the use of movement, layout and transport of
materials in construction sites (Ibrahim et al. 2010). The construction industry was used by Gilberth in his famous motion studies that established some of the principal foundations of scientific management (Gilberth 1911).

Construction is a type of production (Heizer & Render 2005) that has helped in the development of management techniques such as total quality management, project management, and business process improvement. Bertelsen and Koskela (2004, p. 2) have defined construction as “a complex production of a one kind product undertaken mainly at the delivery point by cooperation within a multi-skilled ad-hoc team”. This definition of construction indicates at least four characteristics: construction is production, it produces a one-of-a-kind product, it is complex and undertaken through cooperation by a temporary organisation (Ibrahim et al. 2010). Construction often involves a wide range of stakeholders and, therefore, complex management processes. Society can benefit from learning about how the industry operates and diffuse this learning for other industries.

In return for its desirability and meeting its social contract, the construction industry requires a range of resources to operate including materials, equipment, labour, and finance. Society can deny access to these resources if the construction industry does not meet its social contract. It can do this by embargo of suppliers of purchased items or otherwise showing dissatisfaction through commercial means, such as raising prices and industrial action to limit or eliminate access to labour.

In terms of capability, or the ways resources are combined to create value for construction organisations, the following key success factors further define what the industry may expect from society in order to survive:
1. Flexible labour force. The ability to expand and curtail operations rapidly in line with market demand enables operators to alter the size of labour forces in good time to match the short term cycles, and the ability to hire high quality, productive workers, especially in times of low labour availability.

2. Having contacts within key markets. This enables strategic alliances and relationships with building and construction companies. This is critical for the services component, which contributes a large component of the gross product of the industry.

3. Development of new products. This is particularly important for infrastructure projects such as with the development of ‘smart roads’. Also important will be the ability to pre-sell such developments.

4. Business expertise of operators. Includes excellent project management skills along with time, financial, labour and consortium management skills.

5. Having a good reputation. This is important to meet time, quality and cost specifications aid in tendering for new projects and ensures repeat business (Dunn 2010, p. 20). While reputation must be earned, it is society’s right to convey if the construction industry meets its expectations. For example, if a firm completes construction projects on time and on budget, customers will accept that it has earned a good reputation, and this is important for the firm’s survival and growth.

This list of key success factors further demonstrates the construction industry’s need for resources granted by society. The list includes access to human resources and relational attributes. It is clear that poor market image caused by breach of social contract would have a significant impact on the industry’s capability. The construction industry needs to have legitimacy in order to access resources necessary for survival, more specifically:
labour, purchased building materials and equipment, and reputational assets such as relationships and market image.

3.4 The Australian Public’s Interest in the Construction Industry

3.4.1 Introduction

As stated earlier, the construction industry has had significant economic and social importance throughout Australia’s history of white settlement. At the time of the RC, the importance of the industry had reached a stage where its unlawful behaviour could no longer be tolerated by society. The Australian Government’s main interest in the construction industry was concern that it was not operating productively. In other words, it was not using the resources allocated to it by society in an effective manner. The lack of productivity meant that there were market inefficiencies, capital and other resources, such as labour, not being used by society in a way that met its best interests. There was another serious concern for government. Many of its constituents were being directly affected by the industry’s behaviour. As the second BIT Report (Hadgkiss 2005) stated, many Australians seeking an honest living, both business owners (contractors) and workers, suffered social inequities such as financial hardship, job loss, violence, and intimidation, as a result of behaviour in the construction industry. It was in the public interest that this behaviour stop.

3.4.2 Economic Importance

Some key statistics help explain why the construction industry is economically important. Economy rank is the industry’s position compared to other Australian industries.
Table 3.2: Key Statistics on the Australian Construction Industry (2010-2011)

<table>
<thead>
<tr>
<th>Statistic</th>
<th>Data</th>
<th>Economy Rank</th>
</tr>
</thead>
<tbody>
<tr>
<td>Revenue ($m)</td>
<td>293,783.0</td>
<td>119/706</td>
</tr>
<tr>
<td>Value Added ($m)</td>
<td>78,228.0</td>
<td>97/706</td>
</tr>
<tr>
<td>Employment (people)</td>
<td>1,109,664.0</td>
<td>140/697</td>
</tr>
<tr>
<td>Domestic Demand</td>
<td>N/a</td>
<td>33/215</td>
</tr>
<tr>
<td>Revenue per Employee ($'000)</td>
<td>264.75</td>
<td>65/603</td>
</tr>
<tr>
<td>Share of the Economy (%)</td>
<td>6.19</td>
<td>335/621</td>
</tr>
</tbody>
</table>

(Source: IBIS: Dunn 2010, p. 35)

The terms in this table are defined as follows:

Industry revenue: The total sales revenue of the industry, including sales (exclusive of excise and sales tax) of goods and services; plus transfers to other firms of the same business; plus subsidies on production; plus all other operating income from outside the firm (such as commission income, repair and service income, and rent, leasing and hiring income); plus capital work done by rental or lease. Receipts from interest royalties, dividends and the sale of fixed tangible assets are excluded.

Industry value added: The market value of goods and services produced by an industry minus the cost of goods and services used in the production process, which leaves the gross product of the industry (also called its Value Added).

Employment: The number of working proprietors, partners, permanent, part-time, temporary and casual employees, and managerial and executive employees.

Domestic demand: The use of goods and services within Australia; the sum of imports and domestic production minus exports.

Revenue per employee: industry revenue divided by employee numbers.

Share of the economy: industry revenues divided by national GDP. (Dunn, 2010)
In analyzing this table, it is clear that strong demand is a key factor in determining the industry’s importance to Australia. Construction of residential and non-residential buildings is an essential service, as is infrastructure. The relatively high revenue per employee ranking is an indicator of productivity, but also reflects the comparatively low wages paid to industry employees. The industry’s total wages only ranks 335/621 (Dunn 2010, p. 35).

Since 2002, construction industry “profit margins (profits as a proportion of sales) have generally remained within a band of 4% to 5%, lower than for all other sectors of the economy, excluding retail trade and wholesale trade” (AIG 2008). At the time of the RC, profit margins trended downward between 2002 and 2006 with the exception of a slight pick-up in 2004 (AIG 2008). “Thereafter, profit margins lifted, rising from 3.9% to 4.9% in December 2007” (AIG 2008).

The construction industry remains very important to Australia’s economy. However, its performance must be concerning to the Australian Government. In the decade since the RC in 2003, profit margins are still very small and in 2011-2012 actually decreased further to a very tight 3.3% (ABS 2013, p.10). At face value it seems the reforms of the RC have not increased productivity in the industry.

3.4.3 Cultural Importance

The RC focused on the construction industry’s indirect impact on Australian society and its economy. The industry’s role as an essential service was emphasized:

Every Australian business, and every Australian citizen, uses the built environment (Cole 2003, vol. 1, p. 3).

The industry’s impact on the economy was also highlighted:
All industries would benefit from an increase in output as a result of the reduction in the cost of building and construction (Cole 2003, vol. 1, p. 3).

The RCR goes on to quantify the negative impact the industry’s poor performance had on Australia’s economy and the positive outcomes that may be expected if the industry improved.

Were productivity growth to match that of the market sector, economic modeling shows that the accumulated gain in real gross domestic product between 2003 and 2010 would approximate $12 billion. Modelling shows that if that occurs, all sectors of the economy benefit:

- workers benefit from the 12 per cent pay rise in the first three years;
- the building industry benefits from output growth of 0.6 per cent by 2010;
- Australia benefits from an accumulated increase in real gross domestic product of $11.5 billion by 2010;
- exports would grow and imports fall; and
- output of all industries would grow with particular benefits to manufacturing and processing industries (Cole 2003, vol. 1, p.3).

In taking this view, the RC was developing a business case for the need for reform of the Industry. It is clear that the industry is important to Australia and it provides many direct and indirect benefits for the country. To unlock these benefits, the RC argued that productivity must increase (Cole 2003, vol. 1, p.3). The reforms recommended by the RC laid the blame for the industry’s poor performance with its culture, manifested in terms of unlawful behaviour. This section has suggested that part of the Industry’s cultural problems was that its sense of importance led to perceptions that could operate outside the law. The structural reforms recommended by the RC essentially indicated that the industry needed to change the way it does business if it was to improve its productivity and achieve its economic potential. The industry structure which existed prior to the RC was characterised by competition between construction firms (macro-level) and between industry stakeholders (micro-level). The intensity of competition was so high that it caused dysfunctional behaviour. Research has shown that competition levels correlate with profit; the higher the competition, the lower the profit
(Grant 2013). The analysis which follows will explain the nature of competition in the construction industry. The level of competition is the main reason for the industry’s under-performance and explains why it has a profit margin of only 3.3% in 2011-2012 (ABS 2013, p.10).

3.5 The Australian Construction Industry’s Structure

3.5.1 Competition between Firms

Industry concentration is an important factor explaining competition levels because it influences price competition (Grant 2013). Industries with high concentration, for example a single dominant player such as Microsoft, can charge whatever prices they like. Those with two or three dominant players, such as an oligopoly, may create price restraint, sometimes through “collusion” but otherwise via parallel pricing (Grant 2009, p. 78). Under these industry conditions, competitors must match rivals’ pricing in order to be competitive. As the number of firms supplying a market increases, coordination of prices becomes more difficult and the likelihood that one firm will seek to attract customers via price cutting will increase (Grant 2009, p. 78).

The analysis which follows is based on the data that was available from industry reports and the ABS. This data generally covered the period 2010 to 2013. However, it is used to illustrate the nature of competition in the construction industry. The following tables provide industry statistics for the period 2001-2015 to provide trend analysis at a broad level.
## Table 3.3: Industry Data

<table>
<thead>
<tr>
<th></th>
<th>Revenue ($m)</th>
<th>Value Added ($m)</th>
<th>Establishments</th>
<th>Enterprises</th>
<th>Employment (People)</th>
<th>Wages ($m)</th>
</tr>
</thead>
<tbody>
<tr>
<td>2001-02</td>
<td>166,564.20</td>
<td>51,746.10</td>
<td>301,733.00</td>
<td>281,687.00</td>
<td>665,024.00</td>
<td>24,385.60</td>
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<tr>
<td>2002-03</td>
<td>185,231.70</td>
<td>55,532.20</td>
<td>313,157.00</td>
<td>289,509.00</td>
<td>688,607.00</td>
<td>25,859.70</td>
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<tr>
<td>2003-04</td>
<td>203,334.60</td>
<td>60,780.30</td>
<td>332,691.00</td>
<td>303,048.00</td>
<td>801,058.00</td>
<td>30,620.00</td>
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<tr>
<td>2004-05</td>
<td>234,351.10</td>
<td>69,065.00</td>
<td>336,936.00</td>
<td>308,405.00</td>
<td>875,556.00</td>
<td>34,850.90</td>
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<tr>
<td>2005-06</td>
<td>273,509.40</td>
<td>75,201.10</td>
<td>352,188.00</td>
<td>322,404.00</td>
<td>985,000.00</td>
<td>38,608.50</td>
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<tr>
<td>2006-07</td>
<td>286,370.40</td>
<td>78,343.90</td>
<td>373,026.00</td>
<td>341,306.00</td>
<td>1,031,000.00</td>
<td>41,594.90</td>
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<td>2007-08</td>
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<td>75,332.20</td>
<td>388,534.00</td>
<td>355,324.00</td>
<td>1,030,000.00</td>
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<td>2008-09</td>
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<td>76,185.60</td>
<td>395,737.00</td>
<td>361,908.00</td>
<td>1,058,840.00</td>
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<td>2009-10</td>
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<td>80,862.10</td>
<td>417,756.00</td>
<td>380,173.00</td>
<td>1,158,490.00</td>
<td>44,517.60</td>
</tr>
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<td>2010-11</td>
<td>319,284.00</td>
<td>83,231.30</td>
<td>429,847.00</td>
<td>390,793.00</td>
<td>1,207,725.00</td>
<td>45,741.80</td>
</tr>
<tr>
<td>2011-12</td>
<td>330,682.00</td>
<td>86,018.20</td>
<td>441,963.00</td>
<td>401,412.00</td>
<td>1,250,841.00</td>
<td>47,228.40</td>
</tr>
<tr>
<td>2012-13</td>
<td>343,248.00</td>
<td>88,927.70</td>
<td>454,097.00</td>
<td>412,031.00</td>
<td>1,298,373.00</td>
<td>48,692.50</td>
</tr>
<tr>
<td><strong>Economy rank</strong></td>
<td><strong>119/706</strong></td>
<td><strong>97/706</strong></td>
<td><strong>49/617</strong></td>
<td><strong>65/603</strong></td>
<td><strong>140/697</strong></td>
<td><strong>335/621</strong></td>
</tr>
</tbody>
</table>

(Source: Kelly, 2016a)

## Table 3.4: Annual Change

<table>
<thead>
<tr>
<th></th>
<th>Revenue (%)</th>
<th>Industry Value (%)</th>
<th>Establishments (%)</th>
<th>Enterprises (%)</th>
<th>Employment (%)</th>
<th>Wages (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>2001-02</td>
<td>N/A</td>
<td>N/A</td>
<td>N/A</td>
<td>N/A</td>
<td>N/A</td>
<td>N/A</td>
</tr>
<tr>
<td>2002-03</td>
<td>11.2</td>
<td>7.3</td>
<td>3.8</td>
<td>2.8</td>
<td>3.5</td>
<td>6.0</td>
</tr>
<tr>
<td>2003-04</td>
<td>9.8</td>
<td>9.5</td>
<td>2.2</td>
<td>2.7</td>
<td>8.0</td>
<td>10.6</td>
</tr>
<tr>
<td>2004-05</td>
<td>4.8</td>
<td>4.8</td>
<td>4.0</td>
<td>1.9</td>
<td>7.7</td>
<td>7.0</td>
</tr>
<tr>
<td>2005-06</td>
<td>10.2</td>
<td>8.8</td>
<td>1.3</td>
<td>1.8</td>
<td>9.3</td>
<td>13.8</td>
</tr>
<tr>
<td>2006-07</td>
<td>16.8</td>
<td>8.5</td>
<td>4.5</td>
<td>4.5</td>
<td>12.5</td>
<td>10.8</td>
</tr>
<tr>
<td>2007-08</td>
<td>4.7</td>
<td>4.2</td>
<td>5.9</td>
<td>5.9</td>
<td>4.7</td>
<td>7.7</td>
</tr>
<tr>
<td>2008-09</td>
<td>-2.6</td>
<td>-3.8</td>
<td>4.2</td>
<td>4.1</td>
<td>-0.1</td>
<td>1.1</td>
</tr>
<tr>
<td>2009-10</td>
<td>2.1</td>
<td>1.1</td>
<td>1.9</td>
<td>1.9</td>
<td>2.8</td>
<td>0.3</td>
</tr>
<tr>
<td>2010-11</td>
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<td>2.7</td>
<td>2.3</td>
<td>2.3</td>
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<tr>
<td>2011-12</td>
<td>4.4</td>
<td>3.4</td>
<td>3.1</td>
<td>2.6</td>
<td>4.4</td>
<td>2.5</td>
</tr>
<tr>
<td>2012-13</td>
<td>4.1</td>
<td>2.9</td>
<td>2.9</td>
<td>2.8</td>
<td>4.2</td>
<td>2.7</td>
</tr>
<tr>
<td>2013-14</td>
<td>3.6</td>
<td>3.3</td>
<td>2.8</td>
<td>2.7</td>
<td>3.6</td>
<td>3.3</td>
</tr>
<tr>
<td>2014-15</td>
<td>3.8</td>
<td>3.4</td>
<td>2.7</td>
<td>2.6</td>
<td>3.8</td>
<td>3.1</td>
</tr>
<tr>
<td><strong>Economy rank</strong></td>
<td><strong>119/706</strong></td>
<td><strong>97/706</strong></td>
<td><strong>49/617</strong></td>
<td><strong>65/603</strong></td>
<td><strong>140/697</strong></td>
<td><strong>335/621</strong></td>
</tr>
</tbody>
</table>

(Source: Kelly, 2016a)
The tables show that the construction industry has steadily grown since the period around the RC in 2003 (see table 3.3). In terms of competition, the growth in number of firms was steady with an exception in 2006-2009 where there was above average increase. The growth in revenues was strongest in the year before the RC, and a few years afterwards in 2005-2007, but weaker in other years suggesting more competition for work (see table 3.4). The average revenue per employee and the average wages have hardly changed since 2003, further illustrating the stable nature of competition since the time of the RC. In general terms, the tables suggest stability in the nature of competition, which means it is reasonable to assume the detailed analysis of the
industry which follows may be indicative of the nature of competition at the time of the RC.

The construction industry is a very fragmented industry, in the sense that it has many competitors and the industry is not concentrated. Industry concentration measures the extent to which the top four players dominate an industry (Grant 2002, p. 78). In 2009-10, the construction industry had a low level of concentration with the major players accounting for less than 10.0% of total revenue (Dunn 2010, p. 19). The industry is Australia’s second most fragmented after agriculture (Dunn 2010, p.19). This reflects, in part, the very diverse nature of the industry which is characterised by significant variations in the type of activity undertaken, the size of players, the level of capital intensity (Dunn 2010, p.19), high proportion of non-employers, that is, sole operators. As a fragmented industry the large number of firms makes price an important competitive strategy and leads to high intensity of competition.

The first industry sector examined is residential construction. This sector represents AUD$59.3 billion in revenues and it has 25,686 firms employing 101,000 people (ABS 2013). The residential construction sector may be further classified into two segments: housing construction and multi-unit apartment and townhouse construction. The housing construction segment is defined by intense competition. It has low concentration of ownership, causing a fragmented structure, and is characterised by its many small-scale firms which operate in narrow regional markets. Only around 3.0% of firms employ more than 20 persons, and only 46 firms (0.1%) employ more than 200 people (ABS 2013). These statistics provide important insight into industry structure and competition in the housing segment. There are many very small firms (30,429) who employ 19 staff or less (ABS 2013). It suggests intense competition where customers can trade off builders on price. This means that it is difficult to differentiate and the only
way to be successful is to tender the lowest price. Intense price competition means firms with successful cost leadership will survive (Grant 2013). Cost leadership in the housing segment occurs by lowering costs in the areas of building materials and labour. The small firms are competing on price and operating on very small profit margins.

In 2017, the housing industry generated $42.5 billion in revenue, profit of $3.5 billion, wages of $3.9 billion, 41,750 businesses, historical growth (2012-2017) of 1.4%, and projected growth (2017-2012) of 1.7% (Kelly 2017a, p. 2). The statistics hide the fact that the bigger firms have a relatively high market share. The major players are multi-establishment operations with a presence across several states and many regional markets (Kelly 2017a, p. 1). While the four largest homebuilders account for less than 10% of annual industry revenue, the top 100 builders in Australia account for around 41% of the national housing market (Housing Industry Association 2015). Nevertheless, the housing segment is very fragmented.

The main basis for competition in the housing construction segment is product differentiation, based on proven quality, efficiency and timeliness. Price differentiation becomes an important basis for competition when the potential builders satisfy these other prerequisites (Kelly 2017a, p. 6). While price is important, the most important factor is market reputation in terms of quality and track record in areas of efficiency and timeliness. Being an established, large firm probably has advantages here over smaller firms. In terms of geography, the most states with the most building activity are, in order: Victoria, Queensland, and New South Wales, however, the industry is increasingly globalising with the entry of overseas firms (Kelly 2017a, p. 6). Overall, the housing construction industry segment’s level of competition is rated high and likely to increase further.
The other residential segment is multi-unit apartment and townhouse construction. In 2016, this industry generated $19.3 billion in revenue, profit of $1.6 billion, wages of $1.8 billion, 14,780 businesses, historical growth (2012-2017) of 6.1%, and projected growth (2017-2012) of 2.3% (Kelly 2016a, p. 2). The segment has a low concentration of ownership despite the existence of several very large scale players. The four largest players in this segment are currently estimated to account for 21.6% of total industry revenue (Kelly 2016a, p. 7). This segment is very interesting because the major players in the non-residential sector also compete in this sub-segment. Therefore, the multi-unit apartment and townhouse construction segment represents a move into the residential sector for firms traditionally in the non-residential sector. Contrary to the traditional housing construction segment, this segment has a relatively high proportion of activity undertaken by medium to large scale operators, such as Leighton, Multiplex and Bilfinger Berger, which principally operate in the non-residential building and engineering construction sectors. Other leading players such as BGC and Mirvac have substantial operations in the traditional housing industry.

Contracts to this industry are awarded based on a combination of factors, of which price is seldom the principal consideration. Firms are invited to tender for projects based on factors such as: proven reputation for quality; timeliness; financial security; and efficiency (Kelly 2016a, p. 6). Price differentiation becomes an important basis for competition after the abovementioned prerequisites have been met. Small-scale operators rely heavily on word of mouth referrals to obtain contracts and network with property developers, financial institutions and real estate agents within their regional market (Kelly 2016a, p. 6). These relationships are usually based on reputation to complete projects within budget and on time.
Large scale contractors in this industry are increasingly taking an equity interest in property development consortia (Kelly 2016a, p. 6). This equity stake effectively blocks competition from other builders and ensures the flow of work for the equity participant. This trend towards equity involvement by the builder is apparent across all scales of construction but most evident in landmark projects such as Docklands developments in Melbourne and Delfin Lend Lease’s Greystanes quarry site in Sydney. The promotion of sales through the construction of speculative developments tends to be limited to the medium to large scale builders. The labour intensive nature of this segment limits the benefits achieved from economies of scale in the construction process. However there are some areas where economies can be achieved, particularly in marketing and materials purchasing (Kelly 2016a, p. 6). Scale economies are also evident in the purchase of inputs materials as large-scale companies typically standardise the material requirements across a wide range of designs and receive substantial discounts by bulk purchasing a particular line of bricks or tiles etc. Smaller scale operators receive trade discounts from material suppliers but are generally unable to buy inputs at the same price as the larger companies (Kelly 2016a, p. 6).

The multi-unit apartment and townhouse market segment is characterised by a high degree of internal and external competition. The industry includes many small and medium scale players competing for a share of regional markets, and several larger scale players capable of competing across the national market. The smaller scale players are generally excluded from competing at the top end of the market, whereas the larger players can compete for all scale of construction (Kelly 2016a, p. 6). The demarcation between property developer and prime contractor is blurred for many large scale inner city developments in the multi-unit apartment and townhouse market. Mirvac for example was both developer and prime contractor on several of Australia’s largest
projects in the late 1990s, including the Olympic Village at Homebush, with smaller building firms subcontracting to complete discrete segments of these projects (Kelly 2016a, p. 6). There is a high degree of overlap between the multi-unit dwelling market and the housing and non-residential building market and firms in this industry are increasingly confronted with competition from firms principally operating in these other building markets (Kelly 2016a, p. 6). When the other building markets are confronted by cyclical declines in demand, firms typically cross into the multi-unit dwelling market to chase contracts. The larger commercial builders are able to bring knowledge, reputation and financial relationships to compete in this market (Kelly 2016a, p. 6).

The second industry sector examined is non-residential construction. This represents AUD$42.3 billion in revenues and it has 5,612 firms employing 59,000 people (ABS 2013). The non-residential construction sector may be further classified into two segments: Commercial and Industrial Building Construction and Institutional Building Construction.

The first industry segment in the non-residential sector is the commercial and industrial building construction. In 2016, this industry generated $34.7 billion in revenue, profit of $1.8 billion, wages of $4.2 billion, 9,890 businesses, historical growth (2012-2017) of 2.1%, and projected growth (2017-2012) of 1.3% (Kelly 2016b, p. 2). The four largest contractors generate less than 10% of annual industry revenue (Kelly 2016b, p. 7). Relatively few companies are capable of competing for the large scale “landmark” projects, such as sporting stadiums and multi-story office complexes. Therefore despite the low concentration of ownership, the few large firms exercise some degree of influence over market trends. Over the past decade there has been a trend towards greater concentration of ownership among the major players. Leighton Holdings
acquired the John Holland Group which in turn acquired Transfield Construction. Bilfinger and Berger, the parents of Baulderstone Hornibrook acquired Abigroup Limited, and Downer EDI Limited acquired Stork ICM.

Competition is principally based on proven quality, efficiency and timeliness rather than pricing (Kelly 2016b, p. 6). In practice, the smaller the project the more important price competition becomes as the basis for differentiation (Kelly 2016b, p. 6). Large-scale projects are usually put to tender, either a public tender advertised in the newspaper or to closed tender (selected contractors invited to tender) (Kelly 2016b, p. 6). The selection of contractors for a closed tender is based on reputation and close relationships with developers, financiers and other related parties (Kelly 2016b, p. 6).

The second segment in the non-residential sector is institutional building construction. In 2016, this industry generated $11.6 billion in revenue, profit of $0.8 billion, wages of $1.4 billion, 3,275 businesses, historical growth (2012-2017) of -3.0%, and projected growth (2017-2012) of 3.7% (Kelly 2016c, p. 2). The industry has a low concentration of ownership, with the four largest contractors accounting for around 20% of annual industry revenue (Kelly 2016c, p. 7). The industry is understood to have a higher concentration of activity than most of the construction industry as few firms are capable of competing for the large scale “landmark” projects from Federal court buildings to hospital complexes.

The market for institutional building construction is characterised by intensely competitive conditions, particularly between the many small to medium scale contractors which compete for a share of activity in relatively narrow regional markets (Kelly 2016c, p. 6). Industry competition is based on differentiation between builders on the basis of proven quality, efficiency and timeliness rather than solely on pricing.
Large-scale projects are usually put to tender, either a public tender advertised in the newspaper or through the government gazettes, or to closed tender where the client invites selected contractors to tender for a project (Kelly 2016c, p. 6). The selection of contractors for a closed tender is based on reputation (past performance) and close relationships with developers and public sector procurement officers (Kelly 2016c, p. 6).

Several builders have established reputations for the construction of specialist buildings such as hospitals such as Thiess Contractors and Baulderstone Hornibrook, and these firms effectively establish a basis upon which to attract further contracts from other regional authorities (Kelly 2016c, p. 6).

While in broad terms, the institutional construction market has similar competitive dynamics as the other segments, it can see from the above that the nature of competition is different to other construction segments. Tendering is the preferred buying process and reputation (track record) and relationships are key success factors for winning contracts (Kelly 2016c, p. 6). Being in business for many years is a real advantage in this market. In terms of geography, the states with the most building activity are: New South Wales, Queensland, and Victoria are all about the same size in terms of markets, followed by Western Australia (Kelly 2016c, p. 6).

The third industry sector is heavy and civil engineering construction. This represents AUD$37.8 billion in revenues and it has 7,300 businesses and wages of $10.8 billion (Kelly 2017b, p. 2). The fourth industry sector is concreting services. It is included to illustrate the type of construction services supporting the major industry segments. This represents AUD$7.7 billion in revenues and it has 11,650 businesses and wages of $1.7 billion (Kelly 2016d, p2). These sectors are excluded from this study as the aim is to
focus on the residential and non-residential sectors because these firms were most involved in the RC.

3.5.2 The Impact of Competition on Industry Structure

The analysis has shown how competition was intense in all construction industry segments. There are two broad conclusions that may be drawn in terms of the impact of competition on industry structure. First, while the whole construction industry suffers from intense competition, there are differences in the levels of competition amongst the segments. These differences influence the structural issues that led to the RC. Segments with less intensity of competition, measured by higher profitability, may have experienced less pressure to “bend the rules” in terms of their financial management and reporting, therefore being more compliant with the industry’s social contract.

The second broad conclusion that may be drawn is that there were important differences between large and small firms across all segments. Large firms, head contractors, tend to compete against other large firms. Smaller firms, subcontractors, tend to compete against other small firms. Firm size has a direct impact on changes in the construction industry’s structure. The following table presents a trend analysis of number of firms by employment to illustrate changes in firm size over the past 25 years. The gross product per person employed figure is used as a proxy for firm performance, that is, productivity.
Table 3.6: Firm Size Distribution of Employment and Gross Product Trend Analysis

<table>
<thead>
<tr>
<th>Firm-Size Employment</th>
<th>1-19 staff</th>
<th>&gt;20 staff</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>1988-89</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Employment x Firm Size ‘000</td>
<td>265.0</td>
<td>130.0</td>
<td>395.0</td>
</tr>
<tr>
<td>Employment x Firm Size percentage no. of total firms</td>
<td>67.1</td>
<td>32.9</td>
<td>100</td>
</tr>
<tr>
<td>No. of firms</td>
<td>95,803</td>
<td>2,255</td>
<td>98,059</td>
</tr>
<tr>
<td>Gross product per person employed $’000</td>
<td>31.8</td>
<td>54.9</td>
<td>39.7</td>
</tr>
<tr>
<td><strong>1996-97</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Employment x Firm Size ‘000</td>
<td>417.9</td>
<td>66.0</td>
<td>484.1</td>
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<tr>
<td>Employment x Firm Size percentage no. of total firms</td>
<td>86.4</td>
<td>13.6</td>
<td>100</td>
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<tr>
<td>No. of firms</td>
<td>193,100</td>
<td>1,200</td>
<td>194,300</td>
</tr>
<tr>
<td>Gross product per person employed $’000</td>
<td>29.9</td>
<td>60.0</td>
<td>33.4</td>
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<td><strong>2011-12</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Employment x Firm Size ‘000</td>
<td>590</td>
<td>360</td>
<td>950.0</td>
</tr>
<tr>
<td>Employment x Firm Size percentage no. of total firms</td>
<td>62.1</td>
<td>37.9</td>
<td>100</td>
</tr>
<tr>
<td>No. of firms</td>
<td>204,949</td>
<td>4,834</td>
<td>209,783</td>
</tr>
<tr>
<td>Gross product per person employed $’000</td>
<td>n/a</td>
<td>n/a</td>
<td>98.6</td>
</tr>
</tbody>
</table>

(Source: Toner 2006 for the 1988-89 and 1996-97 figures, which were calculated from ABS statistics. The 2011-2012 data was gathered from ABS 2012.)

The data sources define small firms in this way (for example, less than twenty staff). The RCR defines small firms as less than five employees (Cole 2003, vol. 1, p.13). The ABS defines these as micro firms. The thesis adopts the RCR definition (as explained earlier section 3.2.4), however, this current analysis reports the data from these alternative sources and the definitions that they provide.

Table 3.6 highlights several important points about firm size for industry structure analysis. First, in terms of total employment, the industry has more than doubled since 1988-89, increasing from 395,000 to 950,000. Second, in terms of employment by firm size, there was a big shift towards smaller firms between 1988-89 and 1996-97, which then swung back towards larger firms in 2011-12. In 1988-89, small firms employed
67.1% of the industry’s staff; in 1996-97, this had increased to 86.4%. This shows how there was an explosion in very small firms as tradespeople realised it was easy to set up as small business owners and subcontract to larger firms. However, in 2011-12 the balance had swung back the other way and large firms now represent a higher proportion of the industry’s employment than in 1988-89. Third, in terms of number of firms, there was an explosion in the period 1988-89 and 1996-97, where the number of firms more than doubled. However, the number of large firms almost halved in this period, so the growth was driven by new small firms. In 2011-12, the total number of firms had only increased by 8.0% since 1996-97. However, the number of large firms had increased by about 400%. Fourthly, in terms of gross product per person employed, the figures decreased by 15.8% in the period 1988-89 and 1996-97, however, it had increased significantly, by 195%, by 2011-12. This indicates that the construction industry’s productivity had increased significantly in the period since the RC.

This trend analysis highlights that the construction industry moved towards more small firms (subcontractors) and fewer large firms (head contractors) in the decade leading up to the RC but has since swung back towards more head contractors in the decade after the RC. These changes in industry structure had an impact on the nature of competition and the way business was conducted. Firstly, it seems the structural reforms of the RC have been successful, in the sense that the socio-political power inequities created by the high proportion of subcontractors has been reduced in the decade following the RC. While there is still many small firms, there has been a swing towards larger firms in terms of number of these firms and their proportion of the industry’s employment. Large firms now represent a higher distribution than 1988-89 figures.

The existence of considerable risk for firms in the construction industry is one of the factors leading to extensive subcontracting. The level of risk for each firm has
increased, especially on larger projects due to the shift from cost-plus to fixed price contracts (Toner 2006). Fixed price contracts were introduced in the later 1980s and became the norm in the early 1990s (Toner 2006). Previously cost-plus contracts placed most of the risk of cost overruns and time delays on the developer or owner of a building project (Toner 2006). A portion of the risk faced by the head contractor is passed down the contractual chain to each subcontractor with fixed price contracts (Toner 2006). That is, subcontractors also face penalties for delays and are paid a fixed price for their services (Productivity Commission 1999, p. 14). It is arguable that heightened risk facing each firm involved in larger construction projects has created an incentive towards greater subcontracting (Toner 2006).

There was a trend towards outsourcing in the 1990s which influenced the boom in small construction firms. There are five inter-related management rationales for introducing outsourcing. Hall and Bretherton (1999) believe these relate to:

- risk reduction as described above; meeting peak demand for output by outsourcing production; buying-in specialised technology, equipment or skills;
- cost reduction by focussing on the competitive strengths of the firm and buying in non-core products and services; and, introducing market discipline within the organisation out-sourcing activity and amongst external suppliers of services or goods by encouraging increased competition (p. 20).

The outsourcing argument receives considerable support from the fact that the bulk of increase in employment and number of firms has occurred in the construction trade services segment of the construction industry (Construction Training Australia 2007). This segment provides specialised services such as excavation, plumbing, carpentry, bricklaying, electrical, concreting and painting, purchased by firms engaged in Residential, Non-Residential and Engineering Construction (Construction Training Australia 2007). Further support for the view that larger firms are seeking to cut costs is provided by data showing differential movements in output per worker between large
and small firms. Between 1988-89 and 1996-97 nominal gross product per person in establishments with employment of more than 20 persons increased by 9.2 per cent. It is probable that larger firms are subcontracting an increasing share of the on-site construction work to construction trade services and specialising and retaining more value-added work such as project bidding; design; financial management; project management and engineering (Toner 2006).

3.6 The Australian Construction Industry’s Stakeholders

There are multiple stakeholders who have an interest in the activities and performance of the construction industry. These stakeholders interact and their social behaviour when interacting was a critical factor in the social contract breach that led to the RC. There are two types of stakeholders: private stakeholders and public stakeholders.

ST considers the various groups that exist in society, and how the expectations of each group may have more (or less) impact on corporate strategies (Deegan 2009, pp. 346-347). The main private stakeholders in the construction industry are:

1. Owners/Shareholders
2. Staff including:
   a. Management
   b. Engineers
   c. Project Managers
   d. Accountants
   e. Human Resources
   f. Other employees
This list is based on interpretation of industry participants derived from the thesis’s analysis of the RCR. The following table (table 3.7) presents an introduction to the role, expectations, and impact of each of these groups in the construction industry’s social contract. The comments represent underlying assumptions about each stakeholder, which are connected to the research themes (see section 2.4 in chapter 2), and will be examined in later chapters. These assumptions are based on the thesis’s interpretation of the stakeholders’ attitudes and behaviours (see chapters 5 and 6).

<table>
<thead>
<tr>
<th>Stakeholder</th>
<th>Role</th>
<th>Expectation</th>
<th>Impact</th>
<th>Research Objective chapter 2</th>
</tr>
</thead>
<tbody>
<tr>
<td>Owners/Shareholders</td>
<td>Monitor performance</td>
<td>Profit driven</td>
<td>Strong drive towards non-compliance via pressure on management</td>
<td>4, 7, 10, 11, 12, 13, 14, 15</td>
</tr>
<tr>
<td>Management</td>
<td>Make decisions</td>
<td>Job security</td>
<td>Drive towards non-compliance via pressure on project managers and engineers</td>
<td>4, 7, 10, 11, 12, 13, 14, 15</td>
</tr>
<tr>
<td>Project Managers</td>
<td>Complete construction jobs</td>
<td>On time, on budget</td>
<td>Drive towards non-compliance via pressure on staff</td>
<td>4, 10,12</td>
</tr>
<tr>
<td>Engineers</td>
<td>Quality control</td>
<td>Customer satisfaction</td>
<td>Drive towards non-compliance via pressure to cut corners</td>
<td>10,12</td>
</tr>
</tbody>
</table>
Table 3.7: Private Stakeholder Overview and Underlying Assumptions

<table>
<thead>
<tr>
<th>Stakeholder</th>
<th>Role</th>
<th>Expectation</th>
<th>Impact</th>
<th>Research Objective chapter 2</th>
</tr>
</thead>
<tbody>
<tr>
<td>Accountants</td>
<td>Apply standards</td>
<td>Report truth</td>
<td>Drive towards compliance via negotiation with management and project managers</td>
<td>3, 10, 11, 12, 14, 16</td>
</tr>
<tr>
<td>Human Resources</td>
<td>Staff productivity</td>
<td>Staff morale</td>
<td>Drive towards compliance via representing staff to management</td>
<td>10, 12</td>
</tr>
<tr>
<td>Other Employees</td>
<td>Do the work</td>
<td>Firm survival</td>
<td>Responsive to pressures</td>
<td>10, 12</td>
</tr>
</tbody>
</table>

The main public stakeholders in the construction industry are:

1. Regulators/Government
2. Unions
3. Accounting bodies
4. Auditors
5. Customers
6. Public generally

This list is based on interpretation of industry participants derived from the thesis’s analysis of the RCR. The following table (table 3.8) presents an introduction to the role, expectations, and impact of each of these groups in the construction industry’s social contract. The comments represent underlying assumptions about each stakeholder,
which are connected to the research themes (see section 2.4 in chapter 2), and will be examined in later chapters. These assumptions are based on the thesis’s interpretation of the stakeholders’ attitudes and behaviours (see chapters 5 and 6).

<table>
<thead>
<tr>
<th>Stakeholder</th>
<th>Role</th>
<th>Expectation</th>
<th>Impact</th>
<th>Research Objective (chapter 2)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Regulators/Government</td>
<td>Monitor public interest</td>
<td>Social contract is followed</td>
<td>Strong drive towards compliance via pressure on owners and management</td>
<td>1,2,3,5,6,8,9,13,14</td>
</tr>
<tr>
<td>Unions</td>
<td>Advocate for staff</td>
<td>Job rewards</td>
<td>Very strong drive towards compliance via pressure on owners and management</td>
<td>2,5,6,7,9,10,11,12,13</td>
</tr>
<tr>
<td>Accounting bodies</td>
<td>Ensure compliance with standards</td>
<td>Follow the rules</td>
<td>Drive towards compliance via pressure on owners and management</td>
<td>3,14,16</td>
</tr>
<tr>
<td>Auditors</td>
<td>Monitor and report on compliance with standards</td>
<td>Evidence of following the rules</td>
<td>Drive towards compliance via pressure to management</td>
<td>3,14,16</td>
</tr>
</tbody>
</table>
Table 3.8: Public Stakeholder Overview and Underlying Assumptions

<table>
<thead>
<tr>
<th>Stakeholder</th>
<th>Role</th>
<th>Expectation</th>
<th>Impact</th>
<th>Research Objective (chapter 2)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Customers</td>
<td>Seek and receive construction services</td>
<td>Quality work on time and at low cost</td>
<td>Drive towards non-compliance via pressure on project managers</td>
<td>15</td>
</tr>
<tr>
<td>Public generally</td>
<td>Economic benefit</td>
<td>Corporate citizenship</td>
<td>Drive towards compliance via indirect pressure on owners</td>
<td>1, 2, 4, 5, 6, 13, 14, 15</td>
</tr>
</tbody>
</table>

Each stakeholder is expected to have different roles, expectations, and impact in terms of the construction industry’s compliance with the social contract. The stakeholder groups interact by placing pressure on other groups and in how they respond to these pressures.

3.7 Conclusions

This chapter defined the construction industry, discussed its history, explained the Australian public’s interest in the industry, defined the industry’s structure, and described the industry’s stakeholders. In doing so, it established a platform for the remainder of the thesis by setting boundaries around the study and identifying what it is that is being studied. Given this thesis is a historical narrative of the Australian
construction, it is important to know what happened before the period of focus, 2001 to 2003, to understand some of the factors which led to the social contract breach. The industry was defined as firms competing in residential and non-residential building, with a particular focus on firm size, and an interest in differences by geography (state). The study does not include firms offering engineering construction, and does not examine industry segments in the sense of product or service classifications. The behaviours which led the RC to conclude that the industry was unlawful did not suddenly emerge. These behaviours were embedded in organisational practices, systems, norms and values. Examining the history of the industry from a sociological perspective, leads to understanding why these unlawful behaviours became the norm.

The turning point appears to be a change in political ideology, brought about by the emergence of communism and its adoption by union leaders, particularly from the 1950s onwards. The prosperity of the 1960s boosted union membership and strength.

The 1970s saw a fundamental shift in the industry’s socio-political landscape with unions taking control and dictating the rules of stakeholder interaction. This evolved in the 1980s and 1990s into a culture that communicated the belief that those in power could ignore the law and do things their way. The construction industry has significant economic and social importance. The second paragraph in the RCR explained that the industry “is critical to welfare and prosperity in Australia” (Cole 2003, vol. 1, p. 3). Furthermore, the industry has widespread indirect impact on other sectors of the economy. However, it is not just economically important. In terms of LT, it provides services that make it highly desirable to society. The industry structure which existed prior to the RC was characterised by competition between construction firms (macro-level) and between industry stakeholders (micro-level). These stakeholders were dominated by owners/managers and the trade unions. However, there were a range of
internal and external stakeholders involved in the construction industry’s unlawful behaviour. The intensity of competition was so high that it caused dysfunctional behaviour. Research has shown that competition levels correlate with profit; the higher the competition, the lower the profit (for example, see Grant 2013). The analysis which follows will explain the nature of competition in the construction industry. The level of competition is the main reason for the industry’s under-performance.
CHAPTER 4: HISTORY OF REGULATION

4.1 Introduction

This chapter examines the history of the regulation of the construction industry. The purpose of this chapter is to examine society’s expectations of this industry, its social contract, and its behaviour compared with expectations, using the findings of the RC and associated documents. The chapter includes a discussion of what happened after the RC in terms of legislative change and other regulation, including the activities and reports of a new body, Fair Work Building & Construction (FWBC). The chapter explains the need for regulation of this industry, how this was done, and the industry response.

4.2 Industry Regulation Prior to the Royal Commission

4.2.1 Introduction

The construction industry had a long history of legitimacy, as discussed in chapter 3. The industry was important to Australia and provided valuable services and, as a result, society conferred access to resources such as labour, materials and capital to construction firms. It was in the public interest that the construction industry used these resources wisely. The cost of housing, for example, is very important to society, and efficient use of resources helps keep housing prices low.
LT examines how society becomes aware of social contract breaches in terms of organisational shadow (Bowles 1991) and intolerable inequities (Deegan 2009). Organisational shadow suggests that inappropriate behaviour is hidden from society, and that society suddenly becomes aware that the industry's behaviour was undesirable, and having a negative impact on society. This occurs through a whistle blower, media investigation, or a sudden critical event that becomes public. Intolerable inequities describe behaviour that society is aware of and has either been ignoring or has been trying to moderate. This takes place when society loses patience because the behaviour’s impact was having a more serious effect on society. This study concludes that the social contract breach by the construction industry occurred due to the Intolerable Inequities Scenario (IIS).

4.2.2 How Society Lost Patience with the Construction Industry

The IIS suggests that the construction industry’s tendency towards unlawful behaviour has always been known to the regulator, the government, but that the situation suddenly became intolerable and forced action with increased regulation. In this scenario, the regulator is somewhat tolerant about the social contract breach. They are aware of the market inefficiencies and inequitable distribution of resources within the industry, but they allow it to continue (Deegan 2013). The regulator might do this because they feel the social contract breach is relatively minor or perhaps because the reasons for giving the industry legitimacy initially, desirability in this case, outweigh the negative impact of the social contract breach.

Given Australia’s cultural traditions, it is not surprising that trade unionism found a strong foothold in the construction industry. The workers in the construction industry were mainly labourers or tradespeople who worked for wealthy land owners or property
developers. The political unrest and sense of social democracy emerging in England in the mid to late 19th century found strong support amongst the working class in Australia. In the 1930s the spread of communism found a voice in the trade union leaders of the time. In this way, the history of the trade union movement in Australia is the proud legacy of the working class movement in Australia (CFMEU Victoria 2010). However, it also illustrates the propensity towards unlawful or rebellious behaviour, as described in chapter 3.

The history of regulation of the construction industry is largely a history of government regulation of its behaviour with a particular focus on the trade union movement. After a false start in 1850, the first union for Victorian stonemasons was established as the Independent Society of Operative Stonemasons of Victoria (ATUA 2002). The Victorian Stonemasons will be remembered for laying down their tools at Melbourne University to mark the win of the eight-hour day. Although legislation was already being incrementally instituted, the Stonemasons lead the celebrations. On the 21 April 1856, stonemasons working at the university marched through the streets of Melbourne, gathering fellow tradesmen on the way to the Victorian Parliament. ‘The gain of the eight-hour day was an astounding international precedent, which working men around the world might aspire’ (Museums Victoria 2016, para. 2), and promoted these stonemasons as national and international pioneers of workers’ rights.

The BLF and its antecedent bodies was a politically active union, and what has been described as “the most effective industrial fighting machine in Australia” (Ross 2004, p. 140), the BLF made significant gains in wages and working hours for its membership, as well as instituting many progressive policies such as “green bans, the permanency scheme, workers' control, encouraging women to work in the industry and limited tenure of office” (Ross 2004, p. 168).
Several trade unions have been outlawed, that is de-registered, by the Australian Government. The key example is the BLF which formed in 1972, was deregistered in 1974 under the Whitlam Labor government and permanently deregistered in 1986 following legislative changes instituted by the Hawke Labor government (Singleton 1997, p. 298). The sense of social justice, mateship and solidarity within the Australian trade union movement can be illustrated by the formation of the Painters and Decorators Union in Melbourne in 1886. This union sought to ensure sick or unemployed members were cared for, the provision of funerals in the event of a workplace fatality and protection from encroachment by unskilled craftsmen (Spierings, 1994, p. 2). This union was a legacy of the founding of the union movement through the friendly societies of 1790-1820 that focused on benevolence and sense of community.

A strong theme in the evolution of the trade union movement in Australia in the 20th century was the birth of One Big Union (CFMEU WA 2011, p. 7). This idea came about as officials recognised the value of having one, strong industrial union to secure a better bargaining position for workers on construction sites. However, amalgamation of the various unions associated with the construction industry proved difficult:

Bricklayers, Builders' Labourers, Carpenters and Plasterers agreed to form a single union in 1922. But it was not until 1942 that bricklayers and carpenters effectively amalgamated to form the Building Workers Industrial Union, which became a federal organisation in 1943. Over the following decades, work continued on the formation of one union for the industry with the gradual amalgamation of some of the other building craft unions with the BWIU. For example, the Victorian Tile layers amalgamated in 1964 and Stonemasons in 1965. In WA, the Bricklayers amalgamated with the BWIU in 1968. SA bricklayers decided to form a Branch of the BWIU in 1968. Qld stonemasons and BWIU amalgamated with the bricklayers in 1973. Nationally, the BWIU, the Plasterers Federation and the Operative Painters and Decorators Union also began working on amalgamation from 1966 (CFMEU WA 2011, p. 8).
The emergence of strong industrial unions in the metal industry was viewed as a threat by the Conservative Government of the early 1970s. Consequently, new legislation was enacted preventing any reasonably sized unions from amalgamating. Subsequently, large unions could only amalgamate with small organisations (CFMEU WA 2011, p. 7). However, there were numerous unions spread across construction, forestry, mining and energy industries. In the early 1990s, “One Big Union”, the Construction, Forestry, Mining and Energy Union (CFMEU) Construction and General Division, emerged for the construction industry with a federal structure and representation in every State and Territory (CFMEU WA 2011, p. 7). Those numerous unions amalgamated along industry lines to form each of the divisions of the CFMEU. Each division of the CFMEU operates autonomously, with its own membership, executive, resources, industry policies and campaigns (CFMEU WA 2011, p. 7).

This historical narrative of the construction industry’s trade union movement provides two key findings in relation to the IIS. First, the regulator, the government, has always been aware of the rebellious and at times unlawful behaviour of the trade unions. This is shown by the many battles between the trade union and other stakeholders for more than a century. Second, it shows that the regulator has not always been tolerant of the industry and has intervened when it has lost patience, as illustrated by the serious action of de-registering some trade unions by making their activities illegal. There was a growing awareness of the need for society to impose order on the construction industry in the 1990s, as demonstrated by several state royal commissions (for example, Gyles 1992). However, it was not until 2001 that the Federal Government showed it had lost patience and it announced the most public symbol of dissatisfaction with the industry, a national Royal Commission.
The Dark Shadows Scenario (DSS) scenario suggests that instead of the regulator being aware of problems and deciding not to act, the construction industry’s inappropriate behaviour was hidden from society and it suddenly emerged as having such a negative impact on society that it must be stopped. This scenario suggests the regulator was either unaware of the unsatisfactory behaviour within the industry or that society expectations had changed and what was previously acceptable or tolerated behaviour was no longer so. This raises questions of whether new information emerged which made the regulator see the behaviour as more serious than previously perceived or whether society’s expectations changed just prior to the RC (2003). The main evidence for this scenario is the range of public enquiries into the conduct of the Construction Industry beginning in the 1990s and a major television investigation which culminated in 2001. It suggests that both new information and changes in society’s expectations occurred around the same time.

LT recognises that society’s expectations can change over time. Whereas an industry or organisation might be allocated legitimate status at one time, there is no guarantee that this status is forever. Indeed it is the responsibility of the entity to monitor and respond to changing society demands. The most common example is environmental impact. Deegan (2009, p. 327) cites an example from BHP Billiton on 27 July 2006 where the CEO explained that legitimacy in terms of public opinion was as essential to business survival as any traditional skill such as finance or marketing.

In chapter 3, it was noted how the construction industry gained legitimacy primarily because it was desirable, that is it provided service, accommodation, infrastructure and a standard of living that society valued. However, actions that are proper or appropriate were not always considered positively. The main focus of society’s attention was on the rebellious nature of the industry’s trade unions. Discipline was meted to the industry by
the government in deregistering unions. For many years there seems to have been an uneasy truce between the industry and society, punctuated by conflict between the government and the unions. However, things changed. There came a point when society’s perception of the desirability of the services provided by the industry became outweighed by its dissatisfaction with its actions.

The RC described the construction industry as having a “culture of disregard for the law” (Cole 2003, vol. 1, p.13). This unlawful behaviour was “fostered because of the short term project profitability focus of all those in the industry” (Cole 2003, vol. 1, p.13). Therefore, everyone was blamed and competition was the cause.

### 4.3 Factors Leading to the Royal Commission

A media investigation, broadcast on the respected public affairs television program Four Corners, brought the disorderly behaviour of the construction industry which had continued for decades into the public’s lounge rooms as they watched television. Perhaps the most distasteful finding was the extent of in-fighting between union leaders. Whereas the public could tolerate, to some degree, the militant actions of union leaders fighting for workers’ rights, they were less tolerant of union leaders fighting between themselves for power, along with suggestions of inappropriate financial gains (Neighbour 2001). The Federal Government was embarrassed and the Four Corners investigation forced the regulator to act.

The Australian Federal Government was aware of unsatisfactory industrial relations activity within the construction industry decades before the RC commenced in 2001. The government tried various methods to bring order to the industry including:
discipline, deregistering of construction industry unions in the 1970s and 1980s, and legislation, the *Workplace Relations Act 1974* and the *Trade Practices Act 1974* aimed to provide the legal tools to deliver industry reform. However, these methods failed to deliver satisfactory results. In 1997, the Government introduced the National Building Industry Code of Practice. The Code and the Guidelines were an attempt to regulate the conduct of industrial relations, through the medium of contract rather than legislation, on construction projects funded by government. The aim was to bring order to the industry by setting behavioural guidelines that industry must adhere to if it wished to win Government contracts. The Code of Practice:

Establishes minimum standards businesses must meet to be eligible for Australian Government building and construction work. The National Code and the Implementation Guidelines for the National Code of Practice for the Construction Industry (Guidelines) set out the responsibilities of all parties on construction projects funded by the Australian Government. The Guidelines outline the process for complying with the National Code. The Guidelines were developed to assist the Australian Government and interested parties to interpret and implement the National Code.

The National Code and Guidelines aim to:
- establish higher standards of workplace relations behaviour
- provide greater flexibility and productivity.

They ensure the building and construction industry:
- is client focussed
- has relationships built on trust
- observes ethical principles in tendering
- is committed to continuous improvements and development of best practice.

Parties wishing to ensure compliance with the National Code should use the Guidelines as their first point of reference. The Guidelines are a practical guide to following the National Code.

Compliance with the National Code and Guidelines is a condition of tender for government projects (FWBC 2012c, para. 1).

The Implementation Guidelines summarise the current social contract, that is, what is expected by society from the construction industry in order to gain access to necessary
resources, especially revenues from government contracts. The Guidelines require client focus, trust, ethical behaviour, and improvement. This was a clever way of imposing appropriate behaviour because it offered financial gain in return for following the industry’s social contract. If construction firms wanted to win government contracts they had to comply with the National Code. However, it was not completely successful. There was much work available in the private sector if firms did not wish to follow the National Code.

By the late 1990s neither legislation nor commercial pressure, most especially the National Building Industry Code of Practice, were sufficient to bring order to the construction industry. In April 2001 the then Minister for Workplace Relations, Tony Abbott, asked the Employment Advocate (EA), Jonathan Hamberger, to provide a report regarding “practices in the building industry” (Westmore 2001, para. 1). In a statement released with the announcement of the RC, Minister Abbott cited the report by the EA, dated May 2001, which referred to “allegations about strike pay being extorted from employers, coercion in agreement making, de facto compulsory unionism enforced by some union organisers, payment of bribes and secret commissions, and allegations of the misuse of industry super funds” (Westmore 2001, para. 5). The report combined with a separate investigation by television journalists to highlight the construction industry’s breach of the social contract.

In analysing the report by the EA, (Westmore 2001) identified several important themes for investigation by the RC. First, employers failing to deliver on their obligations to their employees. According to Westmore (2001, para. 11), “one of the reasons why union militants have been able to get away with standover tactics is that some maverick employers operated within the industry, and in the downturn in the housing industry after the introduction of the GST, thousands of building workers lost their entitlements
when the firms which employed them went bankrupt”. This was a political mess for the Federal Government because these workers were not receiving their legal entitlements and, as representatives of society, they expected the Government to act on their behalf. A second theme was union bullying tactics. The report by the EA documented a range of “appalling allegations”, in particular, coercion and intimidation by union delegates, which characterised the industry in several states (Westmore 2001, para. 12). The main type of bullying was to deny employers access to critical resources, such as employees, and threatening strike action unless they used union members and adhered to union demands for employment conditions. Unions also demanded employers used subcontractors of their choice. Essentially the unions blackmailed employers to meet their demands. This unlawful behaviour was the result of the growing power and aggression by some unions beginning in the 1970s. As chapter 3 showed, the unions assumed control of the industry in the 1970s and the report by the EA simply highlighted behaviour that was embedded within the industry’s culture.

The third theme for investigation by the RC was inertia by law enforcement agencies. The report by the EA criticised other law enforcement agencies (including the police) for failing to act on problems in the construction industry, including criminal activity, alleging that complaints “will simply not be actioned with any priority, or at all” (Hamberger 2001, p. 2). It seems that there were two causes of inaction: lack of authority and lack of evidence, due to fear by witnesses. The EA reported that 66 per cent of all complaints received by the Office of the EA by 2000 concerned the building and construction industry and in 2001 the figure had risen to 76 per cent (Hamberger 2001, p. 1). However, it lacked “the power to investigate these allegations, and potential witnesses were unwilling to come forward, due to fears of reprisals” (Westmore 2001, para. 17). This provides evidence for the socio-political power inequities within the
industry at the time. Clearly many people were not happy with these inequities but felt intimidated and unempowered to act. The inability of the authorities to enforce appropriate behaviour added to the feelings of powerlessness.

The issues raised in the report by the EA lay blame on both sides. It seems that employers failed to properly look after employees and workers feared for job security and salary payment. The industry was characterised by smaller operators who collapsed in difficult times leaving their employees without a job and money owing to them. The unions reacted to this by advocating to protect the interests of their members. However, the bullying of employers by unions seemed to cross the line of fair work practice.

The report by the EA indicated that almost all of the complaints received by its Office were from the large commercial sector of the industry, rather than the cottage (home builder) sector (Westmore 2001, para. 13). This means that there was an important ambiguity in the socio-political context of the construction industry stakeholders leading to the RC. While the behaviour of smaller companies seemed to incite the unions to aggressively defend the rights of their members, the unions focused their political action, that is bullying, on the larger companies. The larger companies, in turn, complained to the authorities, such as the Office of the EA, but received no help. The authorities failed to resolve complaints made by the larger companies because they did not have the power to enforce the law. The situation seems to have settled on an uneasy truce where the employers tended to submit to the political force created by the unions in return for access to necessary resources; employees to do the work.

Accounting practice comes under scrutiny because some of the activity resulting from this political pressure involved money, such as unlawful strike pay and bribes. Accountants working in the construction industry would have been aware of this
unlawful treatment of company finances. While the report by the EA highlighted there was misuse of occupational health and safety procedures within the construction industry, the major points involved financial mismanagement. The report alleged misuse of various industry funds, including trust funds established to preserve employee entitlements such as leave pay and superannuation: “There have been allegations that senior union appointed trustees have sought to influence the investment decisions of at least one of these trusts for political and/or industrial purposes” (Hamberger 2001, p. 6). According to Westmore (2001, para. 17), “a range of other allegations, including secret commissions and criminal activity within particular unions, were also reported”. The report by the EA highlighted for the Government that the construction industry was misbehaving in a way that could no longer be tolerated. The industrial relations conflict which had been the focus of regulators since the 1970s had evolved into activities which may be described as illegal. The misuse of funds, bribery and corruption were illegal activities and escalated the unlawful behaviour to a level where the Government had to act.

### 4.4 Media Exposure

Matters came to a head when the unions turned on themselves and bitter in-fighting became public. This was exposed by a media investigation into the construction industry which appeared on national television on the well respected public affairs program, Four Corners, on the ABC.

On 21 May 2001, the ABC television program, Four Corners, aired a story titled “Divided We Fall”. The story was about the battle for power between construction industry unions. During the interview, one of the participants, Mr John Sutton
(Divisional Secretary CFMEU Construction Division), made allegations of organised criminal activity within the union. These allegations were cited by government ministers as justifying the calling of a royal commission. Using the technique of CA, the transcript is examined to identify the four characteristics of text content: frequency, direction, intensity, and space (Neuman 2006, p. 325). The transcript of the interview contains 6,564 words. Table 4.1 summarises the coding into key themes found in the transcript using the four CA characteristics:
<table>
<thead>
<tr>
<th>Code</th>
<th>Frequency</th>
<th>Direction</th>
<th>Intensity</th>
<th>Space*</th>
</tr>
</thead>
<tbody>
<tr>
<td>Corruption</td>
<td>36</td>
<td>Negative – accepting bribes</td>
<td>Strong</td>
<td>15%</td>
</tr>
<tr>
<td>Enemies/fighting</td>
<td>20</td>
<td>Negative – between unions</td>
<td>Strong</td>
<td>8%</td>
</tr>
<tr>
<td>Power struggle</td>
<td>18</td>
<td>Negative – between unions</td>
<td>Very strong</td>
<td>7%</td>
</tr>
<tr>
<td>Threatening/intimidation</td>
<td>11</td>
<td>Negative – against politicians</td>
<td>Strong</td>
<td>5%</td>
</tr>
<tr>
<td>Leadership</td>
<td>9</td>
<td>Negative – management</td>
<td>Weak</td>
<td>4%</td>
</tr>
<tr>
<td>Illegal activity/Crime</td>
<td>8</td>
<td>Negative – against other unionists</td>
<td>Strong</td>
<td>4%</td>
</tr>
<tr>
<td>Lies</td>
<td>7</td>
<td>Negative</td>
<td>Strong</td>
<td>3%</td>
</tr>
<tr>
<td>Strike action</td>
<td>7</td>
<td>Negative – against employers</td>
<td>Strong</td>
<td>3%</td>
</tr>
<tr>
<td>Hatred</td>
<td>5</td>
<td>Negative – between unions</td>
<td>Very strong/emotive</td>
<td>2%</td>
</tr>
<tr>
<td>Ideology</td>
<td>5</td>
<td>Negative – anti-employer</td>
<td>Strong</td>
<td>2%</td>
</tr>
<tr>
<td>Mismanaged funds</td>
<td>4</td>
<td>Negative – unaccountability</td>
<td>Strong</td>
<td>2%</td>
</tr>
<tr>
<td>Government</td>
<td>3</td>
<td>Negative – inaction</td>
<td>Weak</td>
<td>1%</td>
</tr>
<tr>
<td>Violence</td>
<td>3</td>
<td>Negative – on contractors</td>
<td>Strong</td>
<td>1%</td>
</tr>
<tr>
<td>Employees not paid</td>
<td>2</td>
<td>Negative – against employers</td>
<td>Weak</td>
<td>1%</td>
</tr>
<tr>
<td>Public image</td>
<td>2</td>
<td>Negative – embarrassed</td>
<td>Strong</td>
<td>1%</td>
</tr>
<tr>
<td>Greed</td>
<td>1</td>
<td>Negative</td>
<td>Strong</td>
<td>0.4%</td>
</tr>
<tr>
<td>History/background/memories</td>
<td>1</td>
<td>Negative – baggage</td>
<td>Strong</td>
<td>0.4%</td>
</tr>
<tr>
<td>Inaction</td>
<td>1</td>
<td>Negative – delay</td>
<td>Weak</td>
<td>0.4%</td>
</tr>
<tr>
<td>Other paragraphs</td>
<td>101</td>
<td>N/a</td>
<td>N/a</td>
<td>41%</td>
</tr>
</tbody>
</table>

* % of paragraphs this code was mentioned as a proportion of total paragraphs in the text (n=244).
Table 4.1 uses CA (Neuman 2006, p. 325) to examine the interview transcript. The purpose is to identify whether the themes within this thesis associated with unlawful behaviour exist within this transcript. The RCR argues that the construction industry suffered from a long-standing culture which encouraged unlawful behaviour. It was also argued that this was caused by the culture within the unions. The table’s analysis uses a separate historical document, this transcript, to verify the claims about union culture.

Frequency identifies how often coded themes were mentioned in the transcript. The codes were derived from characteristics of unlawful behaviour which emerged from this thesis, for example, corruption. The frequency column lists the number of paragraphs in the transcript which mentioned corruption. Direction is the message within the content in the transcript associated with the code and the target group, for example, hatred was about other unions. This is a very interesting finding because it illustrates the competitive and confrontational nature of culture within the unions. Some union officials felt their adversaries were anyone who stood in the way of achieving their goals, including other union officials. Intensity is the strength of feeling in the content associated with the code, which was mainly very strong. Finally, space is the percentage of paragraphs with that code (that is, frequency) divided by the total number of paragraphs (n=244). The spatial analysis provides context for the relationship between how many times the code is mentioned and the total size of the document. The higher the space percentage, the more the coded theme emerges in the document. Corruption is mentioned in 15% of paragraphs, followed by enemies/fighting (8%), and power struggles (7%). This suggests fierce political in-fighting and a combative culture. The reason there are some single frequency paragraphs listed in the table is to highlight relevant codes. For example, greed was only mentioned in one paragraph, which is somewhat surprising given the self-interest in the industry.
The transcript is an important historical document, particularly in the context of this study, because it provides a rich snapshot of the dynamics of the trade union movement just prior to the RC. It highlighted the type of behaviour that society decided was a breach of the social contract. Adding to the importance of the transcript is that it documents the comments and actions of the trade union officials themselves. The infighting validates the social contract breach because it explains the nature of the inappropriate behaviour from an insiders’ perspective. Table 4.1 shows that the dominant themes in the transcript are

1. Corruption
2. Political power struggles between union leaders including allegations against enemies such as poor leadership, lying, hatred, greed, criminal activity, mismanaged funds, violence, and threatening or intimidating contractors and politicians

In the whole transcript only two references were found explaining why the trade unions were aggrieved with society, that employees were not being paid. Furthermore, only two references were made to the unions’ public image. The leadership of the unions at that time were clearly only interested in their personal power struggles and either unaware or did not care about society’s perceptions of them. Indeed, the then secretary of the NSW CFMEU union Mr Andrew Ferguson said on several occasions during the ABC interview that he made ‘no apologies’ for the unions’ actions, including demanding payments from contractors in a variety of situations such as to pay for the union’s annual employees’ picnic and as punishment for the death of a labourer in a site accident.
To investigate the transcript in more detail, CDA is used to examine some of the main themes. The following table examines some of the themes using the CDA framework from Gee (2011).
<table>
<thead>
<tr>
<th>Theme</th>
<th>Significance</th>
<th>Practices</th>
<th>Identities</th>
<th>Relationships</th>
<th>Politics</th>
<th>Connections</th>
<th>Sign Systems</th>
</tr>
</thead>
<tbody>
<tr>
<td>Corruption</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Quote 1 (see below)</td>
<td>Outrageous</td>
<td>Location is isolated (home base)</td>
<td>Villain (Sutton)</td>
<td>NSW Branch is the enemy</td>
<td>Sutton is responsible for the NSW Branch problems</td>
<td>Corruption able to be proven (truth)</td>
<td>Evil</td>
</tr>
<tr>
<td>Quote 2 (see below)</td>
<td>Stink</td>
<td>Business arrangement</td>
<td>Union leaders are villains and workers are victims</td>
<td>Inappropriate relationships between union officials and contractors</td>
<td>Union leaders are above the law</td>
<td>Assigns perception to workers</td>
<td>Smelly</td>
</tr>
<tr>
<td>Quote 3 (see below)</td>
<td>Swearing</td>
<td>Received bribes</td>
<td>Union leader (Sutton) is richer than he should be</td>
<td>Union leader has benefited from contractor favours</td>
<td>Union leaders are criminals</td>
<td>Denies evidence</td>
<td>Symbols of wealth</td>
</tr>
<tr>
<td>Quote 4 (see below)</td>
<td>Police involvement</td>
<td>Investment properties suggest inappropriate income</td>
<td>Union leader (Ferguson) investigating alleged corruption</td>
<td>Union leaders willing to punish their own</td>
<td>Union leaders can be good guys</td>
<td>Police action unresolved</td>
<td>Dark</td>
</tr>
<tr>
<td>Enemies/Fighting</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Quote 5 (see below)</td>
<td>Got to go</td>
<td>Invisibility</td>
<td>Union leader (Sutton) is locked away in head office</td>
<td>Union leader (Sutton) has no relationship with workers</td>
<td>Distance between union leaders and workers</td>
<td>Invisibility is ineffectiveness</td>
<td>Isolated</td>
</tr>
<tr>
<td>Power Struggle</td>
<td></td>
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<tr>
<td>----------------</td>
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<td></td>
<td></td>
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</tr>
<tr>
<td><strong>Quote 6 (see below)</strong></td>
<td>Dictator</td>
<td>Leadership of the union</td>
<td>Union leader (Reynolds) is self-interested</td>
<td>Lack of consultation</td>
<td>Leaders are above everyone else</td>
<td>Undemocratic</td>
<td>Power</td>
</tr>
<tr>
<td></td>
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<td></td>
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</tbody>
</table>

CHAPTER 4: HISTORY OF REGULATION
The CDA of these quotes from the Four Corners program is examined further.

**Quote 1:** MARTIN KINGHAM: I just say that's an outrageous distortion of the truth. The only proven corruption, um, that is currently in evidence in the construction industry at the moment is in the New South Wales branch and in John Sutton's home base.

This quote alleges that the NSW Branch is corrupt and that its leader, Mr John Sutton, is responsible. The CDA highlights the significance of the comment, the identity assigned to Sutton, the adversarial relationship between the NSW Branch of the union, and lays blame on Sutton.

**Quote 2:** JOHN SUTTON: I think building workers sitting in their sheds, in Perth or in Melbourne or in Sydney or wherever, when they hear that the union leader who's meant to be - particularly if it's a Multiplex site - the union leader that's meant to be looking after their interests on that site is actually in a business arrangement, ah, with the owner of that site or that building company, I think the average building worker would reckon it would stink.

This quote is a response from Mr Sutton where he alleges inappropriate behaviour against other union branches and introduces another stakeholder – the union members or workers – and how they would not support the allegedly corrupt behaviour of their leaders. The inference is that while the union leaders might benefit from corruption, the members do not, and are therefore innocent by-standers in this social contract breach. While they are involved in undesirable activity, that is strike action, this is under the direction of the union leaders who are painted as the villains in this transcript.

**Quote 3:** KEVIN REYNOLDS: Ah, and this mob here, they're along the same line too. They're asking the same questions. I've got a f---ing boat bigger than the Queen Mary that's been supplied to me by *****. I've got f---ing units all over this town. I've got an ice-cream parlour somewhere. I think about the only thing I don't f---ing own is that Parliament House across the road there. Right? But what they all can't come up with is any facts on this s---. You know, they can't come up with any facts. 'Cause I'll tell you why they can't come up with any facts. There ain't no f---ing facts. I ain't got any beach house, I haven't got a boat, I haven't got anything. I've got a f---ing pub with $1.8 mortgage and they
ask me about that and everyone knows about the pub. And I'm a bit disappointed you don't know a bit more about it, 'cause you should be all down there drinking at the f---ing joint.

This quote is a response to allegations of corruption against one of the union leaders, Mr Reynolds. It illustrates the strength of emotion and aggressive language used by these men. While his anger is understandable, given the seriousness of the allegation, that is corruption, it is a ferocious response. The union leaders appear to be uncompromising individuals. It suggests how difficult it may have been for contractors and politicians to deal with them. Indeed, introduced later in the transcript is Mr Tom Domican, who was allegedly a ‘stand-over man’, who was employed by contractors to deal with “industrial relations matters”, that is trade union officials. This created a culture where accounting staff working for contractors would have found it difficult to deal with the pressure exerted by these men.

**Quote 4:** SALLY NEIGHBOUR: The allegations pitted Ferguson against his deputy, Craig Bates, the assistant secretary in NSW. Bates was close to the sacked delegates and the signing of enterprise agreements was his job. He'd also recently bought two inner-city investment properties in Sydney, worth more than $700,000. ANDREW FERGUSON: I had privately started to do some investigations. I did property searches. I asked Bates for an explanation about properties that he recently purchased. His explanation was that it was none of our business. We notified the police of what allegations that we had received and the police are investigating those allegations.

This quote is another allegation of inappropriate financial benefits received by union leaders. However, it is particularly interesting because in this case, a union leader took responsibility to investigate and involve police in order to follow the rules of society. It suggests a number of important activities which would be considered appropriate by society that is moving the unions towards the social contract rather than away from it, namely, acceptance that there is a problem, the gathering of evidence, and involving the appropriate authorities.
Quote 5: KEVIN REYNOLDS: John Sutton has got to go! Now a lot of youse would be saying, "John who? "Who the f---'s this John Sutton?" Well, I tell you why you'd be saying that, 'cause the national leader of your union, I can't remember in the last six years him ever being in Perth. I can't remember him ever visiting a site in Perth. I can't remember him ever shaking hands with any building workers in Perth. I mean, he's got this attitude that the sun rises and sets in Pitt Street in Sydney, and that's where he should be. He doesn't...

This quote is indicative of comments involving the enemy theme. Many of the problems within the trade union movement which emerged in the transcript, such as allegations of corruption and other illegal activity, were made by men who seemed to be personal enemies. In this quote Mr Reynolds is attacking his enemy Mr Sutton. The level of animosity between the union leaders appears to be linked to ideology, that is measured by degree of ‘left-winged or communist belief’, as well as history, relationships, and power struggles.

Quote 6: SALLY NEIGHBOUR: One who wanted to get rid of him was former union organiser, Terry McParland, who challenged Reynolds for the job of state secretary. McParland has been a vocal critic since Reynolds sacked him from the union. TERRY MCPARLAND: I'm not happy with the way the union's being run. And, ah, I'm not happy with the man who's been the secretary for 25 years. Ah, I believe he's a dictator. He runs the union for himself and no-one else has got a say.

In summary, the following conclusions about the causal relationships in the themes found in the ABC Four Corners transcript using CA and CDA techniques.
The analysis identifies a range of antecedents for the political forces, manifested by the power struggle and allegations between union leaders, followed by the outcomes of employees not being paid and poor public image.

The second scenario, the DSS, more accurately explains what happened. The analysis of the government enquiries shows that the regulator was dissatisfied with the behaviour of the construction industry for at least a decade before the RC. Therefore, the social contract breach was not something that was hidden and suddenly emerged. The catalyst was probably the Four Corners media investigation, which gave wide public exposure to the behaviour of the trade union officials within the industry. While the information provided by the media investigation was not new, it highlighted for many people the seriousness of the cultural problems within the industry. The CDA of the Four Corners
transcript shows a blatant disregard for others’ opinions, that is society, and suggests some of the union officials saw themselves as a law unto themselves. The lack of respect for society’s opinion showed a disregard for the social contract. It suggested some union officials did not care what society expected. The self-interest of some individuals was further highlighted by the union in-fighting. The pursuit of power was not limited to conflict between stakeholders, it occurred within the unions themselves. The publicity surrounding this media report suggested to the government that they must act and that society would no longer tolerate the industry’s behaviour.

In terms of LT, the construction industry’s behaviour was considered no longer proper or appropriate. While its services were still desirable, the benefits provided were outweighed by the costs of the inappropriate behaviour. Society, through Minister Abbott and the Australian Federal Government, indicated it was unhappy with the construction industry’s behaviour and launched the RC to investigate the size and true nature of the social contract breach.

4.5 The Royal Commission

4.5.1 Regulator’s Explanation of the Need for the Royal Commission

The Australian PM announced the RC in August 2001 by stating that Commissioner Cole was appointed to investigate certain matters in relation to the building and construction industry. Those matters were defined in the Letters Patent as follows:

(a) the nature, extent and effect of any unlawful or otherwise inappropriate industrial or workplace practice or conduct, including, but not limited to:
(i) any practice or conduct relating to the Workplace Relations Act 1996, occupational health and safety laws, or other laws relating to workplace relations; and

(ii) fraud, corruption, collusion or anti-competitive behaviour, coercion, violence, or inappropriate payments, receipts or benefits; and

(iii) dictating, limiting or interfering with decisions whether or not to employ or engage persons, or relating to the terms on which they be employed or engaged;

(b) the nature, extent and effect of any unlawful or otherwise inappropriate practice or conduct relating to:

(i) failure to disclose or properly account for financial transactions undertaken by employee or employer organisations or their representatives or associates; or

(ii) inappropriate management, use or operation of industry funds for training, long service leave, redundancy or superannuation;

(c) taking into account your findings in relation to the matters referred to in the preceding paragraphs and other relevant matters, any measures, including legislative and administrative changes, to improve practices or conduct in the building and construction industry or to deter unlawful or inappropriate practices or conduct in relation to that industry. (Cole 2003, vol. 2, p.3).

The PM’s statement makes it clear that this is akin to a criminal investigation with the use of the word ‘unlawful’ or otherwise inappropriate conduct. The TOR ask the RC to find evidence of this unlawful behaviour and offer solutions. The document explains that the regulator feels the social contract with the construction industry has been breached and wants the legitimacy gap closed so that the industry can once again be considered legitimate. CDA is now used to analyse the PM’s statement aiming to find deeper insight into the regulator’s motives and add to our understanding of the legitimacy gap. The following table (table 4.3) uses the CDA framework adapted from Gee (2011), as discussed in section 2.2.4 of chapter 2, to complete the reconstruction:

1. **Significance**: how is this language being used to make certain things significant or not?

2. **Practices (activities)**: what practice or activity is this language being used to enact?

3. **Identities**: what identity or role is this language trying to get others to recognise?
4. Relationships: what sort of relationship is this language trying to create with others?

5. Politics: who or what is being assigned values of being normal, right, good, correct, proper, appropriate, valuable, the way things ought to be, high status – and the inverse of each of these labels.

6. Connections: how does this language connect or disconnect things or make something relevant or irrelevant?

7. Sign systems and knowledge: does this language privilege or dis-privilege certain technical or jargon groups?

This CDA framework analyses the language used in the PM’s statement to reconstruct the social reality of the regulator’s perception of the nature of the social contract breach is summarised in table 4.3.
<table>
<thead>
<tr>
<th>Theme</th>
<th>Significance</th>
<th>Practices</th>
<th>Identities</th>
<th>Relationships</th>
<th>Politics</th>
<th>Connections</th>
<th>Sign Systems</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Explicit Social Contract Expectations</strong></td>
<td></td>
<td></td>
<td></td>
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<td></td>
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<td></td>
</tr>
<tr>
<td>Industrial Relations</td>
<td>Anti-competitive</td>
<td>Conduct of work practices</td>
<td>Union leaders are villains and workers are victims</td>
<td>Suggests collusion between unions and employers</td>
<td>Legislation must be followed</td>
<td>Illegality</td>
<td>Rules of engagement set by unions</td>
</tr>
<tr>
<td>Employment Practices</td>
<td>Dictating</td>
<td>Human Resource Management</td>
<td>Union leaders are villains and employers are victims</td>
<td>Cronyism, nepotism</td>
<td>Union leaders are above the law</td>
<td>Inequity</td>
<td>Rule makers win</td>
</tr>
<tr>
<td><strong>Implicit Social Contract Expectations</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Financial Disclosure</td>
<td>Failure</td>
<td>Accounting</td>
<td>Management negotiating</td>
<td>Management, unions, sub-contractors</td>
<td>Money creates influence</td>
<td>Unaccountable</td>
<td>Privilege deal makers</td>
</tr>
<tr>
<td><strong>Pragmatic Motives</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Corruption</td>
<td>Inappropriate</td>
<td>Leadership of the union</td>
<td>Self-interest</td>
<td>Management, unions, sub-contractors</td>
<td>Participants make the rules</td>
<td>Illegality</td>
<td>Privilege power holders</td>
</tr>
<tr>
<td><strong>Moral Motives</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Appropriate use of funds</td>
<td>Inappropriate</td>
<td>Leadership of the union</td>
<td>Self-interest</td>
<td>Management, unions, sub-contractors</td>
<td>Participants ignore the law</td>
<td>Illegality</td>
<td>Privilege those with control of funds</td>
</tr>
<tr>
<td><strong>Legitimacy Gap</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Changes to legislation or administration necessary to deter unlawfulness</td>
<td>Deter</td>
<td>Government</td>
<td>Regulator taking charge</td>
<td>Watchdog, policing</td>
<td>Enforcing law</td>
<td>Prevention</td>
<td>Dis-privilege regulator</td>
</tr>
</tbody>
</table>
The CDA shows that the PM’s Statement was conservative in its use of language (see significance) but critical of the range of activities involved in the social contract breach. It clearly identifies the unions as being at fault but also includes, implicitly, management and sub-contractors. The connections reveal illegality, inequity, and lack of accountability as the important themes in this document. The government wants to communicate to the industry that it will not tolerate this behaviour any further (see deter) and that it wants to introduce fairness and accountability to the industry, particularly in terms of industrial relations and funds management and disclosure. Accounting is implicated in terms of the latter point.

In terms of the individual CDA themes, the following conclusions may be drawn. First, the analysis distinguishes between explicit and implicit social contract expectations. Explicit expectations are legal requirements, for example legislation or activity required by law (Deegan 2009). Table 4.3 shows what the regulator expected of the construction industry in terms of the law, and why these expectations were not being met. The main issues were industrial relations and employment practices, where the language used by the PM’s statement suggests connections of illegality and inequity. It identifies union leaders being villains and workers and employers as victims. Implicit expectations are areas outside the law but still deemed desirable by society (Deegan 2009). The main issue here was financial disclosure, where the language used by the PM’s statement suggests connections of unaccountability. It uses strong words to describe the significance of this behaviour, failure, and to allocate identities as management doing deals. It does not identify accountants specifically. However, financial disclosure is an activity that involves accountants, so they are implicated.
Second, the analysis distinguishes between pragmatic and moral motives. The table shows the regulator’s perception about why the construction industry misbehaved. Pragmatic motives are derived from self-interest, for example, profit (Deegan 2009). The main issue here was corruption. Moral motives involve responsibility, desire to do the right thing, for example, good corporate citizenship (Deegan 2009), the principle concern being appropriate use of funds. In both cases, the language used by the PM’s statement suggests connections of illegality. The identities were all those with self-interest, and while union leaders were implicated, the language is cautious, using the word ‘inappropriate’. Deegan (2009) identifies a third motive, cognition, which is shared mental models, for example peer group pressure, norms, or just the way things are done in the industry. This involves the cultural problems later identified by the RCR in 2003, however, at this stage the PM’s statement does not specifically use language regarding cognition, possibly because the cultural behaviours were unknown at that time.

Third, the analysis explains the legitimacy gap, in terms of expectation change; how society expectations have changed over time, current requirements which were different from the past; and organisational shadow, when previously unknown information about an industry or organisation becomes known (Deegan 2009). The table shows that the language in PM’s statement identified expectation change as the main factor. As a result of the regulator perceiving the construction industry was not meeting its social contract, both explicitly and implicitly, and the nature of the industry’s pragmatic and moral motives, the government required changes to the way the industry was being regulated. The connections were about prevention and the regulator wanted identity as taking charge. However, the sign symbols showed that the regulator’s history of powerlessness showed it was dis-privileged in terms of the socio-economic power inequities amongst
construction industry stakeholders. While the PM’s statement suggests the regulator wanted a relationship with the industry where it was a watchdog with a policing role, the social reconstruction of the reality of the industry at the time was that the regulator was often ignored.

### 4.5.2 How the Royal Commission Gathered Evidence

The RC was initiated and funded by the Federal Government. Despite this, the Commissioner Cole argued strongly that the RC was independent and objective:

> This Royal Commission was conducted entirely independently of the Commonwealth Government. I did not receive, nor would I have accepted, any instruction from the Government. At all times this Commission maintained its independence from the Government and, indeed, from all other institutions and persons (Cole 2003, vol. 2, p. 15).

This statement is intended to distance the RC from the Government. Using the CDA framework, the language used explains the significance of the statement with the word ‘entirely’. Commissioner Cole wants there to be no doubt about its independence. Similarly, in terms of activities, the phrase ‘at all times’ aims to make it clearly understood that the investigation never wavered from its path of independence. The phrase ‘I did not receive, nor would I have accepted’, establishes Commissioner Coles’s claim to be a man of integrity. Finally, the phrase ‘from all other institutions and persons’ defines the RC’s relationships with the construction industry and its stakeholders, as an independent and separate authority. Commissioner Cole then goes on to explain how the Government played no role in the conduct of the RC, for example in determining the witnesses or material placed before the RC (Cole 2003, vol. 2, p. 15).

However, there are two anomalies in this account: first, Commissioner Cole states he never received instruction from the Government, yet there was a TOR; and second, Commissioner Cole argues that the Government did not interfere in the conduct of the
investigation, yet RC staff were called before the Senate Legal and Constitutional Committee on four occasions to answer questions about its conduct (Cole 2003, vol. 2, p. 15), and the RC provided the Attorney-General with information relating to 96 Questions on Notice from the Committee (Cole 2003, vol. 2, p. 15). It seems that while Commissioner Cole went to great lengths to argue his independence from the Government, and therefore the integrity of his findings, the Government did keep a close eye on the conduct of the investigation.

The RC used a “multi-pronged approach” (Cole 2003, vol. 2, p. 17) in its investigations and procedures prior to conducting hearings. The aim was to ensure as many people as possible with an interest in the construction industry were made aware that there was an opportunity to give feedback on the industry’s behaviour, as explained by this extract:

…in October 2001, an invitation was extended to all governments, organisations, companies, unions and persons with an interest in the subject matter of the Commission to provide submissions addressing relevant matters. In addition, at about the same time the Commission sent requests for information to almost 6500 organisations throughout Australia, and established a 1800 telephone number that could be used to give information to the Commission. The advertisements placed in the national and state press before the preliminary hearing also invited interested persons to provide submissions to the Commission addressing any matters falling within the Terms of Reference. Similarly, towards the conclusion of hearings, the Commission again advertised in the national and state press seeking final submissions in relation to the Commission’s investigations (Cole 2003, vol. 2, p. 17).

The Government also provided submissions, as did various industry groups, such as the MBA. Interestingly, “only two major construction companies put in submissions, and the CFMEU, and the Automotive, Food, Metals, Engineering, Printing and Kindred Industries Union (AMWU) were the only unions to do so” (Cole 2003, vol. 2, p. 17). This suggests that the industry’s main stakeholders, and those most under investigation, did not want to cooperate with the RC, or at least did not want to volunteer information. Commissioner Cole expressed disappointment in the number of submissions received.
which “reflected the general lack of co-operation experienced by the Commission in the
conduct of its investigations” (Cole 2003, vol. 2, p. 18). This attitude was not limited to
the head contractors and unions, Commissioner Cole was disappointed that the voice of
society, state governments, seemed disinterested, as illustrated by this extract:

…only sparse submissions were received from the governments of Tasmania,
Western Australia, Northern Territory and New South Wales. No general
submissions were received at all from the Governments of Victoria, South
Australia or the Australian Capital Territory (Cole 2003, vol. 2, p. 18).

This apparent lack of cooperation at the early stages of the investigation continued as it
moved to preliminary hearings. In October 2001, Commissioner Cole wrote to almost
150 major participants in the building and construction industry with an invitation to
consult with him confidentially, and only 29 organisations or individuals (19%)
accepted the invitation (Cole 2003, vol. 2, p. 18). Less than 20% of the key industry
stakeholders were willing to meet with Commissioner Cole tasked by society to
investigate the industry’s behaviour. This suggests that the industry did not want to
cooperate with the RC, that it did not want to offer information to Commissioner Cole,
and perhaps that it had something to hide. Evidence to support this claim is found in
Commissioner Cole’s following statement:

It must be said, in light of disclosures which have emerged at public hearings,
that many of those consulted were less than frank with the Commission (Cole

While the phrase ‘less than frank’ falls short of accusing industry stakeholders of lying
to Commissioner Cole, it suggests that even the small proportion who were willing to
meet with Commissioner Cole were reluctant to tell the truth about the industry’s
behaviour. The cultural issues embedded in the industry were evident in its relationship
with the government, in this case Commissioner Cole. Even when the Federal
Government announced a nation-wide investigation into the industry, stakeholders refused to follow society’s expectations and cooperate. This was an industry which felt it could operate outside society’s expectations.

Commissioner Cole had more success with the release of Discussion Papers. There were 18 Discussion Papers released over the course of the RC, covering a wide range of topics, designed to stimulate interest amongst industry stakeholders. After the release of each Discussion Paper, Commissioner Cole wrote to parties he felt may be interested inviting a response. A total of 140 responses were received in total (Cole 2003, vol. 2, p. 18). Commissioner Cole was happy with the quality of this information and he felt they “contributed significantly to my Final Report” (Cole 2003, vol. 2, p. 18). However, 140 responses equates to less than 8 responses per Discussion Paper, and when it is considered that there were almost 100,000 firms operating in the industry employing almost 700,000 people, two issues emerge: first, only a small proportion of the industry was engaging in the RC’s findings and second, the majority of the industry was not represented in the RC’s findings.

Faced with barriers to his investigation, Commissioner Cole pursued three legal avenues in the hope of obtaining information from those unwilling to provide it. First, he obtained cooperation from the Australian Taxation Office (ATO) “for the purpose of conducting its inquiries” (Cole 2003, vol. 2, p. 20). However, there were legal restrictions under the Income Tax Act, and an individual’s information could not be disclosed to Commissioner Cole, meaning the information gathered was not of “much assistance” (Cole 2003, vol. 2, p. 20). Second, Commissioner Cole received information, on one occasion, gathered from listening devices provided by another Government agency (Cole 2003, vol. 2, p. 20). Third, Commissioner Cole obtained a total of six search warrants but these “were not a major source of information obtained”
for the RC (Cole 2003, vol. 2, p. 20). Commissioner Cole then enacted his authority
delegated by the Government in its TOR for the RC to coerce industry stakeholders to
provide information, as illustrated by this extract:

Finally, the Commission used its coercive powers to obtain information relevant
to its Terms of Reference. Those coercive powers took a number of forms. The
two most important powers were the power to issue notices to produce (which is
discussed below) and the power to summons persons to attend and give
evidence. Extensive use was made of both of those powers (Cole 2003, vol. 2, p.
20).

Witnesses were summoned to give oral evidence at hearings (Cole 2003, vol. 2, p. 20),
in other words, industry stakeholders were legally forced to give information. The
hearings were designed to gather information regarding industry behaviour that was
apparently well known within the industry but not to the general public. The hearings
aimed to gather evidence and “make public practices and attitudes in the building and
construction industry that the Commission’s investigations identified” (Cole 2003, vol.
2, p. 21). The hearings were designed to illustrate to the public the extent of the
construction industry’s social contract breach.

The hearings were defined in terms of scope and process. The scope was that the RC
could not investigate all cases of inappropriate behaviour that came to its attention. The
decision regarding which cases to investigate was made by the Counsel Assisting the
RC, who “called evidence of practices or conduct that they regarded as representative,
or that were illustrative of particular problems” (Cole 2003, vol. 2, p. 2). Therefore,
Commissioner Cole’s legal advisors decided to investigate the matters which were most
serious or widespread. The process involved RC investigators pursuing “leads” which
represented cases of inappropriate behaviour, persons who could provide information
relevant to the lead were identified and contacted, and interviews were conducted and in
most cases recorded (Cole 2003, vol. 2, p. 22). On most occasions witnesses cooperated
and written statements proved an effective way to gather necessary information. On some occasions witnesses were uncooperative and legal summons were invoked; most of these cases involved union officials or members (Cole 2003, vol. 2, p. 23).

The final step in the RC’s information gathering process was to produce ‘Overview Evidence’, which was an opportunity for employers or employees within the industry to provide a perspective on their “position” and to explain the industry structural issues (Cole 2003, vol. 2, p. 24). Commissioner Cole refers later in volume 2 to the way evidence was evaluated, particularly when there was conflicting evidence, that is, opposing views, as illustrated by this extract:

Where the evidence of witnesses conflicted, my general approach was as follows. I considered whether there was any documentary evidence, or evidence from independent witnesses, that lent support to either version of events. Where there was such evidence, the version of events that was consistent with the documentary or independent evidence was generally preferred, even if that version was not completely corroborated by the documentary or independent evidence (Cole 2003, vol. 2, p. 47).

In terms of the findings, Commissioner Cole makes two important points. First, the findings were uncontested in the sense that they were unchallenged by industry stakeholders. Second, while the findings were highly critical of the industry’s behaviour, it stopped short of publicly announcing criminal conduct. Instead, the Commissioner compiled specific instances of alleged criminal activity into a final volume which was not made public and was, instead, referred to the Director of Public Prosecutions for further investigation, as illustrated by this extract:

Consequently, I have not made findings to the effect that named individuals, organisations or companies have committed criminal offences. Instead, my views in relation to matters that might have constituted breaches of the criminal law have been set out in a separate volume, which I have recommended should not be made public. In that volume, I have set out the matters that I recommend be referred to appropriate law enforcement agencies for consideration and, if
appropriate, further investigation with a view to determining whether criminal charges should be laid (Cole 2003, vol. 2, p. 59).

Commissioner Cole also addresses the important issue of blame and who is accountable for the industry's unlawful behaviour. His comments here are particularly relevant for this study and in particular the examination of the role of accountants employed by the industry. At face value, inappropriate conduct is unacceptable, and all firms and individuals who participated in activity considered unsatisfactory by society, that is the RC, and are accountable for this behaviour. However, many participants in the RC tried to justify their behaviour in terms of them having no choice about whether to participate in the activity. The following extract illustrates how Commissioner Cole is reasonably tolerant of this view:

One major reason for avoiding making findings of ‘inappropriate’ conduct, even if an individual, organisation or company had departed from an apparently objective standard of appropriate behaviour, was that such departures were often explained by those involved as a reasonable response, taking into account deficiencies in the law and law enforcement mechanisms within the building and construction industry, to threats of unlawful action by others (Cole 2003, vol. 2, p. 61).

Commissioner Cole tends to excuse firms and individuals from participating in inappropriate behaviour if they did not initiate it and if they were responding to pressure exerted by others in the interests of doing their job. He stated that it was common for people to state “they thought that that conduct was the best way that they could discharge their obligation to act in the best interests of their shareholders or members, which they may have felt obliged to do whether or not it was objectively appropriate” (Cole 2003, vol. 2, p. 61).

Commissioner Cole stops short of absolving people who felt they were victims from all blame, but he does acknowledge that the industry structure created conflicting interests
which created considerable pressure on individuals to cooperate with inappropriate behaviour based on their knowledge of past conduct (Cole 2003, vol. 2, p. 62). In other words, people knew there would be consequences if they did not comply, and they based this perception on hard evidence; they had seen what could go wrong if people did not cooperate. Perhaps most importantly for this study and the role of accountants, Commissioner Cole is somewhat sympathetic towards the pressure individuals were under to act in the best interests of their stakeholders. For managers, their jobs required them to protect the interests of owners by ensuring the firm was profitable. It was common knowledge amongst the industry that firms with a history of industrial disputes found it more difficult, if not impossible, to win future work. Managers may have found it impossible to refuse to engage in improper practices, such as “sizeable payments that have been made for the apparent purpose of securing industrial peace” (Cole 2003, vol. 2, p. 61), because if they failed to do so they may have felt they were negligent in doing their job. A similar argument may be applied to accountants.

4.5.3 The Royal Commission Findings

The RC tabled its final report in March 2003. The content of the RCR and its findings are used in several ways in this study. The main focus is in chapter 4 of the report where the culture of the construction industry is analysed in terms of its work practices. In chapter 5, the focus is on regulation and why the regulator felt the industry had breached its social contract. The analysis which follows, therefore, analyses the main findings only, to place the construction industry’s legitimacy gap within the overall context of the history of regulation of the industry.

“The RC found that the construction industry was characterised by a widespread disregard for the law, cataloguing over 100 types of unlawful and inappropriate
conduct” (FWBC 2012b, para. 3). The following analysis examines selected text from volume 1 of the RCR. The text was selected because it was considered to summarise information most relevant to this study. More specifically, the information reveals the nature of the social contract breach, and provides evidence of the regulator’s perception of the legitimacy gap. In the summary of findings and recommendations at the start of volume 1 of the RCR, paragraph 11 states:

Culturally, first, there needs to be a recognition by all participants that the rule of law applies within the industry. The rule of law requires that parties honour and implement agreements they have made. It requires that they abide by industrial, civil and criminal laws. At present, they do not. The structural reforms will assist this necessary cultural change (Cole 2003, vol. 1, p. 4).

Using the CDA framework for analysis, the language is somewhat cautious. It does not use words such as criminal or unlawful and does not specifically lay blame. The phrase ‘recognition by all’ suggests strong significance, and indicates that some construct industry stakeholders do not recognise the law. In terms of identity, it simply refers to ‘parties’, which identifies no one in particular. However, it does imply that the behaviour is not limited to particular stakeholders. In terms of connections, the recommendation links two important issues. First, the societal expectation is that stakeholders abide by the law. Second, the main social contract breach is that construction industry stakeholders do not abide by the law. The legitimacy gap, therefore, is the degree of unlawfulness, that is, the extent to which the industry does not abide by the law. Paragraph 16 makes it very clear that the construction industry has breached its social contract:

These findings demonstrate an industry which departs from the standards of commercial and industrial conduct exhibited in the rest of the Australian economy. They mark the industry as singular. They indicate an urgent need for structural and cultural reform (Cole 2003, vol. 1, p. 6).
In this statement, Commissioner Cole uses the phrase ‘departs from the standards’ to state that the industry does not behave the way the rest of Australian industry behaves. The use of the word standards indicates an expectation, a level of behaviour, that is, a social contract. While Commissioner Cole was cautious in his earlier statements about industry culture, he makes the departure from society’s standards explicit in paragraph 17:

At the heart of the findings is lawlessness. It is exhibited in many ways. There are breaches of the criminal law (Cole 2003, vol. 1, p. 6).

Commissioner Cole makes two qualifications to soften the allegation of lawlessness. First, he indicates that much of the breaches of criminal law relate to the “provisions of the Workplace Relations Act 1996 (C’wth)” (Cole 2003, vol. 1, p. 6). Therefore, industrial relations practices are the main cause of lawlessness. Second, he suggests the consequences of these breaches of criminal law were most likely to be “sanction is a penalty rather than possible imprisonment” (Cole 2003, vol. 1, p. 6). While this latter point suggests that the size of the social contract breach is relatively minor, in the sense of the consequences of breaking the law, Commissioner Cole is starting here society’s view and not his own. Elsewhere throughout the reports, Commissioner Cole expresses his frustration at the limits of power of authorities in dealing with the industry’s unlawful behaviour. For example, in volume 2 he discusses his anger at witnesses who openly refused to cooperate with the RC’s investigation, even under summons, because they knew the consequences were only a small fine. In evaluating the size of the social contract breach in terms of consequences for breaches, Commissioner Cole is stating that society allocates a relatively minor penalty. However, it is clear that he disagrees with society on this point and believes much stronger punishment should be allocated towards those parties who do not obey the law.
The analysis turns now to look at volume 11 of the RCR which is titled Reform – Achieving Cultural Change. First, Commissioner Cole defines the scope of the problem: “there is widespread disrespect for, disregard of and breach of the law in the building and construction industry” (Cole 2003, vol. 11, p.13). Second, he explains that “the criminal, industrial and civil law is breached with impunity” (Cole 2003, vol. 11, p.13).

Adopting the content discourse analysis framework, the language used here is scathing. The phrase ‘widespread disrespect for, disregard of and breach’ suggests this is very significant unlawful behaviour, and in terms of politics the word ‘impunity’ suggests no fear of consequences by industry stakeholders.

Commissioner Cole then goes to the root cause of the problem and lays the blame for unlawful behaviour with industrial relations. He argues that this situation has emerged because industry stakeholders believe that industrial relations sits outside the law:

The culture in the industry is that the criminal law does not apply because industrial circumstances are involved. The attitude is that the applicability of industrial law is optional because there is no body whose function it is to enforce it, or which has the will, capacity and resources to do so. Orders of industrial tribunals, and even courts, are disregarded if such orders are contrary to the views or interests of a participant (Cole 2003, vol. 11, p.13).

Adopting the content discourse analysis framework, the use of the word ‘criminal’ suggests strong significance. The word ‘optional’ is a sign system privileging those with power, and suggesting stakeholder groups could choose whether to abide by the law or not. In terms of politics, there is frustration with the role of authorities and their inability to enforce the law.

Commissioner Cole identifies the socio-political power inequities which had created the industry’s culture. He states that “the result is that industrial power, not right or entitlement, determines outcomes” (Cole 2003, vol. 11, p.13). This statement goes to
the basis of the structural problems inherent in the industry’s stakeholder relationships. Those with power were the winners. Power was obtained by industrial action. The inequities in the stakeholder relationships were driven by intense competition which created small profit margins. As a result “short term commercial expediency prevails” (Cole 2003, vol. 11, p.13), which meant that employers, both head contractors and subcontractors, had to submit to those with the power to decrease their profitability, that is the unions. The unions held power in the industry because they could enact industrial action, and firms with a history of industrial disputes were less likely to win work because it meant delays and low productivity. To win work and be profitable, employers had to avoid industrial action, which meant complying with union demands. The inequity in the industry’s socio-political relationships is further explained by the following:

If unlawful action causes loss to others, that loss is not recovered. That is because of the difficulty, cost and time involved in bringing proceedings for recovery, the uncertainty of outcome, the view that continued relationships with unions are important, and the knowledge that if recovery action is taken the likelihood is that further industrial action will be taken causing yet further loss. Litigation for loss recovery is regarded as a bargaining chip to be used in future resolution of industrial disputes, rather than as a serious attempt to hold those causing loss responsible for it (Cole 2003, vol. 11, p. 13).

This extract explains the powerlessness of employers. They felt there would be high cost and little benefit to be gained from seeking legal action against unions for loss caused by industrial action. The cost involved was explained by Commissioner Cole as follows: “head contractors and subcontractors are subject to severe cost penalties for delayed completion” (Cole 2003, vol. 11, p.13). The real cost to employers due to industrial unrest and stoppages was “immediate loss from standing charges and overheads, and prospective loss from liquidated damages” (Cole 2003, vol. 11, p.13). Using the CDA framework, the language used here indicates a very significant problem
for employers. The phrases ‘severe cost penalties’ and ‘immediate loss’ would make managers in any industry very anxious; and it adds evidence for Commissioner Cole’s identification of employers as victims. The social reconstruction of stakeholder relationships in the construction industry at the time of the RC suggests that owners and managers of contractors must have been under considerable pressure. Commissioner Cole is tolerant of their engagement in the industry’s unlawful behaviour because he suggests it is natural that owners and managers would want to minimise or prevent activities that cause ‘severe cost penalties’ and ‘immediate loss’, otherwise they would be negligent in their roles. This is a particularly important finding for this study because it is reasonable to assume the same behaviour from accountants employed by the industry.

Commissioner Cole explains that the unions had nothing to lose and everything to win from the outcomes of industrial action. He states “in contrast, unions suffer no loss from unlawful industrial action. They know they will not be held accountable for unlawful industrial action by the criminal, industrial or civil law” (Cole 2003, vol. 11, p.13). The outcome, according to Commissioner Cole was ‘inevitable’; employers conceded to the unions, the “rule of law is diminished”, and “productivity is diminished” (Cole 2003, vol. 11, p. 13). The consequences of this social contract breach were that the Australian economy as well as contractors, subcontractors and employees were disadvantaged.

4.5.4 The Royal Commission Recommendations

LT is used to interpret the RC’s main recommendations for cultural change in the construction industry. LT examines three aspects of the recommendations: social contract, breach, and legitimacy gap. Social Contract explains the ‘what’, in terms of what society expected from this industry. Breach explains the ‘how’, in terms of the
behaviour that the regulator found unsatisfactory. Legitimacy gap explains the ‘why’, in terms of the reasons for the gap occurring. Society’s expectations of the construction industry may be understood from two perspectives:

1. Explicit: legal requirements, for example, legislation or activity required by law

2. Implicit: areas outside the law but still deemed desirable by society

Society’s legal requirement of the construction industry is what is explicitly stated by law, that is legislation or other legal document, and endorsed by Government as the representative of the society in which the industry operates. This assists our understanding regarding what society expected of the industry, that is, what was the social contract. The following quote presents the RC’s opening findings presented in volume 11 Reform - Achieving Cultural Change:

1. The building and construction industry in Australia requires significant cultural change. Such change is necessary if the rule of law is to be reintroduced to conduct and activities within the industry, if individuals’ freedoms are to be maintained, and if the industry is to achieve its economic potential. Change is required in the attitudes of all sectors of the industry, including governments, clients, head or subcontractors, industrial organisations and employees.

2. In summary, I recommend that cultural change be achieved by:
   - The Commonwealth Parliament enacting a statute of special application to the industry.
   - Creating a new statutory norm which clearly delineates between unlawful and lawful industrial conduct.
   - Creating a Commission with responsibility for investigating unlawful conduct occurring in the industry.
   - Rendering those causing loss from unlawful industrial action liable for such loss and prosecuting such conduct.
   - Establishing a just, quick and cheap method of assessing and recovering loss caused by unlawful industrial action.
   - Imposing a statutory obligation to report actual or threatened industrial action to the Commission.
   - Providing that only fit and proper persons may hold office in, or exercise official functions on behalf of, industrial organisations.
The nature and extent of the unlawful and inappropriate conduct disclosed in the hearings before me and recorded in this report should not continue uncorrected. (Cole 2003, vol. 11, p. 3).

Using the CDA framework, the language used is assertive and prescriptive. The significance of the recommendations is highlighted by the phrase ‘requires significant cultural change’. The desired activity is the ‘rule of law’. The politics are individual ‘freedoms’. The sign system is that the recommendations will privilege ‘all sectors’ of the industry. The legal expectation, therefore, is that industry stakeholders need to change their cultural behaviours to abide by the law and give all individuals their freedom to act in accordance with the law without unfair workplace pressure. In order to achieve cultural change, the recommendations include establishing an authority to police the industry’s behaviour, with sufficient power to punish unlawful behaviour, and that the consequences of unlawful behaviour should be clearly communicated to all stakeholders. Commissioner Cole’s frustration is evident throughout the RCR; with industry participants but also with the lack of capacity for authorities to deal with unlawful behaviour.

Implicit requirements in the social contract are those that are desirable but not enforceable by law. A cynical perspective might argue that the industry’s social contract prior to the RC was entirely implicit because it did not seem enforceable by law. However, the regulator had established a legal framework, as far back as 30 years before the RC, with the Workplace Relations Act 1974 and the Trade Practices Act 1974, which aimed to provide the legal tools to deliver industry reform. Therefore explicit requirements did exist. Implicit requirements are more related to moral motives, for example a sense of doing the right thing. Commissioner Cole’s recommendations include the implicit requirement of attitudinal change. Attitudes are difficult to monitor and perhaps impossible to police. However, attitudinal change was essential if cultural
change was to be successful. Table 4.4 uses content discourse analysis to examine the
above quote for explicit and implicit requirements.
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<td>Statute explaining difference between lawful and unlawful</td>
<td>Special</td>
<td>Conduct of work practices</td>
<td>Some stakeholders are ignorant of the law</td>
<td>Need to educate the uniformed</td>
<td>Govt. must take the lead</td>
<td>Illegality</td>
<td>Disprivileges the uniformed</td>
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<td>Law enforcement</td>
<td>Inappropriate conduct</td>
<td>Punish indiscretions</td>
<td>Union leaders are villains</td>
<td>Policing</td>
<td>Law breakers will be punished</td>
<td>Inequity</td>
<td>Privileges the law</td>
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<td>Union membership</td>
<td>Fit and proper persons</td>
<td>Unionism</td>
<td>Union leaders are villains</td>
<td>Only work with appropriate people, exclude villains</td>
<td>Exclude undesirables</td>
<td>Betrayal of workers by union officials</td>
<td>Disprivileges union officials</td>
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<tr>
<td><strong>Implicit Social Contract Expectations</strong></td>
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<td>Cultural change</td>
<td>Necessary</td>
<td>Attitudes</td>
<td>Individuals are trapped</td>
<td>All industry stakeholders are involved</td>
<td>Need for democracy</td>
<td>Freedom</td>
<td>Privileges empowerment</td>
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In summary, the RC outlines the social contract in explicit terms by requiring industry stakeholders to follow appropriate legislation as law (statute), being aware of the consequences of illegal behaviour (law enforcement), and only dealing with union officials with proper accreditation and behaviours. Implicit expectations involved cultural change essentially related to fair work practice and employee empowerment and freedom. These themes would carry on throughout the next decade of regulation of the industry.

LT also involves examining the legitimisation process, which is how industries or firms try to attain legitimacy status. The importance of pursuing legitimacy is explained in three ways: pragmatic, based on audience self-interest, moral, based on normative approval, and cognitive, based on comprehensibility and taken-for-grantedness (Suchman 1995, p. 1). Legitimacy is a relative concept in the sense that it is relative to the social system in which the organisation operates at a particular time and place (Deegan 2009, p. 324). Legitimacy motives help with understanding its relativity. Pragmatism is focused on the stakeholder doing what is right for them, morality is the sense of doing the right thing, and cognitive is ‘doing things the way we do it around here’. The legitimacy motives of the various stakeholders within the construction industry will be distinguished. This will then explain the industry’s motives for compliance or non-compliance with the social contract. Stakeholders motivated with pragmatism will be more likely to breach the social contract than stakeholders motivated by cognitive or morality motives (Deegan 2009, p. 324).

The following table uses CDA to examine the RCR (2003) for pragmatic, moral, and cognitive behaviours within the construction Industry. This assists in understanding the nature of the social contract breach, that is, ‘how’ the industry misbehaved. First, the
columns along the top of the table uses the CDA categories adopted for this study. Second, the rows along the left hand side of the table are the key themes emerging from LT’s pragmatic, moral, and cognitive constructs (see Suchman 1995). The themes were coded by the author of this study in order to classify different motives and behaviours within each of the LT constructs. The method was adapted from Gee (2011) and was explained in section 1.5.3.
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<td>Pragmatic</td>
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<tr>
<td>Bullying: Industrial Pressure</td>
<td>Threatening, surrender, inappropriate</td>
<td>Short-term profit traded off against long-term self-interest</td>
<td>Union officials villains, all others victims</td>
<td>Contractors are blackmailed</td>
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<tr>
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<td>Bullying: Union officials are appropriate</td>
<td>Improper, suspension, revoked</td>
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<td>Illegal, avoidance</td>
<td>Avoiding paying tax</td>
<td>Criminals</td>
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<td>Financial: donations</td>
<td>Failed to report, widespread practice, inappropriate</td>
<td>Financial incentives</td>
<td>Bribery</td>
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<tr>
<td>Financial: extortion</td>
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<td>Financial: Phoenix companies</td>
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<td>Evasive</td>
<td>Management are irresponsible</td>
<td>Working alone</td>
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<tr>
<td>Theme</td>
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<td>Compliance</td>
<td>Bending the rules</td>
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<td>Exploitation</td>
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<td>Disprivileges workers</td>
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<tr>
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<tr>
<td>Law enforcement:</td>
<td>Lawlessness,</td>
<td>Industrial relations,</td>
<td>Unions are villains</td>
<td>Unions make their own laws</td>
<td>Above the law</td>
<td>Criminal</td>
<td>Privileges rule breakers</td>
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<tr>
<td>Breaking the law</td>
<td>widespread disregard, contracting</td>
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<tr>
<td>Accounting practice</td>
<td>Failure, inadequate</td>
<td>Not following standards</td>
<td>Unions doing their own thing</td>
<td>Accountants vulnerable</td>
<td>Insecurity</td>
<td>Survival</td>
<td>Disprivileges accountants</td>
</tr>
</tbody>
</table>

**Moral**

<table>
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<tr>
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<th>Benefit all sectors</th>
<th>Industry behaviour</th>
<th>Industry letting down rest of society</th>
<th>Under-performing</th>
<th>Irresponsible</th>
<th>Isolated</th>
<th>Disprivileges society</th>
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</thead>
<tbody>
<tr>
<td>Empowerment: apprenticeships</td>
<td>Facilitate, encourage</td>
<td>Recruitment, training</td>
<td>Employers as mentors</td>
<td>Young people vulnerable</td>
<td>Irresponsible</td>
<td>Avoidance</td>
<td>Disprivileges young people</td>
</tr>
<tr>
<td>Empowerment: full payments</td>
<td>Entitlements</td>
<td>Payroll</td>
<td>Employers as providers</td>
<td>Workers are vulnerable</td>
<td>Irresponsible</td>
<td>Avoidance</td>
<td>Disprivileges workers</td>
</tr>
<tr>
<td>Empowerment: staff training</td>
<td>Method</td>
<td>Training</td>
<td>Employers caring for staff</td>
<td>Workers must be qualified</td>
<td>Compliance</td>
<td>Survival</td>
<td>Privileges qualifications</td>
</tr>
<tr>
<td>Empowerment: workers</td>
<td>Obligation</td>
<td>Human Resource Management (HRM)</td>
<td>Caring for sick or injured staff</td>
<td>Workers are vulnerable</td>
<td>Irresponsible</td>
<td>Avoidance</td>
<td>Disprivileges workers</td>
</tr>
</tbody>
</table>

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<table>
<thead>
<tr>
<th>Theme</th>
<th>Significance</th>
<th>Activities</th>
<th>Identities</th>
<th>Relationships</th>
<th>Politics</th>
<th>Connections</th>
<th>Sign Systems</th>
</tr>
</thead>
<tbody>
<tr>
<td>Industrial relations: dispute resolution</td>
<td>Rule of law must apply</td>
<td>HRM</td>
<td>Inequity</td>
<td>Workers are vulnerable</td>
<td>Stand-over tactics</td>
<td>Intimidation</td>
<td>Privileges contractors as victims</td>
</tr>
<tr>
<td>Industrial relations: enterprise bargaining</td>
<td>Necessary</td>
<td>Industrial relations</td>
<td>Unions as advocates</td>
<td>Workers are exploited</td>
<td>Stand-over tactics</td>
<td>Intimidation</td>
<td>Privileges contractors as victims</td>
</tr>
<tr>
<td>Law enforcement: independent authority needed</td>
<td>Free of pressures</td>
<td>Industrial relations</td>
<td>Watchdog role</td>
<td>Objective authority</td>
<td>Powerless authorities</td>
<td>Apathy</td>
<td>Disprivileges authorities</td>
</tr>
<tr>
<td>Law enforcement: no consequences</td>
<td>Need penalties, policing</td>
<td>Industrial relations</td>
<td>Policing role</td>
<td>Anarchy</td>
<td>Powerless authorities</td>
<td>No penalty</td>
<td>Disprivileges authorities</td>
</tr>
<tr>
<td>Relationships: conflicting goals</td>
<td>Control</td>
<td>Value appropriation</td>
<td>Conflicting agendas</td>
<td>Competition</td>
<td>Negotiation</td>
<td>The powerful win</td>
<td>Disprivileges workers</td>
</tr>
<tr>
<td>Cognitive</td>
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<tr>
<td>Empowerment: need freedom of association</td>
<td>Provisions</td>
<td>Management control</td>
<td>Workers independence</td>
<td>Multiple networks</td>
<td>Personal choice</td>
<td>Freedom</td>
<td>Privileges workers</td>
</tr>
<tr>
<td>Work practices: deny individual freedom</td>
<td>Interference, denial of rights</td>
<td>Industrial relations</td>
<td>Unions controlling</td>
<td>Workers are controlled</td>
<td>Powerless staff</td>
<td>Autonomy</td>
<td>Privileges workers</td>
</tr>
</tbody>
</table>
The CDA indicates that there are a range of themes explaining the motives of industry stakeholders in breaching the social contract. The main theme is pragmatism or self-interest. There is a culture of bullying and coercion as well as poor financial management. The sign systems privilege rule breakers, and contractors as victims. The analysis highlights socio-political power inequities; illustrated by connections. The role of accounting in relation to non-financial work practices is discussed in this chapter. The role of accounting in relation to the financial areas is discussed in this chapter 6. The moral themes are about doing the right thing and include empowerment of staff, need for law enforcement, as well as industrial relations and relationships. However, the results show that workers are often disprivileged and vulnerable to employers/owners/management (that is, contractors) avoiding responsibilities. The cognitive themes are shared cultural norms across the industry and include the need for fair work practices related to freedom of individuals.

Table 4.5 explains the construction industry’s legitimacy gap in terms of ‘how’ it happened and ‘why’ it happened. In terms of the ‘how’, the behaviour that the regulator found unsatisfactory is explained by the horizontal themes on the left hand side of the table. In terms of the ‘why’, the reasons for the legitimacy gap occurring are explained by the LT constructs, pragmatic, moral, and cognitive, with evidence provided by the CDA classifications on the top of the table.

The RC lays the blame for the social contract breach mainly with the unions and for the reasons of self-interest and lack of fear of consequences. However, blame may be shared amongst all stakeholders. The ultimate cause of the industry’s behaviour is competition and profit. Industry structure meant intense competition, tight profit margins, and a short term focus. Customers were demanding and wanted projects to
finish on time and on budget. The unions were aware of these pressures and used them to their advantage. They set themselves up as the industry regulator, interested in the long term, due to their concerns for employment of their members. The sustainability of the industry was the unions’ goal because it meant safe and secure long term employment for members. They used tight profit margins and contractors’ need to meet time schedules demanded by customers to negotiate a powerful industry position. They knew that industrial action would lead to delays, projects over-schedule, and unhappy customers. They used this to coerce contractors to cooperate with their self-interests in return for no industrial action. It was essentially industrial blackmail. This assists our understanding regarding the nature of the social contract breach, that is, why and how the industry misbehaved.

In summary, this section used LT to examine three aspects of the RC’s recommendations on cultural reform for the construction industry: social contract, breach, and legitimacy gap. The social contract explains what society expected of the industry. The analysis shows that explicit expectations required industry stakeholders to follow appropriate legislation as law (statute), being aware of the consequences of illegal behaviour (law enforcement), while implicit expectations involved cultural change essentially related to fair work practice and employee empowerment and freedom. The breach explains why society felt the industry was not fulfilling its contract, that is, why it was misbehaving. The analysis shows that there was bullying, inadequate financial management, disempowerment, conflicting relationships, unfair workplace practices, industrial disputation, and unsatisfactory law enforcement. The legitimacy gap explains how this situation has occurred and how the industry behaviour came to differ from society’s expectations. The analysis shows that there was a culture of industrial pressure which led to organised financial mismanagement; failed moral
responsibility to do the right thing by society and the owners of the resources conferred by society; and a shared cognitive denial of freedom of individuals to act without fear of consequences.

4.6 Industry Regulation After the Royal Commission

4.6.1 Introduction

Commissioner Cole submitted his final reports and they were tabled before Federal Parliament in March 2003. Commissioner Cole had recommended significant structural and cultural reform if the construction industry was to repair its legitimacy gap. A study of this reform is, therefore, an empirical investigation of the legitimisation process, helping with understanding how an industry regains legitimacy once it has been lost.

Following the RCR, reforms were announced by the DEWR (2003), Australian Productivity Commission (APC) Report (2004), the BIT Reports (2004, 2005), the BCII Act 2005, the Office of the ABCC (2005), The Wilcox Report (2009), and the current regulatory environment. The history of regulation presented by these activities, largely reconstructs the government’s efforts to implement the recommendations of the RC. In this sense, it is somewhat of a one-sided history in that it represents society’s attempts to legitimise the industry. However, also gained is perspective about the industry’s response to regulation in this period. The nature of the activities undertaken by the government to implement the recommendations of the RC and their evolution reveals much about how much the industry helped itself regain legitimacy, that is, the legitimisation process.
4.6.2 The Department of Employment and Workplace Relations (2003)

The DEWR was the Government Department tasked with implementing the recommendations of the RC. In 2003, the Department issued a statement regarding the outcomes of the RC. This statement is analysed using the CDA framework in order to identify the regulator’s focus immediately after the RC was completed. While the statement is repetitive, in the sense that it covers some of the same material presented above in the section on the RC findings, it is an important historical document because it explains what mattered most to the regulator at that time. The DEWR statement is the regulator’s attempt to filter the 23 volumes of the RCR and distil this into a social reconstruction of the industry’s social contract. It tells what the regulator, on behalf of society, expected from the construction industry just after the RC.

The DEWR statement summarised the RC findings as “lawlessness” (DEWR 2003, p. 5). DEWR highlights Commissioner Cole findings regarding the “widespread disregard for criminal, civil, and industrial laws mark(ing) the industry as singular”, as support for taking action to “fix” the industry (DEWR 2003, p. 9). DEWR is highlighting for the public that the social contract has been breached and that this can no longer be tolerated.

DEWR then explained why it was now time to fix this problem. The DEWR statement explained how previous attempts to regulate the industry had failed. It accepted Commissioner Cole’s findings that “the current workplace relations laws were ineffective for the building industry and that the existing regulatory bodies have insufficient structures to enforce the law and standards of behaviour applicable to other industries” (DEWR 2003, p. 16). This statement shows that the regulator accepts some responsibility for the construction industry’s social contract breach because existing legal frameworks were unable to enforce the contract onto industry stakeholders. It also
indicates the regulator's acceptance that an important part of the solution legislation change to increase the power of regulatory authorities.

Tables 4.6 and 4.7 use CA and CDA frameworks to summarise this analysis of the DEWR statement. It explains the Government's interpretation of the RC findings and represents an endorsement.

<table>
<thead>
<tr>
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<tbody>
<tr>
<td><strong>Social Contract Expectations</strong></td>
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<tr>
<td>Explicit: Lawlessness</td>
</tr>
<tr>
<td>Implicit: Law enforcement difficult</td>
</tr>
<tr>
<td>Cognitive: Disregard for the law</td>
</tr>
</tbody>
</table>
Table 4.7: Content Discourse Analysis of Selected Themes from Department of Employment and Workplace Relations (2003)

<table>
<thead>
<tr>
<th>Theme</th>
<th>Significance</th>
<th>Activities</th>
<th>Identities</th>
<th>Relationships</th>
<th>Politics</th>
<th>Connections</th>
<th>Sign Systems</th>
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<tbody>
<tr>
<td><strong>Explicit Social Contract Expectations</strong></td>
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</tr>
<tr>
<td>Lawlessness</td>
<td>Widespread disregard</td>
<td>Industrial relations, employment</td>
<td>Union leaders are standover men</td>
<td>Unions intimidating employers and workers</td>
<td>Unions in charge</td>
<td>Illegality</td>
<td>Dis-privilege law makers</td>
</tr>
<tr>
<td>Implicit Social Contract Expectations</td>
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</tr>
<tr>
<td>Law Enforcement Difficult</td>
<td>Significant weaknesses</td>
<td>Industrial relations, Management, HRM, Accounting, Taxation</td>
<td>Invisible criminals</td>
<td>Management, unions, subcontractors</td>
<td>Feel bulletproof</td>
<td>Unaccountable</td>
<td>Fighting shadows</td>
</tr>
<tr>
<td>Pragmatic Motives</td>
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<tr>
<td>Misuse of Funds</td>
<td>Compliance</td>
<td>See above</td>
<td>Self-interest</td>
<td>Management, unions, subcontractors</td>
<td>Law unto themselves</td>
<td>Illegality</td>
<td>Dark shadows</td>
</tr>
<tr>
<td>Moral Motives</td>
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<tr>
<td>Industrial agreements</td>
<td>Flouted</td>
<td>HRM</td>
<td>Unions do deals</td>
<td>Management, unions, subcontractors</td>
<td>Law unto themselves</td>
<td>Illegality</td>
<td>Head in the sand</td>
</tr>
<tr>
<td>Occupational Health and Safety</td>
<td>Ignored</td>
<td>HRM</td>
<td>Short-cuts taken</td>
<td>Management, unions</td>
<td>Workers exploited</td>
<td>Safety</td>
<td>Risk takers</td>
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<tr>
<td>Cognitive Motives</td>
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</tr>
<tr>
<td>Disregard for the law</td>
<td>Widespread Deep-seated</td>
<td>All</td>
<td>Unions, management bad guys</td>
<td>Management, unions</td>
<td>Law unto themselves</td>
<td>Illegality</td>
<td>Privileges outlaws</td>
</tr>
</tbody>
</table>
Table 4.7: Content Discourse Analysis of Selected Themes from Department of Employment and Workplace Relations (2003)

<table>
<thead>
<tr>
<th>Theme</th>
<th>Significance</th>
<th>Activities</th>
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<th>Relationships</th>
<th>Politics</th>
<th>Connections</th>
<th>Sign Systems</th>
</tr>
</thead>
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<tr>
<td><strong>Legitimacy Gap</strong></td>
<td></td>
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<td></td>
</tr>
<tr>
<td>Law must be enforceable</td>
<td>Urgent Need</td>
<td>Government</td>
<td>Regulator</td>
<td>Watchdog, policing</td>
<td>Enforcing law</td>
<td>Toothless</td>
<td>Shooting without bullets</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>taking charge</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Arrogance for society</td>
<td>Unlawful conduct</td>
<td>All</td>
<td>Separate community</td>
<td>Relationship with rest of society fractured</td>
<td>Separate state</td>
<td>Untouchable</td>
<td>Privileges individualism</td>
</tr>
</tbody>
</table>

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The CDA shows that the DEWR Statement was highly critical of the construction industry. This was shown by the language used to measure the significance of the problem, that is, unlawful, widespread, and deep-seated. It also comments on a wider range of activities compared with the PM’s Statement, particularly occupational health and safety and taxation. It is scathing in its attack on the culture which made industry stakeholders feel they were above the law and could act as they wished. It also reveals frustration with the regulation of the industry, particularly the inability to enforce the law. There is the suggestion that the perpetrators realised that their behaviour would not, or perhaps could not, be punished and that this exacerbated the problem. Therefore, this statement includes the regulators of the industry stakeholders in being responsible for allowing the lawlessness to carry on. This raises questions about the role of accounting in the industry’s behaviour and accounting bodies, including auditors and the regulators of accounting standards.


As established in chapter 3, the construction industry is very important to Australia. Commissioner Cole explained that the industry’s performance had a significant direct and indirect impact on many sectors of the economy. PIT explains how society confers resources on industries and firms in return for them meeting society’s expectation to use those resources wisely. Commissioner Cole found structural issues that caused inefficiencies within the industry and poor performance. After the RC was completed in 2003, the Government directed the Productivity Commission to investigate further why the industry was performing poorly and not meeting its social contract.

The APC is the “Australian Government's independent research and advisory body on a range of economic, social and environmental issues affecting the welfare of
Australians” (Productivity Commission 2016, p. ii). The role of the APC is “to help governments make better policies in the long term interest of the Australian community” (Productivity Commission 2016, p. ii). The Productivity Commission completed a study of the construction industry in 2004. The Report focused mainly on the Construction Industry’s actual work practices, that is, what companies do to build houses, factories, offices, and infrastructure. The focus, therefore, was on how the construction industry utilised the resources allocated to it by society and its efficiency. The Report’s recommendations were about construction quality, safety standards, use of materials, employee training and skills. In this way, the focus was more “micro” because it focused on what companies do. The RC, and subsequent efforts at regulation, focused more on “macro” issues in the sense of interactions between companies.

The Productivity Commission recognised that the Construction Industry regulatory system was flawed. However, the Report looked at it from a different angle compared to the “macro” reviews. The Productivity Commission explained the regulatory system as follows:

The building sector is subject to a diverse range of regulations by all levels of government. Reform of building regulation essentially has been directed at improving this regulatory system, with a particular focus on achieving a national framework. Assessing this reform requires an examination of the ABCC’s performance in relation to its mission statement, objectives and work program (Productivity Commission 2004, p.25)

This shows that the Productivity Commission focused on the regulation of building construction itself, that is, whether buildings are safe and sound, rather than the activities of industry stakeholders. It suggests a legacy view, that is, the way the industry had always been regulated, with a focus on the product itself rather than the companies. The APC report found that regulation was fragmented in the sense that responsibility for governance of building construction itself was carried out by various...
levels of Government, that is, Federal, State and Local, and there were inconsistencies across state boundaries.

Regulation, historically, was focused around the Building Code of Australia, which centred on planning and building standards. The following extract provides information on the code:

“The Building Code encourages productivity and lawful workplace relations on building sites. It sets out the Australian Government’s expected standards for building contractors or building industry participants involved in Commonwealth funded construction projects. The Building Code codifies the obligations previously contained in the National Code of Practice for the Construction Industry. It came into effect on 1 February 2013” (Department of Treasury and Finance 2015, p. 18).

The Building Code aims to establish higher standards of workplace relations behaviour; and improve flexibility and productivity. However, prior to the current regulator’s focus on workplace relations, the building code was about quality control. The regulatory process, therefore, has historically focused mainly on building inspectors checking on the quality of work and on local government planners ensuring that the building met local community expectations. Regulation was classified into these activities:

1. Design Phase: approvals, permits, insurance, contracts.
2. Construction Phase: inspections, accreditation of materials & processes
3. Completion & Use Phase: occupancy certificate, essential services, maintenance checks, Dispute resolution

The main theme here is building performance and conformance with society and consumer expectations. The way the industry conducted its business seemed to be largely ignored as long as its product, the buildings and infrastructure, was satisfactory.
4.6.4 Building Industry Taskforce (2002-2005)

On the 1 October 2002, the BIT was established as an interim body to secure the law in the construction industry before the establishment of the national agency envisaged by Commissioner Cole (FWBC 2012b). It was an important step in the Government’s new reform agenda. The DEWR emphasised the importance of reform:

The Australian Government supports the key recommendations of the Royal Commission. Reform of the building sector is a priority matter for the Government. The Government is committed to ensuring that the rule of law applies in the building industry as it does everywhere else. With the constructive cooperation of industry participants and all levels of government, a fairer, safer and more decent industry will emerge. The Government recognises that it needs to show leadership and address the specific issues in the building and construction industry (DEWR 2003, p. 8).

DEWR explained that the BIT was created as ‘an initial priority’ was to establish a “dedicated body with the power to investigate and enforce the workplace relations law on building sites” (DEWR 2003, p. 27). This was the Interim BIT. By 2003, the Government felt the Interim BIT was “having a positive influence on the industry's behaviour. The industry is realising that people who undertake intimidating and standover tactics will be prosecuted” (DEWR 2003, p. 36). The Interim Taskforce became a permanent taskforce in March 2004 and operated until the Office of the ABCC was established in October 2005 (FWBC 2012b). The BIT released two reports on its activities and the environment in which it operated:

- Upholding the Law - One year on: Findings of the Interim Building Industry Taskforce
- Upholding the Law: Findings of the Building Industry Taskforce

Both of these BIT Reports are analysed to assess the construction industry’s response to the RC activities and reports, that is whether the industry began to try to comply with society expectations and to bridge the legitimacy gap. The Government was pleased
with the initial progress of the BIT. The DEWR praised the initial work of the taskforce (DEWR 2003, p. 11).

The first BIT Report, One Year One, provides evidence of the construction industry’s initial response to the Federal Government’s decision to conduct a RC into its activities. The Report was released on 25 March 2004. The RC told the industry that it has breached its social contract and that it is no longer ascribed legitimate status by society and access to resources which is granted as a result of legitimacy.

The construction industry should have responded to the RC in a positive fashion, that is, seek to first acknowledge society’s concerns and second to address them, in a bid to regain legitimacy. However, the first BIT report indicates that the construction industry did not respond in this way. The covering letter to the Minister for Employment and Workplace Relations by the BIT Director, Nigel C Hadgkiss, includes this comment:

herewith is a report which provides an overview of the environment in which the Taskforce operates, highlighting in particular the continuation of unlawful and inappropriate behaviour in the industry. The document also addresses the overwhelming requirement for greater powers in order to fulfil the Government’s objective of securing the rule of law (Hadgkiss 2004, p. ii).

Hadgkiss is highlighting his frustration as the industry appears to have carried on with the behaviour which led to the RC and the lack of authority to force the industry to cooperate. This is clear evidence that the regulator’s decision to conduct a RC and Commissioner Cole’s findings did not succeed in changing the industry’s unlawful behaviour. Commissioner Cole clearly stated that there was a social contract breach. This was endorsed by the Government through the statement from the DEWR. Society had expressed its dissatisfaction with the industry in its strongest possible terms. Yet the first BIT Report found that the industry had not been shocked into action. It seemed to ignore the RC and to carry on its unlawful behaviour regardless.
In defining the nature of the unlawful and inappropriate behaviour, that is the social contract breach, Hadgkiss lists the following:

- Nature of complaints received by the Taskforce
- Introduction not restoration of the rule of law
- Contempt for the law
- Organised crime and corruption in the industry
- Violence, thuggery and intimidation
- Donations or outright extortion
- An industry like no other
- Misuse of occupational health and safety
- Fear of retribution (Hadgkiss 2004, pp. 3-13).

This list of unlawful and inappropriate behaviour is consistent with the themes identified using CDA of the RC findings. However, the BIT report uses even stronger language, such as ‘outright extortion, contempt, and fear’ to highlight the significance of the problem. The phrase ‘organised crime and corruption’ is particularly disturbing.

Mr Hadgkiss has taken criticism of the industry to another level. There is nothing cautious about these comments. Mr Hadgkiss must have felt he had strong evidence to support his claims. It seems the industry was getting worse, rather than better, after the RC.

The first paragraph of the Executive Summary explains how the construction industry continued to breach its social contract and why this angered the Government:

Behaviours that are unacceptable by general community standards are the norm in the industry. Too many Australians attempting to earn an honest living have become victims of the industry’s blatant disregard for the law (Hadgkiss 2004, p. iv).

There is considerable powerful language in this statement which is highlighted by the CDA framework. The most important content are the words ‘unacceptable’, which clearly states the significance of the problem; ‘too many’, which is a connection phrase to amplify the problem; ‘honest living’, which is a political attribute given to workers...
for good behaviour in contrast with union leaders; ‘victims’, the identity given to workers; and ‘blatant disregard for the law’, is the activity causing the social contract breach.

Mr Hadgkiss makes the accusation that the construction industry has always been lawless:

The challenge...is not to simply restore the rule of law to the industry, it is to introduce the rule of law for the first time (Hadgkiss 2004, p. iv).

This is a very important comment because it suggests that the construction industry should have never been given legitimacy status because its behaviour was never proper or appropriate. This means that society’s tolerance for the industry was based on the desirability of its services and not its activities or the way it conducted business. This is an important finding for this study in the social reconstruction of the role of accounting, because accountants employed by the industry may have become aware that the industry was different to other industries and the practice of accounting may also have to be different due to the suggestion that it had never operated lawfully.

The unique nature of the industry made it extremely difficult for the Government to resolve the social contract breach, as shown by this extract:

Approaches for reform which may be appropriate for other industries would simply fail in the building and construction industry because of the poor state of workplace relations and the pervading culture of lawlessness. Most concerning to the Taskforce are reports received about threats and intimidation being used as a means of advancing industrial agendas. Such coercion is indicative of how countless industrial disputes are currently resolved in the industry (Hadgkiss 2004, p. iv).

The BIT found that the main problems associated with the social contract breach were corruption and criminal activity. On corruption the report stated: “union officials extort
money and services in return for industrial peace on building sites” (Hadgkiss 2004: p iv). On criminal activity the report stated “The Taskforce is particularly alarmed about elements of organised crime operating within the industry” (Hadgkiss 2004: p iv). It is clear that the BIT report felt the culture of unlawfulness in the construction industry was due to the unions:

The union are a police force of their own but they make up the rules as they go along (Hadgkiss 2004, p. 3).

While it is easy to lay the blame for the construction industry’s behaviour solely with the trade union leaders, the other industry stakeholders were also involved. As illustrated by the following quote from the BIT report, the contractors participated in the corrupt activity, even if it was as unwilling bullying victims:

It is like a school yard. You’ve got your bullies (unions), the wimps (head contractors) and the blokes who just want to have a kick of the footy (subcontractors) (Hadgkiss 2004, p. 1).

From this it can inferred that management was involved because they interacted with the unions over industrial relations matters. The BIT report provides some clues about whether accountants were involved. First, in a section on the role of women in the industry, it states that:

The Taskforce has found that the work engaged in by women tends to be of an administrative, clerical and accounting nature, with women rarely holding senior or middle management positions. Very few women are employed as labourers or in trades, or in professional fields such as architecture or engineering (Hadgkiss 2004, p.16).

While this paints an unflattering picture of the role of accountants in the construction industry, that is, as lower level staff not deserving professional status, it does infer that accountants would probably not have been involved in direct dealings with union
leaders or even contractor management. They might then have been distanced from the actual unlawful behaviour or at least not in a position where they could directly influence the behaviour. This is inferred because of the phrase “rarely holding senior or middle management position” (Hadgkiss 2004, p.16). Of course not all accountants employed by the industry were women, but the status allocated to accountants, lower level, is an important clue in terms of their relationship with other stakeholders, and their level of involvement in the industry’s unlawful behaviour. This is examined further in chapters 5 and 6.

However, there are signs that some accounting staff may have been exposed or involved in some unlawful behaviour. The following quote from the BIT report illustrates the importance of money in the industry:

All decisions come down to money (Hadgkiss 2004, p. 20).

If money was involved in the unlawful behaviour, then accountants had to be involved in some way. If money was exchanged between contractors and union leaders, accountants should have known about it.

The BIT report argued that unions extorted money from contractors, which is illegal activity. Accountants may have been unaware funds were being manipulated in this way. The following extract from the BIT report shows how this manipulation was done.

In the latter part of 2003, a subcontractor was required by a union official to purchase t-shirts, bearing a union logo, at a cost of thousands of dollars per item. The subcontractor provided payment in return for access to the site where he could continue his work. This type of activity is common on sites throughout Australia. In one city, the clothing company awarded these clothing contracts is owned by the wife of a union organiser. In a matter investigated by the Taskforce in February 2004, a subcontractor was charged $1,000 by a union official for each of the seven days he worked on a site. The official demanded this payment because the subcontractor did not have a union endorsed Enterprise
Bargaining Agreement (EBA). The subcontractor was issued with receipts that indicated the payment was for t-shirts (Hadgkiss 2004, p. 9).

The extract provides evidence of inappropriate use of funds and financial mismanagement. In reconstructing the social reality of what happened here, would accountants have been involved in this activity, if not, should they have been, and if so, what was their role? Possibly the payment may have been processed as a lump sum under the expense item t-shirts. However, what happened and how accountants employed by the firms involved behaved is not exactly known. A very good accountant would have investigated and questioned the number of t-shirts purchased for the funds. Despite an expectation of some cognizance of the dubious nature of the transaction, it is difficult to know, when illegal funds are laundered in this way, the extent of the accountant’s involvement. However cash is a different matter.

As seen from the allegations of corruption in the ABC Four Corners transcript, union leaders appeared to expect “donations” to the unions made by contractors as normal part of doing business. Indeed, Andrew Ferguson made several comments defending this practice. In response to a question from Neighbour “so you forced them to pay?”, he explained that contractors “were forced to pay to meet their moral obligations”, and added that “we don’t apologise” (Neighbour 2001). However, the BIT report argues that this practice was extortion, that is, it was forced upon people illegally, rather than a voluntary act of kindness on the part of the donor, as illustrated by this extract from the Report:

The Taskforce believes donations received by unions are not only required from employers but also from union members. Since the tabling of the Final Report of the Royal Commission, head contractors, subcontractors and employees alike have been required to make weekly donations to union ‘fighting funds’ which have been established to help pay for the costs of defending court actions. As many of the donations received by union officials are cash and not receipted, the Taskforce is at a loss as to where the money ends up. The Taskforce lacks the requisite powers to follow the money trail. Moreover, when these kinds of
matters are referred to the Australian Taxation Office (ATO), the Taskforce is unable to receive any feedback on the dissemination of the information because it is not a statutory law enforcement agency recognised under the Income Tax Assessment Act or the Taxation Administration Act. Consequently there is no capacity for the ATO to share information with the Taskforce (Hadgkiss 2004, p. 10).

The extract shows that when cash was involved, it was very difficult to follow the “money trail”. This raises the important question of whether accountants were involved in this money trail and what role accounting practice could have played to bring lawfulness to this activity.

The second BIT report was released on 15 September 2005, two years after the RCR was tabled, and it highlights that the construction industry had done little to repair its legitimacy status. While the cover of the report has newspaper headlines of union officials being bashed and union offices being shot at, suggesting contractors were fighting back, the industry remained in turmoil as illustrated by this statement from Hadgkiss’s covering letter to the Minister:

Contempt for the law and hostility towards the Taskforce remains the culture, and continues to have consequences for those who would like to see reform. This document highlights the continuation of unlawful and inappropriate behaviour in the industry (Hadgkiss 2005, p. 4).

The second BIT report shows that the Taskforce has tried to enforce law within the construction industry had “placed 29 matters before the courts”; and “16 of those court actions have been completed following cases investigated and prepared by the Taskforce” (Hadgkiss 2005, p. i). At face value, this might suggest significant improvement in industry behaviour and progress towards legitimisation. The RC found more than 400 cases of unlawful behaviour. The second BIT report, two years after the completion of the RC, found 29 cases. Twentynine is much less than 400, and so suggests considerable improvement. However, the second BIT report concluded that
two years after the RCR was tabled, “the industry remains plagued by a culture of civil disobedience, coercion, intimidation, threatening behaviour, and contempt for the law” (Hadgkiss 2005, p. i). This means Mr Hadgkiss found the same behaviour as Commissioner Cole in 2003, and the first BIT Report in 2004. The RC had far wider ranging powers and scope than the BIT and, as a result, it is also reasonable to conclude that the 29 cases may represent comparable levels of unlawful behaviour. It is also reasonable to conclude that society should not tolerate even one case of unlawful and behaviour from the industry. Therefore, the 29 cases found by the second BIT report provides strong evidence that the industry had not repaired its legitimacy and there was still a significant legitimacy gap two years after the RC.

The reasons for this continued unlawfulness, despite the RCR and the activities of the BIT, were a culture of fear and retribution, as illustrated by this extract from the Report:

A cause for this ongoing culture of lawlessness is that the Taskforce has been at a loss to pursue complaints because a fair proportion of callers are reluctant to take them to the investigation level. Taskforce investigators maintain that callers often report instances of unlawful activity but do not want to assist any further in the investigation. Such decisions to acquiesce are invariably motivated by the commercial reality that if they do not succumb to this industrial pressure, they will lose their business and livelihood. As a result, it has become increasingly apparent to the Taskforce that industrial problems are very rarely resolved permanently, but rather go into remission (Hadgkiss 2005, p. i).

This culture of intimidation suggests that accountants too might have operated in fear for their jobs and, perhaps, have chosen to ignore unlawful behaviours rather than risk their livelihood. The sense of consequence for those who did not participate in the culture of unlawfulness is further illustrated by this quote:

You have to cheat to compete, Taskforce caller (Hadgkiss 2005, p. 2).
The fact that this caller was willing to call the BIT and offer this comment suggests a sense of moral intolerance for the activity, but acceptance that it was necessary in order to survive in the industry. In explaining that the unlawful behaviour continues, the following quote highlights how contractors felt they had no choice but to participate despite the RC:

employers are talking (to the unions) because they know the union can make their life a misery anyhow - and will still be able to post-Cole (reform), though it will be harder (Hadgkiss 2005, p. 2).

The comment shows how the RC had limited impact, in the two years after its tabling in parliament. While it made the unlawfulness more difficult, this carried on regardless. The industry’s unlawful behaviour involved all participants, however, it is clear that the main problem was the union leaders. The BIT report showed that 72% of complaints received by the Taskforce were against trade union officials (Hadgkiss 2005, p. 4). The following quote further illustrates that the industry continued its unlawfulness despite the RC:

We’re working in an industry that has no laws, Taskforce caller (Hadgkiss 2005, p. 7).

While Hadgkiss appears very frustrated by his inability to enact change, the BIT played an important role in the initial period of reform following the RC in 2003. The reform program included:

- propose a building Act to govern workplace relations in the industry;
- create an enforcement body – headed by the ABCC;
- improve occupational health and safety – a Federal Safety Commissioner;
- increase penalties and allow those affected by unlawful industrial action to recover damages;
- use Australian Government purchasing power to bring about reform and adherence to a new Australian Government Building Code;
- assist employees to protect entitlements they are due;
- encourage training, traineeships and apprenticeships;
• combat tax evasion and fraudulent phoenix company activities (DEWR 2003, p. 58).

This reform package was designed to “introduce a robust enforcement regime to combat the industry’s lawlessness, significantly improve current patterns of conduct and establish the rule of law in the building industry” (DEWR 2003, p. 58).
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<thead>
<tr>
<th>Theme</th>
<th>Significance</th>
<th>Activities</th>
<th>Identities</th>
<th>Relationships</th>
<th>Politics</th>
<th>Connections</th>
<th>Sign Systems</th>
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<tbody>
<tr>
<td><strong>Explicit Social Contract Expectations</strong></td>
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<tr>
<td>Lawlessness</td>
<td>Always been, Blatant disregard</td>
<td>Industrial relations, employment</td>
<td>Union leaders are villains, employees are victims</td>
<td>Unions intimidating employers and workers</td>
<td>Unions in charge</td>
<td>Illegality</td>
<td>Honest living (victims) contrasted with dishonest living</td>
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<td>Organised crime</td>
<td>Elements exist</td>
<td>Extorting money in return for industrial peace</td>
<td>Some criminals involved</td>
<td>Individuals with connection to crime groups</td>
<td>Using coercion to intimidate</td>
<td>Illegality</td>
<td>Bad elements spreading disease</td>
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<td><strong>Implicit Social Contract Expectations</strong></td>
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<td>Law Enforcement Difficult</td>
<td>Significant weaknesses</td>
<td>Industrial relations, Management, HRM, Accounting, Taxation</td>
<td>Invisible criminals</td>
<td>Management, unions, sub-contractors</td>
<td>Feel bulletproof</td>
<td>Unaccountable</td>
<td>Dis-privileges authorities</td>
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<td>Cash incentives with no receipts</td>
<td>Cheat to compete</td>
<td>Industrial relations, tendering</td>
<td>Individuals as underworld figures</td>
<td>Money trail is invisible</td>
<td>Bribery</td>
<td>Criminality</td>
<td>Privileges dishonesty</td>
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<td>Fairer workplace</td>
<td>Robust reform needed</td>
<td>Improved legislation</td>
<td>Toothless legislators</td>
<td>Unions bullying employers</td>
<td>Inequity</td>
<td>Ineffectiveness</td>
<td>Dis-privileges authorities</td>
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<tr>
<td>Theme</td>
<td>Significance</td>
<td>Activities</td>
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<td><strong>Pragmatic Motives</strong></td>
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<td>Industrial disputes used as intimidation to serve self-interest</td>
<td>Coercion, Standover tactics</td>
<td>Industrial relations</td>
<td>Unions are bullies, management are wimps, and sub-contractors just want to play</td>
<td>Management, unions, sub-contractors</td>
<td>School yard bullying</td>
<td>Intimidation</td>
<td>Childish</td>
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<td><strong>Moral Motives</strong></td>
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<td><strong>Cognitive Motives</strong></td>
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<td>Fear of retribution</td>
<td>Fear</td>
<td>Industrial relations, tendering, contracts</td>
<td>Bullies versus victims</td>
<td>Weak are intimidated</td>
<td>Coercion of the weak</td>
<td>Bullies</td>
<td>Privileges those with power</td>
</tr>
<tr>
<td>Decisions influenced by money</td>
<td>Everything</td>
<td>Industrial relations, tendering, contracts</td>
<td>People with power getting rich</td>
<td>Corrupt behaviour is rewarded</td>
<td>Money trail is invisible</td>
<td>Justified criminality</td>
<td>Dis-privileges the exploited</td>
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<td><strong>Legitimacy Gap</strong></td>
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<td>Law must be enforceable</td>
<td>Overwhelming requirement</td>
<td>Government</td>
<td>Regulator taking charge</td>
<td>Watchdog, policing</td>
<td>Enforcing law</td>
<td>Toothless</td>
<td>Dis-privileges authorities</td>
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CHAPTER 4: HISTORY OF REGULATION
Table 4.8: Content Discourse Analysis of Selected Themes from Building Industry Taskforce Reports (2004, 2005)

<table>
<thead>
<tr>
<th>Theme</th>
<th>Significance</th>
<th>Activities</th>
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<th>Relationships</th>
<th>Politics</th>
<th>Connections</th>
<th>Sign Systems</th>
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</thead>
<tbody>
<tr>
<td>Arrogance for society</td>
<td>Contempt, Unacceptable relations</td>
<td>Industrial relations</td>
<td>Separate community</td>
<td>Hostility towards regulators</td>
<td>Aggression</td>
<td>Ideology justifies bad behaviour</td>
<td>Privileges outlaw behaviour</td>
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<tr>
<td>Prosecute illegal activities</td>
<td>Sustained change</td>
<td>Government</td>
<td>Regulator taking matters to court</td>
<td>Regulator taking action over criminals</td>
<td>Prosecution</td>
<td>Demonstrating law is enforceable</td>
<td>Privileges increased authority</td>
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</tbody>
</table>
In summary, the CDA of the BIT Reports reveals that the legitimacy gap remained in the years immediately following the RC (2003) because the regulator did not have sufficient power to enforce the law. The figures in the second BIT Report (Hadgkiss 2005) are particularly damning. The taskforce visited over 1,000 sites, issued around 230 notices to produce evidence to individuals (23% of visits), employers and unions and taken 6 matters to court (0.06%) (Hadgkiss 2005, p. 1). Less than 1% of site visits by the BIT led to a court appearance (Hadgkiss 2005, p. 1).

The language used by the BIT reports is more critical of the industry compared with the previous regulatory reports analysed so far in this study. The BIT feels that lawlessness has actually increased since the RC. Therefore, two years after the RCR was tabled in parliament, 2005, it was not having the desired effect. The social contract breach was actually getting worse. The BIT blames the unions and some union officials for engaging in illegal activities with suggestions of links to organised crime and extortion. The phrase ‘civil disobedience’ is a polite way of describing this behaviour. The BIT is scathing in its perception of the immaturity of this workplace behaviour, using the theme of bullying and phrases such as schoolyard tactics to condemn the industry.

It is important for this study to note that money seems to be more explicitly mentioned by the BIT. The BIT seems to have uncovered financial mismanagement. The fact that ‘money drives every decision’ suggests the power of profitability but also that corruption and bribery were rife. The final recommendation in the second BIT Report was the need to “combat tax evasion and fraudulent phoenix company activities” (Hadgkiss 2005, p. 23). Accountants would have been involved in these types of activities. Managers, union officials, and sub-contractors would probably not have the
skills or knowledge to engage in this type of illegal activity without help from accountants.

4.7 Enacting Reform

4.7.1 Building and Construction Industry Improvement Act 2005

The BCII Act 2005 was the Government’s legislative response to the RC. This legislation established the ABCC as an independent statutory authority. The aim was to provide the Government with sufficient power to enforce law upon the construction industry and an entity (ABCC) to enact these powers. In this sense, the Act and the formation of the ABCC was a positive step to address one of the major frustrations of the BIT, its lack of authority to enforce law. The DEWR report in 2003 explained the reform process of the Act and the formation of the ABCC as follows:

The Australian Government will be implementing the key recommendations of the Royal Commission through the Building and Construction Industry Improvement Bill (building law). The proposed building law will:

- set up an autonomous independent body - headed by the Australian Building and Construction Commissioner to secure compliance with the new law;
- put in place a Federal Safety Commissioner to help improve the occupational health and safety (OHS) performance of the industry;
- give workers a genuine choice when it comes to bargaining;
- strengthen the rules about freedom of association to better deal with closed shops and discrimination;
- make sure that officials of employer organisations and unions are held accountable for their actions;
- provide sanctions for unlawful industrial action; and
- put in place a tough regime which deals with law breakers and substantially increases penalties (DEWR 2003, pp. 106-108).

The Act was a positive step forward in creating a legislative framework to be used to enforce law in the Construction Industry. This addresses a critical barrier to making the
industry comply with its social contract, that is, the regulator’s inability to enforce the law. The announcement of the Office of the ABCC created an authority with more powers than its predecessor, the BIT, and the purpose of enforcing the legislation.

The list of aims above also further highlights the problems identified by the RCR and the BIT reports. The key social contract expectations are fairness, freedom, and choice, with consequences for unlawful behaviour illustrated by the words ‘accountable’, ‘sanctions’, and ‘tough regime’. It is clear that the regulator no longer wants to be seen as a ‘toothless tiger’ and that those involved in unlawful behaviour should fear it. However, the process of holding unlawful individuals accountable for their actions was not clear.

4.7.2 Office of the Australian Building and Construction Commissioner (2005)

The Office of the ABCC (2005–2012) was an independent, statutory authority, whose role was to monitor and promote appropriate standards of conduct throughout the building and construction industry (FWBC 2012a). The ABCC provided education, investigated workplace complaints and enforced compliance with national workplace laws in the construction industry. The ABCC did this primarily by:

(a) monitoring and promoting appropriate standards of conduct by building industry participants,
(b) investigating suspected contraventions, by building industry participants,
(c) instituting, or intervening in, proceedings in accordance with this Act;
(d) providing assistance and advice to building industry participants regarding their rights and obligations under this Act and the Workplace Relations Act; (BCII Act 2005, s. 10).

The ABCC commenced operations on 1 October 2005. As outlined in the BCII Act 2005, section 3 (1), the principle role of the ABCC was to “ensure that building work is carried out fairly, efficiently and productively for the benefit of all building industry participants and for the benefit of the Australian economy as a whole”.

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The difference between the ABCC and its predecessor organisation, the BIT, is that new legislation was provided, that is, the BCII Act 2005, which gave it more law enforcement power. The nature of the powers given to the ABCC illustrated the nature of the legitimacy gap during its seven year life. For example, the ABCC could commence civil penalty proceedings against individuals and organisations who engaged in “unlawful industrial action” (BCII Act 2005, s.38). This term and its unlawful nature, is explained as follows:

- employees performing work in a manner that is different to how it is normally performed
- employees adopting a practise that restricts, limits or delays the performance of work
- a ban, limitation or restriction by employees on performing or accepting work
- a failure or refusal by employees to attend work or perform any work
- the lockout of employees from their employment by their employer (FWBC 2012f).

The ABCC was able to bring against building and construction industry participants who engaged in unlawful industrial action civil penalty proceedings resulting in a fine (BCII Act 2005, s. 38). This reveals that the primary focus of the ABCC was to address illegal industrial relations. Society’s expectations were that the Construction Industry would engage in satisfactory and legal industrial relations by not doing the types of things outlined in the above quote, for example, restrictions on performance of work.

However, the ABCC recognised that unlawful industrial relations were caused by issues associated with industry culture, that is, the way we do things around here. Utilising the insight gathered from previous reports by the regulator (see above), the first issue to be addressed was coercion. Coercion in the building and construction industry was considered unlawful. Coercion of persons includes:

(a) take or threaten to take any action; or
(b) refrain or threaten to refrain from taking any action;
with intent to coerce another person, or with intent to apply undue pressure to another person, to agree, or not to agree:

(c) to make, vary or terminate, or extend the nominal expiry date of, a building agreement under Division 2 or 3 of Part VIB of the Workplace Relations Act; (BCII Act 2005, s. 44).

In addressing unlawful behaviour such as coercion, the ABCC did more than try to prosecute. The first issue it addressed was wages and entitlements. It tried to empower workers by helping them understand their rights. The ABCC provided free information and advice on pay, conditions, and workplace rights and obligations to building and construction industry participants (FWBC 2012d). The ABCC investigated complaints relating to sham contracting, underpayments of wages and entitlements for workers in the building and construction industry (FWBC 2012d).

An example of unlawful work practices was sham contracting. A sham contract is where an employer deliberately misrepresents employment as an independent contracting arrangement, instead of engaging the worker as an employee (Fair Work Act 2009, s. 357). In some cases, this may result in the worker missing out on some entitlements or being pressured to become an independent contractor or being misled about the effect of changing their working arrangements (Office of ABCC 2011a, p.56). The ABCC acted as an advisor and advocate for workers who were unsure of their rights and vulnerable to unfair work practices such as sham contracting.

As the ABCC developed over time, it showed that it was prepared to tackle the issues underlying the construction industry’s social contract breach. On 19 November 2010, ABCC, Leigh Johns, announced that the ABCC would conduct an inquiry into sham contracting in the building and construction industry (FWBC 2012d). On 22 December 2010, Commissioner Cole released a discussion paper and called for written public submissions to the inquiry (FWBC 2012d). A total of 21 submissions were received.
from industry associations, subcontractors, the resources sector, academics and others (Office of ABCC 2011b, p. 5). In March and April 2011 the ABCC held a series of Roundtable events in Sydney, Melbourne, Brisbane, Canberra and Perth, to provide a forum for all industry participants to discuss the nature and extent of sham contracting (Office of ABCC 2011b, p. 73). On 29 November 2011, the ABCC released the Sham Contracting Inquiry Report 2011, which outlined ten recommendations aimed at eliminating sham contracting within the construction industry (Office of ABCC 2011b, pp. 93-107). This enquiry illustrates that the ABCC was willing to pursue unlawful behaviour on an industry-wide basis.

The ABCC also continued with its pledge to provide fairness to Wages and Entitlements. In March 2011 the ABCC assumed full responsibility for investigating complaints relating to wages and entitlements in the construction industry (FWBC 2012a). Prior to this a memorandum of understanding existed between the ABCC and the Fair Work Ombudsman (FWO) for such complaints to be handled by the FWO. The ABCC announced he would terminate this practice when he commenced his appointment on 11 October 2010 (FWBC 2012a).

The second issue it addressed was right of entry. One of the ways unlawful industrial relations was manifested was denying people access to work sites. In this way, unions could control the workplace and signal to all stakeholders that they were in charge of whether work could be conducted on any given day and by whom. This gave them extraordinary power over employers and employees. The ABCC addressed right of entry by overseeing laws regarding how and when a person could enter a building or construction worksite (Fair Work Act 2009). Union officials must hold a valid federal permit and provide at least 24 hours written notice to enter a building or construction worksite. The written notice period may not apply, if the reason for entry relates to an
occupational health and safety issue. (FWBC 2012f). This provided employers with power to deny union officials access to the workplace unless they had good cause and provided sufficient notice to allow employers to prepare.

The third issue the ABCC addressed was law enforcement. The prosecution strike-rate of the BIT was less than 1%; of 1,000 visits to construction sites, only six people were taken to court (BIT Report, 2004, p. 2). In order to be effective in this role, the ABCC was provided strong powers to investigate alleged misconduct and breaches of the law. Section 52 of the BCII Act 2005 provided the ABCC with the power to compel a person who had evidence relating to an investigation to answer questions, or provide information or produce documents. A person that fails to comply with a section 52 notice faced imprisonment for six months, or instead of, or in addition to imprisonment, the court may now impose 2000 penalty points for a natural person fine for breaches, and five times that for a body corporate convicted of an offence. This was provided for under subsection 4B(2) of the Crimes Act 1914.

The fourth issue it addressed was contracting, including tendering and procurement. A fundamental structural problem within the Construction Industry was the allocation of work contracts. Australia is a democratic capitalist society, which means that the Government and society tend to leave business to market forces. In other words, society trusts that business will use resources it allocates efficiently by choosing the best supplier of goods and services. In the case of the Construction Industry, market forces manifested in terms of contracts. The industry awards contracts at multiple levels. A prime contractor, that is a large construction company, may win a contract to build a housing estate, a hospital, school, bridge and so on. In performing this work, the prime contractor may seek the services of other companies, known as sub-contractors. The
process of awarding contracts to prime contractors and sub-contractors has been abused in the past and unlawful behaviour has resulted.

The ABCC addressed the problem of contracting with the National Code for the Australian building and construction industry. The National Code was established in 1997. However, the ABCC recognised its power to bridge the industry’s legitimacy gap and encourage compliance with the social contract. The Australian Government spends billions of dollars annually on construction projects to build schools, universities, hospitals, roads, and bridges. This represents a significant market opportunity for all construction companies. In order to be eligible for Australian Government funded construction work, businesses must be compliant with the National Code (FWBC 2012c). “The National Code and these Guidelines encourage co-operation, ethical behaviour, continuous improvement and best practice by clients and service providers in the construction industry” (Australian Procurement and Construction Council 1999, p. 5). In this way, the ABCC could encourage the cultural behaviour desired by society, that is the social contract, by providing a financial incentive to comply. Only by taking action to bridge the legitimacy gap could construction companies gain access to lucrative government contracts.

In summary, the ABCC made significant progress in addressing some of the underlying cultural work practice problems within the Construction Industry. It differed from earlier regulation because it was supported by specific legislation, the BCII Act, and a strategy aimed at empowering victims and isolating the bullies. By providing employers with an incentive to comply with the National Building Code accreditation to win government contracts, and empowering employees with wages and entitlements support and industrial relations laws to break down bullying, and support to police the industry,
the ABCC made significant progress towards bridging the legitimacy gap in the construction industry.

4.7.3 Fair Work Building and Construction (2010)

Justice Murray Wilcox’s report, ‘Transition to Fair Work Australia for the Building and Construction Industry’ (2009), made recommendations on the structure and powers of an organisation to replace the ABCC. This report was part of a range of measures designed to update the regulation of the construction industry, within the context of a broader changes to industrial relations policy and legislation.

The *Fair Work Act 2009* (C’wth) (FW Act 2009) replaced, from 1 July 2009, the Workplace Relations Act 1996. The FW Act 2009 is the cornerstone legislation for workplace relations laws in Australia (FWBC 2012b) and includes rules regarding:

- terms and conditions of employment
- rights and responsibilities of employees and employers
- compliance and enforcement rules (FW Act 2009, ss. 5-7)

The FW Act 2009 consolidates the government agencies that currently administer the workplace relations system into two new regulatory bodies: Fair Work Australia (FWA) and the FWO (FW Act 2009, s. 595 and s. 682).

The Australian Government introduced the BCII Amendment (Transition to Fair Work) Bill 2009 to parliament. The purpose of the bill was to establish the Office of the Fair Work Building Industry Inspectorate, which replaced the ABCC. The ABCC continued to operate until the BCII Act 2005 was amended. The ABCC was abolished on 31 May 2012, and was replaced on 1 June with the Fair Work Building and Construction (FWBC) as the building industry regulator (FWBC 2012b).
4.8 Current Regulation

The current state of regulation of the construction industry is examined from two perspectives. First, analysis of comments made by industrial relations lawyers about the formation of the FWBC Agency, and the legislative and policy changes and second, the agency’s web-site which explains its activities and services. In combination, this provides a summary of the current efforts to regulate the construction industry and the size and nature of the current legitimacy gap.

The key changes in the BCII Amendment (Transition to Fair Work) Bill 2011 were:

- The Bill abolishes the Office of the Australian Building and Construction Commissioner and establishes a new statutory agency, the Fair Work Building Industry Inspectorate. The Inspectorate will be a stand alone statutory agency.
- While the Bill retains the use of coercive powers by the Director of Inspectorate, it also imposes a number of safeguards.
- The use of coercive powers by the Director of the Inspectorate will be sunsetted in three years, not five years as previously proposed. A decision as to whether the powers will be extended will be made at that time.
- The role of “Independent Assessor” has been introduced with power to make determinations that the coercive powers be “switched off” in respect of particular projects on which “building work” commences after the commencement of the Bill.
- The provisions of the Fair Work Act will apply unchanged to workers in the building industry. Provisions within the Building and Construction Industry Improvement Act which dealt with industry-specific laws (such as unlawful industrial action, discrimination, coercion and unfair contracts) will be repealed.
- The Bill removes existing higher penalties for building industry participants for breaches of industrial law and broader circumstances under which industrial action attracts penalties.
- In order to ensure that all building industry participants are not subject to multiple proceedings, the Inspectorate will be prevented from prosecuting building workers when the parties have settled or discontinued matters (Young 2012, para. 3).

CDA of this evaluation of the legislative changes identifies that the explicit social contract expectations are that the construction industry comply with industry-specific laws, which are related to unlawful industrial action, discrimination, coercion and unfair contracts. The comments also refer to the ‘coercive powers’ and penalties, which are
evidence of expectation change in the legitimacy gap, whereby society expects stronger law enforcement of the industry.

Young (2012, para. 4) concludes that “much like the BCII, the Bill affects the rights and obligations of ‘building industry participants’”. This includes: building employers, building employees, building contractors and building associations (Young 2012, para. 4). The definition of “building work” as existed under the BCII Act is largely retained with one important difference. “The Bill now expressly excludes from the definition of ‘building work’ off-site pre-fabrication made to order components” (Young 2012, para. 5). This is intended to exclude manufacturing that takes place in off-site facilities separate from a building project (Young 2012, para. 5). This evaluation shows who is required to comply with the social contract being enforced by the legislation and the new inspectorate.

The FWBC Agency is headed by a Director, appointed by the Minister. The functions of the Director include, amongst other things:

- providing education, assistance and advice to building industry participants;
- monitoring compliance with designated building laws and the Building Code by building industry participants;
- investigating any act or practice by a building industry participant that may be contrary to a designated building law, a safety net contractual entitlement or the Building Code; and
- commencing proceedings in a court, or to make applications to Fair Work Australia, to enforce designated building laws and safety net contractual entitlements as they relate to building industry participants (Young 2012, para. 6).

This appears to be a more limited scope of activities compared with previous regulatory bodies, such as the ABCC. While the important themes of employee empowerment, compliance, investigation, and law enforcement are retained, it seems that the new regulatory body has more of a watchdog role rather than a change role. The regulatory agency role looks as if it is being wound down. However, law enforcement powers
remain. Inspectors, who are appointed by the Director of the Inspectorate, have the same powers as inspectors appointed under the FW Act 2009, to enter premises, inspect work, interview any person and require a person who has the custody, or access to a document to produce that document (Young 2012, para. 7). Young (2012) provide this summary advice for Construction Industry stakeholders:

Whilst the Bill introduces considerable changes to the BCII Act and in particular the range of matters considered unlawful as well as the nature of penalties that might be imposed, it would be unwise for any employer or union to become complacent.

Rather, there is a high likelihood that the Inspectorate will continue to actively monitor compliance with designated building laws, investigate any act or practice that may be contrary to a designated building law or a safety net contractual entitlement or ultimately commence proceedings in a court, or to make an application to Fair Work Australia.

Further, even though the use of the coercive powers has been curtailed, the Director retains considerable powers to obtain information, documents and answers to questions. We expect these powers to obtain information through means other than the exercise of the coercive powers will be utilised and for the presence of the Inspectorate on building sites to continue (paras.16-18).

The comments reveal that while the industry’s regulatory body appears to have been scaled down, it still has sufficient authority and TOR to have consequences for industry stakeholders who wish to risk breaching the social contract.

The FW Act 2009 seems to have made a significant difference to the industrial relations problems within the Construction Industry. Enterprise agreements made under the FW Act 2009 after 1 May 2012 must include a genuine dispute resolution process that provides for an independent third party, such as Fair Work Australia (FWA), to mediate a dispute (Young 2012, para. 15). An independent third party, such as FWA, must have the capacity to settle the dispute via a binding decision, if the dispute cannot be resolved (Young 2012, para. 15).
The current regulatory environment for the construction industry suggests a much tighter control of the social contract provided by legislation, policy, and regulatory agency activity. The Fair Work Building & Construction web-site has the following “pop-ups” to highlight the type of information it most wants to communicate to users of its site:

1. Learn more about your rights and responsibilities (empowerment)
2. How can FWBC help you? (support)
3. Find out how to win government work (compliance benefits)
4. Are you being paid correctly? (industrial relations and empowerment)
5. Stay-up-to-date (information diffusion) (FWBC 2012f, para. 2)

The menu under the web-site’s tab “Your Legal Rights and Responsibilities” contains these areas:

- Industrial Action
- Occupational Health and Safety
- Right of Entry for Permit Holders
- Union membership – your right to free choice
- Unlawful pressure and coercion prohibited (FWBC 2012e, para. 1)

4.9 The Industry Response to Regulation

Chapter 3 examined how the Construction industry gained legitimacy in the first place through its desirability. Organisations gain legitimacy by proactively seeking to persuade society that they deserve this status, and access to necessary resources (O’Donovan 2002). Gaining legitimacy involves similar strategies as when trying to repair legitimacy. The only real difference is that gaining is a proactive approach and repairing is a reactive approach. Repairing involves responding to a crisis. Lindblom (1994) recommends four strategies to gain or repair legitimacy (see section 2.3.3).

In developing understanding about the process of legitimisation in the construction industry, two approaches are adopted. First, it will examine what, if any, legitimisation
tactics were employed by the industry before and after the RC to maintain, gain or repair legitimacy. Second, it will examine the industry’s disclosures in order to identify the way it communicated its legitimisation tactics. Deegan (2009, p. 332) explains that there has been insufficient empirical research and theoretical development to connect specific legitimisation techniques with efforts to gain, maintain, or repair legitimacy. Lindblom’s recommendations are untested and it is not known whether they work or how to attain legitimacy. Disclosure is the only action known to work.

4.9.1 Industry Efforts to Repair Legitimacy

Evidence that the construction industry did not wish to repair its public image and seek to regain legitimacy status is provided in the previous sections. The evidence comes in two forms: the continued unlawful behaviour found by the BIT and the creation of various regulatory measures (for example, legislation) and authorities since the RC. There were clear signs that the union leaders actively sought to maintain unlawful behaviour. Indeed, rather than seek to regain legitimacy status, union leaders openly defied the Government and sought to challenge the laws imposed on them. The second BIT report cites the case of Craig Johnston, the former Victorian State Secretary of the AMWU, who was sentenced in 2004 following incidents in 2001 associated with an industrial dispute. The BIT report states “From his Victorian prison cell, Johnston subsequently sent a message to unionists to “continue to break these laws” urging them that “if the law is wrong, break it and break it again and force the Government to repeal it” (Hadgkiss 2005, p. 8). Further examples of civil disobedience were found on a website devoted to the Defend Craig Johnston movement, where Craig Johnston is quoted as saying: “The only way that the Workplace Relations Act will be brought down is if there is a full-on onslaught of civil disobedience and breaking the law with political and industrial action” (Hadgkiss 2005, p. 8). This illustrates how the union
movement did not do any of the four tactics suggested by Laughlin (1999) to repair legitimacy. They employed a new tactic, challenge social expectations by breaking the contract so often that society must agree that the expectations cannot be enforced.

There is considerable evidence in the second BIT report that some contractors tried to repair legitimacy by standing up to the unions. The contractors employed the communication tactic - explain how you are doing what society expects – by reporting efforts to confront the unions to the BIT. These actions were then communicated to the broader public by the BIT report. However, these actions did not work. The BIT report lists several tragic stories of contractors facing bankruptcy or substantial financial loss as a result of trying to stand up to the unions. Most accepted the unlawful behaviour as necessary if they were to survive, after trying to behave according to society expectations and it failed.

4.10 Chapter Summary

This chapter provided an historical narrative of regulation of the construction industry. It provides evidence of the nature of the legitimacy gap by establishing the social contract, that is, society’s expectations of the industry, and the social contract breach, that is, the behaviour considered unsatisfactory by the regulator. The narrative shows how the regulator introduced several regulatory bodies and further reviews of the industry in the period since 2003. In the period immediately after the RC, the industry appeared to ignore the regulator’s claim that there was a legitimacy gap and continued with its behaviour. However, there are signs that the industry is now moving towards compliance with the social contract.
The legal evaluation of the legislative and policy changes provided by Young (2012) and the FWBC web-site suggests that the construction industry has made significant progress towards breaching the legitimacy gap. While the existence of the FWBC Inspectorate and the legislation suggests that a legitimacy gap still exists or at least that deterrence is necessary to ensure the breach does not reappear, the regulatory environment appears to be gaining control of the industry.

Given the volume of data examined in this chapter including some historical context of industry regulation, the ABC Four Corners transcript, RC outcomes, DEWR Report, APC report, BIT Report, ABCC and FWBC, and brief reference to recent regulation; the chapter summary will discuss the findings against the relevant research questions posed in chapter two.

**Theme 1 – What Led to the Royal Commission (up to 2003)**

PIT explains why and how society intervenes in business activity. In this study, it is used to explain why the regulator, the Federal Government, felt it needed to take action to improve behaviour in the construction industry. It is also used to explain the types of regulation used by the Government and accounting bodies. A number of questions were posed in chapter 2 which may be answered by chapter 4. The first was question 2: Why did the Federal Government choose to conduct a RC into the construction industry?

In discussing the history of the regulation of the construction industry, there are two broad themes: economic and political forces. The economic forces were driven by uneven power within the construction industry’s stakeholders. This created social inequities between stakeholders. The political forces were driven by Government’s desire to restore equity and balance between stakeholders. Therefore, the first step in the
interpretive framework in this chapter is to code the document text in terms of whether
the text refers to economic or political forces. The themes are:

1. Economic: activities creating social inequities between stakeholders.
2. Political: government frustration with perceived inequities between stakeholders.

An investigation by the EA in 2001, which was prior to the RC in 2003, criticised law
enforcement agencies for failing to act on problems in the construction industry
(Hamberger 2001). The chapter described evidence of the socio-political power
inequities within the industry at the time. Clearly many people were unhappy with these
inequities but felt intimidated and unempowered to act, and the inability of the
authorities to enforce appropriate behaviour added to the feelings of powerlessness.

The RCR was critical of the construction industry trade unions for creating a culture of
intimidation. The ABC Four Corners (Neighbour 2001) investigation into trade unions
highlighted the type of behaviour that society decided was a breach of the social
contract. The chapter’s analysis reveals dominant themes of corruption and political
power struggles between union leaders. There were allegations against enemies such as
poor leadership, lying, hatred, greed, criminal activity, mismanaged funds, violence, and
threatening or intimidating contractors and politicians.

The Federal Government’s decision to conduct a RC into the construction industry may
be explained as a DSS. The social contract breach was not something that was hidden
and suddenly emerged. The catalyst was probably the Four Corners media investigation,
which highlighted for many people the seriousness of the cultural problems.

The analysis of the PM’s statement in 2001 announcing the RC reveals illegality,
inequity, and lack of accountability as important themes. The government
communicated to the industry that it would not tolerate this behaviour any further and
that it wanted to introduce fairness and accountability to the industry, particularly in terms of industrial relations and funds management and disclosure. Accounting is implicated in terms of the latter point.

The second question addressed by chapter 4 is question 5: What criteria does society set in adjudging legitimate status? How can it be known if the industry is legitimate?

LT explains how organisations seek to be perceived as ‘legitimate’ by their society in return for resources necessary for their survival (for example, see Dowling & Pfeffer 1975; O’Donovan 2002). The chapter’s findings answer this question in two ways. First, it establishes undesirable behavior. In doing so, it outlines the type of behavior society will no longer tolerate. The PM’s statement (2001) announcing the RC revealed connections of illegality and inequity. It identifies union leaders being villains and workers and employers as victims. The main issue in terms of implicit expectations was financial disclosure, where the language used by the PM’s statement suggests connections of unaccountability. It uses strong words to describe the significance of this behaviour, failure, and allocate identities as management doing negotiations. It does not identify accountants specifically. However, financial disclosure is an activity that involves accountants, so they are implicated.

The analysis distinguishes between pragmatic and moral motives for misbehaviour. Pragmatic motives are derived from self-interest, for example, profit (Deegan 2009). The main issue here was corruption. Moral motives involve responsibility, desire to do the right thing, for example, good corporate citizenship (Deegan 2009), the principle concern being appropriate use of funds. The identities surrounded self-interest, and while union leaders were implicated, the language is cautious, using the word
‘inappropriate’. Deegan (2009) identifies a third motive, cognition, which is shared mental models, which involves the cultural problems identified by the RCR in 2003.

The third question addressed by chapter 4 is question 7: How did the construction industry perceive its role as corporate citizens? The chapter findings revealed that the construction industry was aware that its behavior was considered unsatisfactory by society but there was a sense of apathy about this reputation. The ABC Four Corners investigation in 2001 showed that union leaders would not apologize for their behavior, suggesting they had no intention of wanting to repair the legitimisation gap. Further, when the RC announced its findings, they were uncontested in the sense that they were unchallenged by industry stakeholders. The construction industry recognised that it was perceived as poor corporate citizens, who had breached their social contract, with a sense of apathy, helplessness, and acceptance.

While the RC was highly critical of the unions, Commissioner Cole was sympathetic towards other stakeholders suggesting they were often victims of intimidation. People knew there would be consequences if they did not cooperate with unlawful behaviour. Perhaps most importantly for this study and the role of accountants, Commissioner Cole was sympathetic towards the pressure individuals were under to act in the best interests of their stakeholders. For managers, their jobs required them to protect the interests of owners by ensuring the firm was profitable. The analysis suggested managers may have found it impossible to refuse to engage in improper practices. Accountants may have found themselves in the same situation.

The fourth question addressed by chapter 4 is question 8: How did society perceive the industry’s role as corporate citizens? The chapter found that construction industry stakeholders do not abide by the law. The legitimacy gap, therefore, is the degree of
unlawfulness, that is, the extent to which the industry does not abide by the law. Commissioner Cole laid the blame for unlawful behaviour with industrial relations. He argued that this situation had emerged because industry stakeholders believed that industrial relations sits outside the law. Commissioner Cole identified the socio-political power inequities which had created the industry’s culture. The basis of the structural problems inherent in the industry’s stakeholder relationships were that those with power were the winners. Power was obtained by industrial action. The inequities in the stakeholder relationships were driven by intense competition which created small profit margins. As a result a short term focus prevailed which meant that employers, both head contractors and subcontractors, had to submit to those with the power to decrease their profitability, that is the unions.

The fifth question addressed by chapter 4 is Question 9: What was the nature of the social contract between the construction industry and Australian society? What did society expect from this industry? Commissioner Cole uses the phrase ‘departs from the standards’ to state that the industry does not behave the way the rest of Australian industry behaves. The use of the word standards indicates an expectation, a level of behaviour, that is, a social contract. The legitimacy gap explains the ‘why’, in terms of the reasons for the gap occurring. Society’s expectations of the construction industry may be understood from two perspectives:

1. Explicit: legal requirements, for example, legislation or activity required by law

2. Implicit: areas outside the law but still deemed desirable by society

The legal expectation was that industry stakeholders need to change their cultural behaviours to abide by the law and give all individuals their freedom to act in accordance with the law without unfair workplace pressure. The implicit requirements
in the social contract are those that are desirable but not enforceable by law. Implicit requirements are more related to moral motives, for example a sense of doing the right thing. Commissioner Cole’s recommendations include the implicit requirement of attitudinal change. Attitudes are difficult to monitor and perhaps impossible to police. However, attitudinal change was essential if cultural change was to be successful. The following table uses content

In summary, the RC outlines the social contract in explicit terms by requiring industry stakeholders to follow appropriate legislation as law (statute), being aware of the consequences of illegal behaviour (law enforcement), and only dealing with union officials with proper accreditation and behaviours. Implicit expectations involved cultural change essentially related to fair work practice and employee empowerment and freedom. These themes would carry on throughout the next decade of regulation of the industry.

**Theme 2 – Post Royal Commission (after 2003)**

Non-compliance with the social contract can also have a negative impact on the organisation or industry’s market reputation or image (Deegan et al. 2000). The sixth question addressed by chapter 4 is question 13: What measures of legitimacy were imposed by the RC on the construction industry? The chapter showed that explicit expectations required industry stakeholders to follow appropriate legislation as law (statute), being aware of the consequences of illegal behaviour (law enforcement), while implicit expectations involved cultural change essentially related to fair work practice and employee empowerment and freedom. The measures of legitimacy were also defined by the social contract breach because Commissioner Cole specified the inappropriate behaviour society expected the construction industry to change: bullying,
inadequate financial management, disempowerment, conflicting relationships, unfair workplace practices, industrial disputation, and unsatisfactory law enforcement.
CHAPTER 5: ACCOUNTING AS SOCIAL PRACTICE - RELATIONSHIPS

5.1 Introduction

The purpose of this chapter is to reconstruct the social reality of how accountants work within the construction industry from a ST perspective. The aim is to examine the social system that accountants work within this industry. Three ST constructs are used as the lens for this examination: relationships, impact, and expectations (Gray, Owens & Adams 1996, p. 45). This chapter will examine the first construct, relationship, and chapter 6 will look at the two remaining constructs, impact and expectations.

These constructs help us explore the social systems within the construction industry. From an ethical perspective, it is argued that all stakeholders should be treated equally and that the (economic) power of various groups should not allow them to have differential influence over the firm (Deegan 2009), whereas, the managerial perspective argues that management will be likely to respond to the expectations of particular (typically powerful) stakeholders (Gray, Owens & Adams 1996). The analysis will examine whether social practice in the construction industry was ethical or managerial. The outcome of this analysis is the social contracts which are ‘negotiated’ with different stakeholder groups (Deegan 2009).

In this chapter, the relationships constructs will be used to discuss the key themes which emerged from analysis of the behaviours within the construction industry. More
specifically, behaviours associated with the activities mentioned by the RC which may have involved accounting practice: (1) tax evasion, (2) underpayment of employee entitlements, (3) non-compliance with payroll tax, (4) creation of phoenix companies, (5) making of and receipt of inappropriate payments, (6) absence of adequate security of payments for sub-contractors, and (7) profit manipulation. These activities involved a range of social behaviours. These are analysed using the relationships construct.

The role of accounting exists within a complex social system. The aim is to examine the social interactions between accountants and other industry stakeholders when accountants were potentially involved in the seven unlawful activities. It is important to note that this thesis does not seek to explicate exactly what happened in the construction industry at the time of the RC. The aim is to examine the role of accounting; not the role or performance of individual accountants. Therefore, this section explores how accountants might have interacted with others based on the evidence available from the RCR.

The three ST constructs, relationships, impact and expectations (Gray, Owens & Adams 1996, p. 45), will be applied as follows. First, SNA will be used to examine the use of power within the social networks within the construction industry. This is relationships. Second, whether the people making decisions about tax evasion were willing to listen to accountants and adjust their behaviour accordingly. This is impact. Third, what did these people expect of accountants when their company was doing tax evasion. This is expectations. This chapter will examine the first area, relationships.
Table 5.1: Themes by Unlawful Activity

<table>
<thead>
<tr>
<th>Activity</th>
<th>Theme</th>
<th>Construct</th>
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<tbody>
<tr>
<td>Taxation</td>
<td>1. Cash payments</td>
<td>Relationships</td>
</tr>
<tr>
<td></td>
<td>2. Fake labour hire</td>
<td>Expectations</td>
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<td></td>
<td>3. Unions threatening to expose employers</td>
<td>Impact</td>
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<td></td>
<td>4. Pyramid Subcontracting</td>
<td>Expectations</td>
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<tr>
<td></td>
<td>5. Use of illegal workers</td>
<td>Impact</td>
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<tr>
<td></td>
<td>6. Fraudulent claims for Goods and Services Tax (GST) Input Tax Credits</td>
<td>Relationships</td>
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<td></td>
<td>7. Large companies</td>
<td>Expectations</td>
</tr>
<tr>
<td>Employee Entitlements</td>
<td>1. Reduce costs</td>
<td>Relationships</td>
</tr>
<tr>
<td></td>
<td>2. Treating employees as sub-contractors</td>
<td>Expectations</td>
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<tr>
<td></td>
<td>3. Failing to pay employees benefits such as superannuation</td>
<td>Impact</td>
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<td></td>
<td>4. Insolvency to avoid payment</td>
<td>Expectations</td>
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<tr>
<td>Payroll Tax</td>
<td>1. Using employees as sub-contractors</td>
<td>Expectations</td>
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<td></td>
<td>2. Grouping of companies</td>
<td>Expectations</td>
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<td></td>
<td>3. Non-registration</td>
<td>Expectations</td>
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<td></td>
<td>4. Lodgment of returns</td>
<td>Expectations</td>
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<td></td>
<td>5. Incorrectly completing returns</td>
<td>Expectations</td>
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<tr>
<td>Phoenix Companies</td>
<td>1. Avoiding payroll tax</td>
<td>Expectations</td>
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<td></td>
<td>2. Acting as company directors while bankrupt</td>
<td>Expectations</td>
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<td></td>
<td>3. Establishing groups of companies to avoid liabilities</td>
<td>Expectations</td>
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<tr>
<td>Inappropriate Payments</td>
<td>1. Buying industrial peace</td>
<td>Impact</td>
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<td></td>
<td>2. Including inappropriate payments in industrial agreements</td>
<td>Impact</td>
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<td></td>
<td>3. Delaying payments to employees, for example wage increases or other entitlements</td>
<td>Impact</td>
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<td></td>
<td>4. Unions demanding payment during industrial action</td>
<td>Impact</td>
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<td></td>
<td>5. Unions exerting pressure to ensure employee entitlements are paid</td>
<td>Impact</td>
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<tr>
<td>Security of Payments</td>
<td>1. Misleading financial viability</td>
<td>Relationships</td>
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<td></td>
<td>2. Lack of capability to assess financial health</td>
<td>Relationships</td>
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<td></td>
<td>3. Contracting system</td>
<td>Relationships</td>
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<td>4. Lack of regulation</td>
<td>Relationships</td>
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<td>5. Legitimate business failure</td>
<td>Expectations</td>
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<tr>
<td>Profit Manipulation</td>
<td>1. Self-interest at the expense of others</td>
<td>Impact</td>
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<td></td>
<td>2. Unwillingness or inability to change behaviours</td>
<td>Relationships</td>
</tr>
<tr>
<td></td>
<td>3. Management of costs</td>
<td>Expectations</td>
</tr>
<tr>
<td></td>
<td>4. Buying work</td>
<td>Relationships</td>
</tr>
</tbody>
</table>

The themes are used to theorize about the nature of the unlawful activity (see grounded theory explanation in section 5.1).
They are used to further illustrate the nature of the unlawful behaviours and allow generalizations about what companies do when they engage in unlawful behaviour associated with for example, employee entitlements, for example, such as treating employees as sub-contractors. Further research, perhaps in other industries, or in construction in other countries, could look at whether this also occurs. It allows measurement constructs to emerge. For example, listing employee entitlements as unlawful behaviour does not equate to a concept that is easily measured by other studies. Nor does the detail of the historical narrative in this thesis because the context is specific, which would make it challenging to compare case situations with others. The themes provide a middle ground, by enabling measurable constructs to be used in further research. For example, it is possible to measure whether other organisations or industries treat employees as sub-contractors, and then infer whether employee entitlements is conducted unlawfully.

5.2 Relationships

5.2.1 Introduction

The relationships between the construction industry’s stakeholders are analysed using SNA theory. SNA is a technique for understanding the nature of connections between people, to visualize them, and to analyse them for tactical and strategic change (Anklam 2002). Borgatti and Foster (2003) proposed two dimensions of SNA research which are helpful in this analysis of construction industry relationships: explanatory mechanisms, which refers to how network ties are seen to function; and explanatory goals which refers to network outcomes. Explanatory mechanisms include patterns of interconnection. This will be used to identify the nature of interaction between stakeholder groups in terms of network quality (depth of contact) and network structure.
(number of contacts and frequency of contact) (for example, Stone 2001). Explanatory goals include homogeneity in actor attitudes, beliefs and practices, as a function of social ties (Borgatti & Foster 2003). This framework is used to further enhance our understanding on the use of power within stakeholders’ relationships in the construction industry because it helps identify changes in behaviour as a result of those interactions.

5.2.2 Social Interaction

5.2.2.1 Introduction

An examination of which stakeholder groups interacted, how often, and for what purpose is conducted. The SNA theory construct, density, is used to examine the interconnectedness of social networks; individuals with high density scores are connected with more than one social network (Stone 2001; Anklam 2005). Density is a positive factor in social networks because it measures frequency of interaction. The more density, the more opportunity to build and maintain relationships, which results in increased communication, trust, and social dependency. In contrast, low density indicates separateness, which results in isolation, mistrust, and conflict. This analysis is to identify the overall network density, that is, the connectivity between all stakeholder groups. It will also highlight differences in density amongst stakeholders, that is, which groups were well connected and which were not.

In terms of the social networks within the construction industry, there are two main social systems: internal stakeholders and external stakeholders. In examining the relationships between these stakeholders, the involvement of accounting practice will be explored when considering the interaction associated with the seven unlawful activities identified by the RC.
5.2.2.2 Overall Social Network Density

Overall, the construction industry’s social network had moderate density. The industry was dominated by its complex contracting system which involved layers of businesses from head contractors (large companies) to contractors (medium sized companies), to sub-contractors (small companies). This required high levels of interaction between owners/managers of these companies when tendering for projects and then in completing the project, if successful. The other dominant player was the trade unions. The unions were at the centre of industrial relations problems within the industry and would frequently interact with owners/managers. Interaction between other stakeholders was much less frequent, which is why the industry’s overall density is described as only moderate. The interaction between stakeholder groups is now examined to identify the density of each group. Internal stakeholders are examined first, followed by external stakeholders.

5.2.2.3 Owners/Managers Network Density

Owners/managers interacted regularly with all other industry stakeholders. This interaction varied in frequency and volume, that is, how many times these individuals interacted with other stakeholder groups and the size of their networks. However, owners/managers had a high density within the construction industry’s social networks overall. In many respects, this level of interaction was a positive factor in the industry’s social networks. As outlined above high density should generate more opportunity to build and maintain relationships; resulting in increased communication, trust, and social dependency. This was the case with owners/managers and most other stakeholders in the construction industry. However, it was not the case in the interaction between
owners/managers and unions, where the characteristics of low density emerged, that is, mistrust and conflict.

In their interactions with other stakeholders, owners/managers played several roles. With staff, the role was negotiator. With small profit margins, owners/managers were often under pressure to cut costs. This emerged in discussions with staff about employee entitlements. The industry sought procedural justice in terms of employee entitlements, particularly in terms of legitimate performance (that is, bonus). Owners/managers sought to “gain a competitive advantage by being innovative in the way they remunerated their employees” (Cole 2003, vol. 3, p. 208). This would have improved employee recruitment and retention if owners/managers could have paid more for higher performing employees. However, pressure from unions meant that employers could not overpay employees as a reward for superior performance.

The RC found evidence of non-uniformity in the pattern agreements, which were a type of enterprise bargaining agreement (EBA), “from the non-residential building, road and bridge construction, and earthmoving sectors of the construction industry” (Cole 2003, vol. 5, p. 267). The pattern agreements were particularly interesting because they were non-union agreements that were intended to reflect what employers were willing to give employees in terms of fair distributive justice for employee entitlements, particularly focusing on aligning employee expectations with feasible employee entitlements. Analysis of these pattern agreements provided positive and negative reports on employers’ adoption of regulatory requirements. On the positive side, all three sectors “had identical provisions relating to leave entitlements, termination and retrenchment procedures, & OHS policies” (Cole 2003, vol. 5, p. 267). The RC felt that this may have been a legacy from the award or awareness of the need to follow statutory requirements (such as in the case of Equal Employment Opportunity [EEO] provisions).
This finding suggests that employers were at least aware that they needed uniformity in terms of employee entitlements. However, they found ways to work outside this pattern agreement. On the negative side, the pattern bargaining differed across these three industry sectors in “the term of the agreement and the wage increases provided” (Cole 2003, vol. 5, p. 267).

With regulators, the role of owner/managers was avoidance. The RC identified widespread unlawful behaviour by the industry. For many owner/managers, the thinking was that everyone else was doing it and the aim was not to get caught. An example was phoenix company activity, which mainly involved directors of companies, that is the owners or managers, who sought to avoid paying tax and other liabilities. The practice appeared widespread and may be described as normal industry behaviour. While the RC was critical of individuals who engaged in this activity, Commissioner Cole focused mainly on the failure of the regulatory system to police this activity. He inferred that individuals who engaged in phoenix activity were opportunistic and were only taking advantage of weaknesses in the regulatory system.

The RC almost apologised for employers in terms of them engaging in inappropriate behaviour associated with profit reporting. The inference was that contractors were under so much pressure that they had no choice but to manipulate profits. An employer group, the MBA, submitted to the RC that contractors who wanted to behave appropriately knew that this behaviour would not be recognised by customers. The MBA stated that its public “position on taxation compliance is based on fair and economically-based competition” (Cole 2003, vol. 9, p. 68). The MBA defended its members by stating that “in an industry where profit margins are traditionally tight, the practice of tax evasion places legitimate businesses at a significant competitive disadvantage when bidding for work against those which do not comply” (Cole 2003,
The MBA placed the blame firmly with customers by arguing that it is “unfortunate that some clients choose to turn a blind eye when accepting quotations for work to the fact that they can only be so significantly under-priced compared to others because of tax noncompliance practices” (Cole 2003, vol. 9, p. 68). In other words, customers should be aware that companies tendering at very low prices would have been engaging in inappropriate behaviour, and therefore, they should have not accept tenders from these unscrupulous companies. However, the reality is that customers will often choose the lowest priced tenderer, as it serves their self-interest to save money themselves.

With other construction companies, the role of owner/managers was competitor. The complex nature of the contractor system in the construction industry meant that companies could be both competitors and allies. On occasions, companies would work together to win a construction project and then complete the project. This would happen because head contractors often outsourced work to other contractors (medium sized companies) or sub-contractors (small companies). However, most construction companies saw other companies as competitors. Due to the small profit margins in the industry, competition was fierce. The outcomes emerged in activities such as employee entitlements.

Owners/managers of construction companies focused on distributive justice in terms of employee entitlements but from a different perspective compared with other internal and external stakeholders. Owners/managers sought uniformity in employee entitlements across the industry. Their objective was equity but only if their organisation could benefit. They wanted to reward employees for their loyalty with equitable employee entitlements. However, the level of reciprocity was determined by industry competition. The RC found that the “cost of an increase in employee
entitlements could be automatically passed up the contractual chain”, if construction companies “know that their competitors must bear similar costs” (Cole 2003, vol. 3, p. 208). In other words, employers would be happy to pay employees their full employee entitlements because they could simply pass this cost onto their customers by increasing the price of construction projects. However, the small profit margins in the construction industry meant that companies risked losing projects and going out of business if they raised prices. Therefore, companies under pressure would try to avoid expenses like employee entitlements rather than risk losing work. Unless all companies agreed to pay full employee entitlements and raise their prices, some companies would compete on price by avoiding employee entitlements.

The complex relationships between construction companies allowed unlawful behaviours to occur. Construction companies engaged in payroll tax noncompliance to various degrees. The degree to which companies engaged in this activity was largely influenced by their size. Smaller companies were more likely to try to avoid the threshold figure.

Tax avoidance and tax evasion was estimated to cost the Australian Government revenue of about $3 billion a year as long ago as 1985 (Potas 1993, p. 1). There is an important distinction between tax avoidance and tax evasion. Tax avoidance is legal, in the sense that any company or individual may seek legitimate methods to reduce their tax liability. However, tax evasion is against the law, and involves the “illegal non-payment of taxes either by under-declaring income or over-declaring deductions or exemptions” (Potas 1993, p. 2).

Tax evasion is generally known as “white collar crime”, because “it is an offence committed by people of high social status, the owners and managers, in the course of
their occupation” (Potas 1993, p.1). Yet it is not restricted to rich people and can be
undertaken by “anyone who has an income and has an obligation to pay tax” (Potas
1993, p. 1). Tax evasion and fraud was apparently quite widespread across many sectors
of Australian industry in the years leading up to the RC. The ATO conducted an audit of
Australia’s top 100 companies in the period 1988-1993, and while only half of these
audits were completed, tax adjustments of more than $1 billion were required (Potas
1993, p. 1).

Firms and individuals “engage in fraudulent behaviour in direct proportion to the
potential gain” (Potas 1993, p. 2). Most people would “naturally prefer to not pay more
tax than they are obligated to pay, and there are always some people who will try to
cheat the system” (Potas 1993, p. 2). Some areas where tax evasion has been practiced
include: “trust shipping (involving the exploitation of the revenue/capital dichotomy),
investing in loss companies, profit shifting, income splitting, gift schemes, exploitation
of trusts and superannuation schemes” (Potas 1993, p. 2). In terms of this study,
questions emerge in terms of whether construction firms would engage in these tax
evasion activities and, if so, what role would accountants have in these activities.

The following case studies illustrate how noncompliance occurred. The first case was an
example of a mid-sized company which primarily engaged in grouping. The second
case was an example of a smaller company which suffered at the hands of larger
companies.

The following extract provides a case study on Emerson Industries from the RCR. It is
used to analyse in more detail the nature of payroll tax evasion in the construction
industry.
In a submission from David Hicks on 18 November 2002, through his solicitor Mr Mark Douglass, Hicks indicated that if the company searches he had undertaken on 23 January 2001 had disclosed the correct information about the status of each company, then he would have conducted further enquiries into the Emerson Group, including making a determination on the capacity of Harkin to be a company director.

Emerson Industries was awarded the Multiplex NSW contract on 19 February 2001, because it had offered the most competitive price. It commenced work on site that month. At that point the payroll tax debt owed by ACN 071 413 191 Pty Ltd to the NSW Office of State Revenue (OSR) remained unpaid. Between January and March 2001 Harkin provided Multiplex NSW with a number of receipts and other documents. An examination of these documents shows, however, that they did not all relate to Emerson Industries. Some of these documents related to ACN 065 040 173 Pty Ltd and others related, or appeared to relate, to ACN 088 440 304 Pty Ltd (formerly Emerson Services). Set out below is a list of the material provided and the company to which it related:

- ATO – Australian Post Office Taxation Receipts for 1 March and 2 March 2001 (company unspecified).
- NSW OSR – ACN 065 040 173 Pty Ltd – payroll tax account for January 2001 was issued to ACN 065 040 173 Pty Ltd but the cheque in payment was drawn on the account of Emerson Industries.
- Enterprise Bargaining Agreement between ‘Emerson Services Pty Ltd & Employees and The Construction, Forestry, Mining and Energy Union, Construction & General Division, NSW Branch, 1999-2002’, dated 14 April 2000 in relation to ACN 088 440 304 Pty Ltd.
- Coverforce Top-up Accident Scheme paid by Emerson Services (ACN 088 440 304 Pty Ltd) on behalf of employees in relation to accident cover and top-up insurance.
- Construction & Building Unions Superannuation Fund (Cbus) paid by Emerson Services (ACN 088 440 304 Pty Ltd) on behalf of employees (Cole 2003, vol. 8, p. 175).

In September 2001 the CFMEU gave Harkin a statement of moneys that had been paid to the ACN 065 040 173 Pty Ltd employees. On this statement, tax was deducted from the gross payments and there was a note at the bottom of the statement stating that Harkin and his wife were liable for the tax payment. Harkin presented this statement to the liquidator of ACN 065 040 173 Pty Ltd (formerly Emerson Services). On 24 September 2001 the Supreme Court of New South Wales ordered the winding-up of ACN 065 040 173 Pty Ltd, and appointed Mr Anthony Milton Sims, chartered accountant and partner, Sims Lockwood, as liquidator. The statement of the director, Liberina Harkin, disclosed unsecured creditors of $2.5 million, including $1.69 million to the ATO, $266 093 to the NSW OSR for payroll tax, $382 935 in workers compensation premiums, more than $108 000 in unpaid superannuation contributions and $46 448 in unpaid redundancy contributions (Cole 2003, vol. 8, p. 185).
The extract provides several findings. First, the phrase “status of each company” suggests a problem with grouping. In other words, the Emerson Group may have been trying to evade payroll tax thresholds by splitting its business activities into different companies. The testimony of Mr Hicks that if he had known the extent of grouping by Emerson then he would not have awarded them the construction contract is particularly interesting. It suggests how difficult it was for customers, in this case the head contractor Multiplex NSW, to untangle the complex contracting arrangements in the construction industry, and the lengths some unscrupulous individuals went to in order to avoid paying tax. Second, the list of documents provided by Mr Harkin to Multiplex NSW showed that the head contractor was trying to do the right thing and to examine its contractor’s (that is, Emerson Group) lawfulness. This suggests that the bigger construction companies tried to follow lawful behaviour, whereas the mid-sized companies, like Emerson Group, and smaller companies were more likely to engage in noncompliance.

A third finding, the point about “moneys that had been paid to the ACN 065 040 173 Pty Ltd employees” and that Mr Harkin and his wife were “liable for the tax payment”, reveals how payroll tax evasion occurred by grouping activities. It seems that Mr Harkin was deducting tax from the gross payments of employees in at least one of his group of companies, and withholding these funds with the intention of later paying them to the taxation authorities. However, as the latter data indicates, when Mr Harkin’s company failed and went into liquidation he owed a large amount to the authorities, including $266 093 to the NSW OSR for payroll tax. This implies that Mr Harking withheld funds from employees for purposes other than to pay tax.

This case raises interesting issues about the role of the regulator in payroll tax evasion. In this case, the construction project was funded by the New South Wales State
Government. It was the refurbishment of the Campbelltown Hospital, which was funded by the Government. At the time of awarding the Emerson Group a contract to work on this project, 19 February 2001, “the New South Wales Government did not have a system enabling it to ascertain that a company being paid for work on a major public hospital project was part of a group which owed it substantial sums in payroll tax” (Cole 2003, vol. 8, p. 189). Commissioner Cole found an “incongruity where Government Code Implementation Guidelines required that contractors and subcontractors should ensure that their workers are appropriately engaged and remunerated and that the appropriate taxation requirements are complied with” (Cole 2003, vol. 8, p. 190). However, “the government itself does not act on information possessed by its revenue arm that another company associated with the principal of a significant subcontractor owes it a large sum in payroll tax” (Cole 2003, vol. 8, p. 190). In other words, the government requires compliance, but does not use its own information sources to check compliance. This highlights the root cause of the problem with payroll tax, it is a self-assessment which places responsibility with the company to do the right thing. This system depends on the goodwill and lawful behaviour of employers. As a result, it creates opportunities where from December 1999 a company associated with Mr Harkin owned the NSW OSR a large sum in unpaid payroll tax, but he was still awarded a large government contract in 2001.

The case poses questions about the responsiveness of the government to information about payroll tax noncompliance. The following extract shows the lengths the unions went to in order to tell the government that the Emerson Group were engaging in payroll tax noncompliance:

On 9 August 2001 Mr Ferguson forwarded to the Hon. Morris Iemma, New South Wales Minister for Public Works and Services, a copy of a letter he had sent to the Labour Council of NSW, about the extent of non-compliance with
payroll tax in the construction industry. Ferguson cited the case of Emerson [Industries] and wrote that Harkin: ‘has been associated with numerous failed companies that have left behind millions of dollars on each occasion in unpaid group tax, workers compensation premiums and payroll taxes. Equally, millions of dollars have been left unpaid to small business for work undertaken.’ Ferguson sent another letter to the Minister on 15 August 2001 about Emerson Industries and the Campbeltown Hospital project, seeking an urgent investigation and seeking the introduction of measures to ensure subcontractors engaged by principal contractors working for the Government comply with their award and statutory obligations (Cole 2003, vol. 8, p. 183).

On 24 September 2001, the Supreme Court of New South Wales ordered the winding-up of one of the Emerson Group of companies. Therefore, the unions’ representations to the Minister had their desired effect and the Government finally investigated Mr Harkins’s business activities. Mr Harkin would have employed an accountant(s) in his business activities. His activities were at least large enough to accrue $266 093 in unpaid payroll tax. At a threshold rate of 5.45%, this suggests he had a total wages bill of at least $5 million. A company of this size would have needed an accountant(s). This leads to the question, what role would Mr Harkin’s accountants have played in his business activities? Certainly, the Emerson Group was involved in grouping and in other activities associated with seeking exemptions from payroll tax. However, these activities would have probably have been done by the owners/managers, that is, Mr Harkin on his own without the input of accountants.

5.2.2.4 Human Resource Management Network Density

HRM staff would have been involved in interaction between owners/managers and unions. Industrial relations matters usually involve HRM staff. If union officials were coercing employers with an objective to achieve industrial relations changes, such as sign an EBA or improve worker conditions, then HRM staff should have been involved in discussions. This is particularly the case in larger construction companies. The role would have been to offer owners/managers policy advice to ensure that construction
companies followed appropriate legislation and other lawful activity involving staff (for example, employee entitlements). However, the RC found evidence that human resource management staff sometimes stepped outside the boundaries of policy advice. A case study about Bovis Lend Lease Pty Ltd, a large construction company, illustrates how HRM staff may have been involved. The following extract summarises the case:

Mr Eric Hensley is the Employee Relations Manager for Bovis Lend Lease Pty Ltd (Bovis), a position he has held since mid-1996. The notion that Bovis would pay $10,000 to the union picnic fund, and $10,000 to a memorial wall fund to ‘recognise the assistance’ of the CFMEU is nonsense. The moneys were paid to fund Bracic’s employment by the CFMEU, as Hensley said. I reject Ferguson’s evidence, both in his statement, and orally. It was internally inconsistent, and unreliable. Bovis paid $20,000 to the CFMEU in accordance with the agreement. On 19 June 2000 Bovis received two tax invoices from the CFMEU: one invoice itemised a $10,000 payment to the ‘Memorial Wall Fund’; the other itemised a $10,000 payment for ‘CFMEU Annual Picnic Sponsorship’. Under examination, Hensley conceded that the invoices were misleading and that he had done nothing to have them corrected. The next day, 20 June 2000, Bracic resigned. On about 29 June 2000, Bracic was employed by the CFMEU as an organiser, effective from 3 July 2000. His gross salary was $41,927.60. The evidence in relation to this incident discloses the use of industrial pressure by Ferguson and the CFMEU aimed at forcing Bovis to re-employ a worker who had repeatedly shown contempt for his employer and a disinclination to do any of the work for which he had been employed. (Cole 2003, vol. 13, pp. 239-248).

This case implicates both HRM staff and Bovis accounting staff. The HRM staff, represented by Hensley, authorised invoices which he conceded were misleading. Accounting staff would have processed these tax invoices.

5.2.2.5 Project Managers Network Density

Project managers play an important role in construction companies. They manage all aspects of a building project often as a turnkey task, from design to hand over to the customer. This includes managing operations and costs, as well as subcontractors. The following extract from a case described in the RCR illustrates the role of project managers working for a large construction company.
Mr Adrian Powell is a Project Manager employed by Westfield Design & Construction Pty Ltd [a large construction company]. As Project Manager, he has overall responsibility for the day to day running of the project he is employed to manage. A number of site-based personnel report to him and, in turn, he reports to a General Manager at Westfield Design & Construction Pty Ltd in Sydney. Powell was responsible for project management at Westfield shopping centres at both Airport West and Fountain Gate. Westfield Design & Construction Pty Ltd (Cole 2003, vol. 16, p. 273).

The extract illustrates a typical project manager role. The phrase owners/managers incorporate all levels of supervision within an organisation. In a company as large as the Westfield Group, Mr Powell’s manager is most likely someone at levels below that of the group owners. Mr Powell is essentially the operations manager responsible for daily management on-site of construction projects. He has staff and some authority. He would also be responsible for liaising with other key stakeholders, particularly owner/managers (see above definition) and unions. The role of the project manager, therefore, was a coordinator.

5.2.2.6 Accountants Network Density

The role of accountants in the construction industry varied depending upon two factors: the firm size and the nature of the activity. Bragg (2007) suggests that in large firms, routine matters would typically be handled by an accountant and more complex matters by a tax expert, sometimes an internal staff member but often an external expert such as a registered taxation firm or accounting firm. Small firms would not employ a full-time accountant, nor a tax expert, so both routine and complex matters would be referred to external experts.

The role of accountants in the seven unlawful activities identified by the RC is difficult to identify. The main focus of the RC was on other stakeholders: owners/managers and unions in particular. However, there is sufficient evidence to re-enact the role of
accountants in the industry’s unlawful activities. This may be done by looking at testimony regarding these activities and asking whether accountants would have been involved in some way. For example tax evasion. The individuals seeking to evade tax, owners/managers, would have interacted with accountants in conducting this activity.

The following is an example of evidence about this type of unlawful activity. Union officials provided some evidence about how tax evasion occurs in the construction industry. The aim is to examine this evidence and to assess whether accountants were involved. Senior union official Ferguson alleged widespread group tax and payroll tax evasion and the use of sham subcontract arrangements and stated that:

In some sectors such as formworking, much of the costing process is based on subcontractors not paying group tax, payroll tax or WorkCover premiums. While it cannot be proved I believe that major developers and builders may have actively promoted these activities among their sub-contractors. I have no doubt that they know of the arrangements and are happy to be complicit, as such practices lower their cost structure (Cole 2003, vol. 9, p. 64).

In this statement, Ferguson is suggesting that large construction companies actively encouraged their subcontractors to engage in tax evasion because it would lower their costs. Given the activity involved cost management, accountants would have interacted with other stakeholders in this tax evasion. The same finding applies to the six other unlawful activities. While the level of involvement of accountants in these activities varied, accountants interacted with other stakeholders, particularly owners/managers when these unlawful activities were taking place.

5.2.2.7 Regulators Network Density

The main regulator of the construction industry was the Australian Federal Government. The government had several regulating agencies that interacted with the construction industry. The government’s main agency involved in taxation was the ATO. The ATO
was responsible for ensuring tax compliance in the construction industry. In a joint submission to the RC, the Australian Industry Group (AIG) and the Australian Constructors Association (ACA) suggested that “the Commission utilise the ATO submission to the Commission in order to inform itself on tax evasion issues” (Cole 2003, vol. 9, p. 55). This statement shows that peak industry bodies trusted the ATO to know the nature and extent of tax evasion in the industry. The AIG and the ACA continued by stating that “the views expressed to the Commission by the ATO are to be preferred to views expressed by industry participants, some of whom make assumptions about tax evasion or avoidance from the perspective of a preference for particular industry working arrangements” (Cole 2003, vol. 9, p. 55). This thinly veiled reference to union officials defends the industry bodies’ members from attack by arguing that Commissioner Cole should trust the ATO rather than the unions because the latter was trying to use tax evasion to coerce employers for other purposes, such as working arrangements.

However, Commissioner Cole felt that the ATO was not an “industry regulator” (Cole 2003, vol. 8, p. 139). Rather, the ATO’s responsibility is to ensure compliance with taxation laws (Cole 2003, vol. 8, p. 139). Its role is to ensure those who “evade payment of taxes are prosecuted, and deterred from further evasion and to minimise the loss of revenue” (Cole 2003, vol. 8, p. 139). The ATO provided support for Commissioner Cole’s argument by noting that “on any reasonable resourcing level the ATO is unable to monitor individual compliance of all taxpayers across their range of obligations” (Cole 2003, vol. 9, p. 81). The ATO therefore “utilises risk assessment and management approaches in order to direct its resources to areas of greatest risk, both within the building and construction industry and as between that industry and the remainder of the community” (Cole 2003, vol. 9, p. 81). The ATO “tailors responses to different
taxpayer groups based upon their level of compliance risk and their history” (Cole 2003, vol. 9, p. 81). In these statements, the ATO is stating that it is not resourced to be a community watchdog and, therefore, its role is not to regulate industry behaviour. It prioritises its investigative activities by focusing on industry sectors representing the highest risk of tax evasion. This point is further illustrated by the fact that “of the top 200 large ATO clients under regular review, 17 were from the construction industry” (Cole 2003, vol. 9, p. 62). This represents 8.5%. While this is a significant figure, it shows that the ATO had more to focus on than the construction industry alone.

While Commissioner Cole was careful to state that the ATO was not an industry regulator, it is included in this section on regulators because its role was to ensure compliance with tax payments. In its submission to the RC, the ATO “noted its long history of involvement with the construction industry and that it had maintained a particular focus in relation to income tax issues, including withholding tax obligations and that, since the year 2000, has been addressing Goods and Services Tax (GST) issues” (Cole 2003, vol. 9, p. 55). The ATO has identified significant areas of tax evasion and stated that “the industry warrants close attention due both to its size (approximately 6% of GDP, 13% of active Australian Business Numbers (ABN’s) and evidence of practices that indicate a high risk of non-compliance with taxation obligations” (Cole 2003, vol. 9, p. 55). While concluding, that “estimating the revenue leakage for the construction industry was problematic and had not proved meaningful, it noted that high levels of cash are used in the industry” (Cole 2003, vol. 9, p. 55). “It described the level of non-compliance as significant” (Cole 2003, vol. 9, p. 55).

The ATO explained that it was unable to act as an industry regulator because it could not “monitor the individual compliance of all taxpayers, and therefore uses risk management approaches to direct its finite resources to areas of greatest risk” (Cole
The way the ATO monitored risk areas explains their role in tax evasion in the construction industry. The ATO did this in three ways. (Cole 2003, vol. 9, p. 81). First, the ATO relies on community information in the form of “tip-offs”. “For the nine months to 31 March 2002, the construction industry accounted for 906 (6 per cent) of 14,996 of the tip-offs received by the ATO, making it the third largest reported industry” (Cole 2003, vol. 9, p. 81). While these figures indicate a significant proportion of tip-off activity is related to the construction industry, it is surprising that there was not more, particularly given the unions’ history of threatening employers with disclosure.

The ATO “undertakes routine analysis of tax lodgements and the levels of tax paid and other relevant data such as information from the AUSTRAC database” (Cole 2003, vol. 9, p. 81). The ATO “engages in specific scoping verification and enforcement activities” (Cole 2003, vol. 9, p. 81). For example, in its submission to the RC, the ATO reported that in “November 1999 the ATO undertook an analysis of AUSTRAC data concerning reportable cash transactions, sorted by location and industry for the preceding four years; and found large amounts of cash in formworking ($99.8 million), concreting ($62.3 million), scaffolding ($49.8 million), excavation ($34.4 million) and steelfixing ($13.9 million)” (Cole 2003, vol. 9, p. 81). Commissioner Cole stated that this “suggested to the ATO that the payment of cash was a common practice throughout these sub-industries” (Cole 2003, vol. 9, p. 81).

The ATO tried to explain the tax evasion in the construction industry by pointing out the highly competitive nature of the industry and stated: “On average, 19.7% of businesses in this industry are in debt to the Tax Office – the average for all business clients is 7.9% and 20% of current insolvency/bankruptcy cases are from the industry”
“Non-payment of tax debts is seen by some in the industry as a means of remaining competitive” (Cole 2003, vol. 9, pp. 56).

In its submission to the RC, the ATO highlighted that considerable revenue has been recovered from the construction industry through the ATO’s compliance activity and provided these examples:

- Formworkers/Steelfixers 1998 – current $20.6 million
- Scaffolders 1998 – current $8.0 million
- Bogus labour hire February 2000 – current $126.1 million
- Phoenix Companies 1998 – current $200.0 million

This information supported the claim by industry groups, the AIG and the ACA, that the ATO could provide helpful information on the nature and extent of tax evasion in the construction industry. The ATO provided evidence to the RC on the types of construction companies most involved in tax evasion. The ATO “placed particular emphasis on the commercial trade services sector” (Cole 2003, vol. 9, p. 55). However, the ATO admitted that it had insufficient resources to adequately police the construction industry and could only undertake random audits.

In his recommendations, Commissioner Cole concluded that the ATO is well aware of the problem of tax evasion in the construction industry, had implemented risk management strategies, and was trying to drive cultural change (for example, through educational programs). In other words, he was happy with the performance of the ATO and felt it was doing all it could to eliminate tax evasion in the construction industry. His only way forward was to recommend that the Commonwealth should consider increasing the ATO resources for compliance activity in the building and construction industry (Cole 2003, vol. 9, p. 89).
Security of payments was another of the seven unlawful activities identified by the RC which concerned regulators. Commissioner Cole was critical of all governments for failing to “monitor, review and improve their approach to prequalification with a view to improving security of payments within the building and construction industry” (Cole 2003, vol. 1, p. 113). Government is a major customer for the construction industry. It could set an industry standard by policing prequalification to ensure that companies it awards contracts to are able to demonstrate financial viability. Commissioner Cole recommended “the Commonwealth require, as a condition of the provision of Commonwealth funding to State or Territory projects, that tenderers be required to promote good payment practices to subcontractors on those projects” (Cole 2003, vol. 1, p. 114).

There were some positive attempts by regulators to police security of payments. In Queensland, the Queensland Building Services Authority Act 1991 was amended in 1999 “to improve security of payments to contractors and to ensure that licensees associated with failed business operations could not regain a licence by simply re-inventing themselves” (Cole 2003, vol. 8, p. 158). This type of legislation is necessary because it “provides the power to exclude any individuals or companies from holding a licence for a period of five years upon certain events occurring” (Cole 2003, vol. 8, p. 158).

In NSW, the Code of Practice for the Construction Industry (CPCI) established principles and standards of behaviour which must be observed by companies “wishing to do business with the Government or working on projects to which the Codes apply, including those with private sector funding” (Cole 2003, vol. 8, p. 189). Subsection 4.2 of the CPCI “relates to security of payments and states that the highest ethical practices must occur throughout the contract chain, including between contractor and
subcontractor and between the subcontractor and his or her employees, to ensure that all parties receive payments due to them” (Cole 2003, vol. 8, p. 189).

In a case study called the Cairns Central project, several of the subcontractors, who worked on the Cairns Central project and experienced difficulties, expressed the view that “if the option of an independent arbitrator had been available at an earlier stage the problems could have been quickly resolved” (Cole 2003, vol. 8, p. 234). The experience of these subcontractors bears out those comments. “Because it was too slow and too expensive to litigate, subcontractors in effect had no option but to accept whatever was offered to them by a head contractor, whether or not the offer fairly valued the work that had been done” (Cole 2003, vol. 8, p. 234).

Commissioner Cole recommended a number of reforms to the regulation of security of payments aiming to address the problems outlined in this section. The reforms are listed to illustrate the nature of changes to security of payments requested by Commissioner Cole. This list will be used later to explore the role of accountants in terms of this changed behaviour. The reform proposals fell into two groups. These are as follows:

The first group targets the financial performance of businesses in the industry, in order to reduce the risk of financial problems that lead to the failure to pay subcontractors. These strategies include:

- utilising prequalification guidelines for government procurement processes to give greater scrutiny to financial viability of the contractor
- enhancing licensing conditions to give greater scrutiny to the financial viability of the builder (Cole 2003, vol. 8, p. 245).

The second group of proposals covers schemes to improve the mechanisms that assist subcontractors in recovering payments that are owed to them, or to provide some protection against the insolvency of parties higher up the contractual chain. Such mechanisms include:

- codes of practice that specify the industry standards for payments to subcontractors;
- trust funds;
- compulsory insurance schemes;
- improved training and information on subcontractors’ rights and responsibilities;
- requiring certain contract clauses and prohibiting other contract clauses;
• arrangements to facilitate rapid adjudication of disputes (Cole 2003, vol. 8, p. 245).

Regulators had introduced a scheme specifically designed to address the problem of underpayment of employee entitlements before the RC. In 2000, the Employee Entitlements Support Scheme (EESS) was introduced. It was a scheme funded by the Federal Government to cover basic payments of employee entitlements. It provided “capped payments that guaranteed employees up to 29 weeks of pay (at ordinary time rates); up to 4 weeks unpaid wages; 4 weeks annual leave (accrued in the last year); 5 weeks pay in lieu of notice; 4 weeks redundancy payment; and 12 weeks long service leave, if any of these were eligible to employees” (Symes 2003, p. 134). The scheme applied to employees who were “terminated on or after 1 January 2000 as a result of their employer's insolvency” (Symes 2003, p. 134). A revised scheme, called the General Employee Entitlements and Redundancy Scheme (GEERS), was introduced on 12th September 2001 (Symes 2003). The GEERS “paid all unpaid wages, all accrued annual leave, all accrued long service leave, all accrued pay in lieu of notice and up to 8 weeks redundancy entitlements” (Symes 2003, p. 134). The amounts payable under the GEERS increased over the following decade through “annual indexation of the statutory cap and a number of revisions to the Operational Arrangements which govern the terms of the scheme” (Anderson 2014, p. 128). The most recent revision, which “took effect on 1 January 2011, reflected the Federal Labor Government’s Fair Entitlements Guarantee, an election promise made in 2010 by the Gillard Federal Government as part of its Protecting Workers’ Entitlements package” (Anderson 2014, p. 128). The statutory cap of “16 weeks’ redundancy pay for all workers was replaced by a cap of four weeks’ redundancy pay for each completed year of service” (Anderson 2014, p. 128).
These schemes are particularly interesting because they were introduced prior to the conclusion of the RC and yet Commissioner Cole still found widespread underpayment of employee entitlements. This suggests these prior schemes were ineffective. On reflection, schemes such as GEERS probably provided a further incentive for unscrupulous company directors to seek insolvency and avoid paying employee entitlements because they may have felt the Government would cover their debt and be less likely to pursue them to pay their employees’ employee entitlements. There is evidence prior to the RC, that companies had tried to avoid paying employee entitlements and had been successfully prosecuted by regulators, but employees were not always able to recover full compensation. In December 1997, “the Grafton Meatworks closed, and its holding company R J Gilbertson’s Pty Ltd, which owned land and buildings, denied liability for the AUS$3 million in accrued entitlements for 245 employees because they were employed by two asset-less labour supply companies in the group” (Anderson 2014, p. 127). An Australian Securities and Investments Commission (ASIC) investigation of the closure found a “deed of cross guarantee from the parent company that still applied, which meant the other companies in the Gilbertson group had to support the debts of the insolvent companies” (Anderson 2014, p. 127). Similarly, “Ghana-based Ashanti Goldfields covered for Cobar Mines Pty Ltd when it went into liquidation in January 1998, with 267 employees losing their jobs as well as accrued entitlements of AUS$10.5 million” (Anderson 2014, p. 127). The threat of action by ASIC led to Ashanti paying the employees the majority of their employee entitlements, 85 cents in the dollar (Anderson 2014, p. 127).

The regulators of the construction industry felt that the underpayment of employee entitlements was unlawful. The RC found that “a culture of lawlessness pervades every level of the industry” (Cole 2003, vol. 3, p. 211). Among the many manifestations of
unlawfulness was the action of companies that evade paying rightful employee entitlements (Cole 2003, vol. 3, p. 211). The focus of regulators was on the fairness of procedural justice, particularly over-entitlement that is, greed. In this case, the RC placed blame on employers for arguing that employees were seeking more than they were entitled too (being greedy), when they and their unions were only seeking what they were legally entitled to.

The regulators tried to enforce appropriate employee entitlements within the construction industry by referring to the definition of “pattern bargaining” which appeared in the Workplace Relations Amendment Bill 2000 (C’wth) (Cole 2003, vol. 5, pp. 57-58). Pattern bargaining “means a course of conduct or bargaining, or the making of claims, involving seeking common wages and/or other common employee entitlements”, which extends beyond a single business, and “is contrary to the objective of encouraging agreements to be genuinely negotiated between parties at the workplace or enterprise level” (Cole 2003, vol. 5, p. 57). This was a lawful method for enterprise bargaining which would encourage uniformity in employee entitlements across the construction industry, that is procedural justice, but still allow flexibility to negotiate above normal employee entitlements, that is legitimate performance or bonus.

While the regulator found evidence that “underpayment or miscalculation of workers’ wages and entitlements” is a substantial problem in the construction industry, it did not feel that it could fix the problem (Cole 2003, vol. 7, p. 202). Indeed Commissioner Cole said “it is unrealistic to expect statutory authorities to intervene each and every time a dispute arises in relation to compliance with statutory or award obligations, or obligations under workplace agreements” (vol. 7, p. 202). This suggests that the regulators were limited in terms of the role they could play in introducing equitable and fair employee entitlements uniformly across the construction industry. While the
regulator could introduce legislative change, Commissioner Cole is here explaining that the problem needed to be fixed by others, primarily employers.

Commissioner Cole was critical of the State and Territory governments for not being tough enough about payroll tax evasion. He encouraged “the States and Territories to adopt measures to prevent evasion of payroll tax obligations” (Cole 2003, vol. 1, p. 16). He acknowledged that while these governments had the right to impose their own view on payroll tax, it was an issue of national importance. He argued that tax evasion was “an issue of importance” in the construction industry (Cole 2003, vol. 1, p. 106). Commissioner Cole highlighted that if regulators were unwilling to properly enforce lawful behaviour regarding taxes, including payroll tax, unscrupulous individuals will “often evade other revenue obligations, and the proper payment of employee entitlements and obtain a competitive advantage over businesses which comply with their obligations” (Cole 2003, vol. 1, p. 106). In other words, by allowing these individuals the opportunity to engage in tax evasion, fraudulent activity becomes an industry norm, and it spreads into other areas, as has been highlighted in this chapter.

Commissioner Cole placed responsibility with the Federal Government for taking a tougher stance on payroll tax evasion. He recommended that “the Commonwealth should take the lead in encouraging States and Territories to introduce measures which eliminate fraudulent conduct such as the evasion of revenue obligations in the industry” (Cole 2003, vol. 1, p. 106). One way forward would be to encourage the “revenue authorities to share information relevant to the detection of payroll tax evasion in the construction industry” (Cole 2003, vol. 1, p. 107). His recommendation was that amendments be made to legislation to enforce a consistent tougher approach across the States and Territories. An initiative was the harmonisation of the key definitions of the payroll tax system, “particularly the definition of wages, between the different
jurisdictions is an important object, particularly in the building and construction industry where many large contractors operate nationally” (Cole 2003, vol. 1, p. 107). The Payroll Tax Authority (PTA) website includes information on the harmonization of payroll tax legislation across the states and territories, showing that this was one of Commissioner Cole’s successful recommendations.

There was also an example in the RCR of Government endorsing payroll tax noncompliance, although probably not intentionally. The following extract illustrates how payroll tax exemptions were part of an incentive package offered by the Queensland Government:

The Queensland Government had a program to attract jobs and development to regional areas like Townsville. The Townsville City Council was anxious to attract investment to the area. At a mining industry seminar held at some time before 1996, Mr Tony Mooney, the Mayor of the Townsville City Council: ‘…made it plain to industry leaders, senior government representatives, financiers and anyone else who is interested that ‘the Townsville community not only welcomes secondary industry such as metals and mineral processing but we are prepared to roll out the red carpet via incentives, fast-tracking approvals and any other assistance required’ (Cole 2003, vol. 18, p. 247).

Thus, the Queensland Government used payroll tax exemptions to encourage investment from overseas. However, it presents confusion and contradiction to local companies in terms of their payroll tax obligations.

One of the main reasons phoenix company activity flourished in Australia was the incompetence of the regulatory system. There was a lack of accountability, lack of cooperation, and inadequate legislation. The RC found that there was a lack of accountability in terms of regulating phoenix companies. Commissioner Cole stated that “there appeared to be no clear guidelines at the Federal Government level as to which agencies were responsible for detecting and policing fraudulent phoenix company activity in the construction industry” (Cole 2003, vol. 1, p. 108). With no-one watching
them, companies would be more tempted to engage in unlawful behaviour. Commissioner Cole recommended that two agencies in particular, ASIC and the ATO, “be given appropriate resources to combat fraudulent phoenix company activity” in the construction industry (Cole 2003, vol. 1, p. 108).

Regulators acknowledged they needed to cooperate more if they wanted to address phoenix company activity. The RC recommended that ASIC and the ATO should cooperate more by “sharing information in order to eliminate or diminish phoenix company activity” (Cole 2003, vol. 1, p. 16). Similarly, Commissioner Cole asked that revenue authorities, including payroll tax authorities, should cooperate by sharing information relevant to the detection of fraudulent phoenix company activity (Cole 2003 vol. 1, p. 107). To implement this recommendation, the Federal Government must work with the State and Territory Governments to permit their revenue authorities to share information. On a similar theme, Commissioner Cole recommended that the ATO be provided with “increased funding to be utilised for compliance activities in the building and construction industry” (Cole 2003, vol. 1, p. 122).

Despite the efforts of the RC to highlight the negative effects of phoenix activity, little was done to implement the measures recommended. In 2009 (six years after the RC), the Federal Government Treasury released a proposals paper entitled ‘Action against fraudulent phoenix activity’ (Anderson 2012). The paper canvassed options to address fraudulent phoenix activity, which it estimated to cost the ATO AUS$600 million per year at the time (Anderson 2012, p. 415).

Commissioner Cole also sought to address the purpose for establishing phoenix companies as a way to eliminate them. With avoiding payroll tax being one of the purposes, he argued that enforcing payroll legislation might deter phoenix activity. He
recommended that the Federal Government encourage the State and Territory Governments to adopt “s16LA of the Pay-Roll Tax Act 1971 (NSW) to address phoenix company activities in the construction industry” (Cole 2003, vol. 1, p. 106). If uniformity across Australia could be achieved by adopting this legislation, then it would make owners fearful of the consequences of phoenix company activity. These provisions in this Act “make all members of a group jointly liable for the payroll tax debts of other group members” (Cole 2003, vol. 1, p. 106). This would make it more difficult to use phoenix companies to avoid tax. On a similar point, the lack of penalties failed to deter fraudulent activity. The RC found that “low levels of penalties have been imposed by the courts where persons have been convicted in relation to phoenix company activity in the construction industry” (Cole 2003, vol. 1, p. 110). Commissioner Cole recommended that there needs to be “an increase in the maximum penalties provided in the Corporations Act 2001 (C’wth) for offences that may be associated with fraudulent phoenix company activity” (Cole 2003, vol. 1, p. 110). This would act as more of a deterrent for fraudulent activity.

Commissioner Cole also tried to address some of the opportunities for unlawful behaviour. For example, he tried to address the problem of allowing unscrupulous directors to voluntarily declare insolvency, by asking the Federal Government and the ATO to consider amending s222AOB of the Income Tax Assessment Act 1936 (C’wth) (ITA Act 1936) “to remove the right of a director of a phoenix company involved in fraudulent activity to avoid the consequences of a Director’s Penalty Notice by placing the company into voluntary administration or into liquidation” (Cole 2003, vol. 1, p. 124). This sought tougher legislation to switch phoenix activity towards voluntary administration and trying to save the company, rather than unlawful behaviour.
While some of Commissioner Cole’s recommendations regarding phoenix activity were not adopted (see above), there was some success in terms of regulators taking a tougher stance. While actual data about phoenix activity and subsequent ASIC actions against directors are not publicly available, ASIC itself seems to know which prosecutions are related to phoenix activity. For example, in 2007, the ASIC Chairman Jeffrey Lucy issued a press release declaring that ASIC had “banned 40 directors for a total of 144 years who have engaged in misconduct following company failures and repeat phoenix activity” (Anderson & Haller 2014, p. 490). This statement provides evidence of increased penalties to deter phoenix activity.

The federal government also tried to respond to Commissioner Cole’s criticism of toothless legislation with two exposure drafts of legislation, the Corporations Amendment (Phoenixing and Other Measures Bill) 2012, passed into legislation in May 2012 and the Corporations Amendment (Similar Names) Bill 2012 remained an exposure draft (Anderson & Haller 2014, p. 474). The legislation recognised that phoenix activity affects more than taxation authorities; such as employees, as well as other stakeholders. In introducing the legislation, the government made the following claims:

These amendments will crack down on ‘phoenixing’, where directors try and avoid having to pay workers’ entitlements and other unsecured creditors by restarting their failed business using a similar company name, sometimes located in the same premises with the same staff and clients.

Under these proposals, directors of a failed company can be held liable for the debts of a company that has a similar name to a pre-liquidation name of the failed company —otherwise known as a phoenix company.

This will stop directors from exploiting the limited liability protections in the corporations law to avoid having to pay any debts, including workers' entitlements, that they incur in a ‘phoenix’ company.
This will ensure that directors cannot keep racking up debts through multiple ‘phoenix’ companies and escape their obligations to pay workers’ entitlements and other creditors (Anderson 2012, p. 423).

Anderson (2012, p. 423) argued that “these were very ambitious claims, and seemed to promise that the government had finally heeded the repeated calls for legislation to tackle phoenix activity”. However, Anderson was quite cynical about whether these claims would actually be met and whether the legislation would be enforceable and indeed eliminate phoenix activity. She concluded that in “reality the proposed legislation does little to help those adversely affected by fraudulent phoenix activity and even less to deter company controllers from this harmful behaviour” (Anderson 2012, p. 413). Further support for criticism of the regulator’s inability to address Phoenix activity was provided in 2012 in response to a consultant’s report on phoenixing in Australia (see Owen 2012 above). Fair Work Australia indicated they would establish relationships with other regulators, including the ASIC and the ATO, to work collaboratively in this area (Owen 2012). The Federal Government responded with a statement that it had introduced stronger legislation, with the Corporations Amendment (Phoenixing and Other Measures) Act 2012 (Phoenixing Act 2012), which came into effect on July 1 2012, to empower the corporate regulator, ASIC, to order the winding up of companies that directors abandon in the context of fraudulent phoenix activity (Owen 2012). Almost ten years after the RC made recommendations calling for cooperation between regulators and stronger legislation, these measures were beginning to be implemented. However, Anderson (2012) argued from a legal perspective that these measures were difficult to enforce; inferring that phoenix activity would continue.

Commissioner Cole recommended changes to the legislation to address payment delays in employee entitlements due to EBA’s. He recommended that The Building and Construction Industry Improvement Act:
a. provide that the objective of enterprise negotiations should be to reach a new agreement prior to the nominal expiry date of any existing agreement; and

b. provide that any obligation imposed on an employer under an enterprise bargaining agreement to pay any wages, allowances, contributions or any other monetary benefits to or on behalf of employees cannot be made retrospective beyond the date of agreement unless the Australian Industrial Relations Commission is satisfied that the employer has unreasonably delayed negotiations (Cole 2003, vol. 5, p. 64).

There are two types of issues involving inappropriate payments in the construction industry: project payments and liquidation. In some countries and on some projects it is unlawful or not permitted for contractors to withhold payments to subcontractors because of delayed and incomplete payments from the owner. For example, the United States Department of Transportation has regulations requiring that general contractors pay their subcontractors after the completion of subcontracts, even if they have not received their own payment from the owner (Touran, Atgun & Bhurisith 2004). The security of payments legislation operating in the states of Australia also nullifies the effect of the “pay when paid” and “paid if paid” clauses in a contract, in order to protect subcontractors from the practice of owners and contractors arbitrarily delaying or denying payment (Uher & Brand 2008).

5.2.2.8 Trade Unions Network Density

The unions interacted regularly with staff, and with owners/managers, and also with regulators. This interaction was frequent and in high volumes, with many individuals in these other stakeholder groups. Therefore, unions had a high density within the construction industry’s social networks. However, this level of interaction was not a positive factor in the industry’s social networks. As outlined above, high density should generate more opportunity to build and maintain relationships, resulting in increased communication, trust, and social dependency. This was certainly not the case with the
unions and other stakeholders in the construction industry. While it may have occurred in interactions between unions and staff, who were union members, it was not so in interactions with other stakeholders. With these other stakeholders, the characteristics of low density emerged namely mistrust and conflict.

In their interactions with other stakeholders, the unions played several roles. With staff, the unions were advocates. The unions were concerned that employers met their obligations towards employees, the unions’ members, in two ways. First, the unions wanted to ensure that employers paid employees what they were legally entitled to while working for the firm, in both salary and non-salary terms. For example, workers should have the firm contribution towards superannuation automatically deposited into their super fund at each pay. Second, the unions wanted to ensure that workers’ were paid what they were owed if the firm went out of business. For example, if a firm becomes insolvent and closes its doors, its employees would often not receive payment for outstanding leave. The unions negotiated with owners or investors and managers to ensure that workers’ rights were protected against these issues.

The unions’ focus was on entitlement as a right. The unions tried to ensure their members, that is construction industry employees, were treated equitably. They felt that equitable employee entitlements, was their workers’ right. In other words, the unions wanted distributive justice in terms of employee entitlements. The RC found that the unions “desired uniformity of outcomes for members as a basic tenet of collectivism. It also reinforced the unions’ bargaining power and their ability to dictate outcomes on building sites” (Cole 2003, vol. 3, p. 208). Some regulators offered support to the unions in advocating procedural justice for employees in terms of their employee entitlements. “The Western Australian Department of Consumer and Employment
Protection submitted to the Royal Commission that unions in the building industry had a legitimate role to play in enforcing employee entitlements” (Cole 2003, vol. 9, p. 25).

With regulators, the unions were whistle-blowers. The three main areas focused on by unions were tax evasion, phoenix company activity, and security of payments. The unions used the first activity, tax evasion, to threaten owners/managers in negotiations for better conditions for their members. The unions used the two latter activities, phoenixing and security of payments, to protect members from not being paid their entitlements.

The unions played a positive role in surfacing the problem of tax evasion. In submissions to the RC there are numerous examples of unions providing evidence of tax evasion. In Queensland, Mr Wallace Trohear, State Secretary of the Construction, Forestry, Mining & Energy, Industrial Union of Employees, Queensland and Branch Secretary of the Construction and General Division of the CFMEU estimated that “up to 65 per cent of the building and construction industry was on sham subcontracting arrangements and is only paying tax on the amount received as award or Enterprise Bargaining Agreement (EBA) rates” (Cole 2003, vol. 9, p. 53).

The unions would have been aware of phoenix activity, as it would have affected their members, particularly in the case of insolvency where people may have lost their jobs. Commissioner Cole felt that the unions might be used as a “whistle-blower” in the sense of making the regulators aware of unlawful behaviour. However, there was no process for community consultation undertaken by the ATO (ATO) (Cole 2003, vol. 1, p. 125).

The history of trade unionism in Australia was to battle against the government. Regulators were often seen as the enemy rather than an ally. It is hard to imagine that the unions would have been keen to help the ATO. However, Commissioner Cole
recommended establishing a BCIF “to examine taxation issues of significance to the
construction industry including phoenix company activity, and to develop workable
solutions to the issues and problems identified” (Cole 2003, vol. 1, p. 125). The forum
was intended to include representatives of all major industry participants including

The unions were concerned about security of payments because it affected the
livelihood of their members. The CFMEU told the RC that:

Principal contractors frequently fail to make payments due under contracts at the
time which they are due. Sometimes there are legitimate disputes as to the
proper performance of contracts by the sub-contractor; in other cases the
principal simply withholds payment for spurious reasons, knowing that the
subbie does not have the means to pursue legal remedies or that the time and
cost of litigation is not justified by the amount owed. The situation is further
complicated by the use of verbal agreements, particularly in relation to
variations. This is one of the major reasons for the high level of insolvencies in
the building and construction industry (Cole 2003, vol. 8, p. 235).

The issues raised in this case, that is, withholding payment for illegal reasons, exerting
influence over weaker stakeholders, and lack of regulation and corporate governance,
are important themes explaining social behaviour within the construction industry, and
are examined further in the next section.

With owners/managers, the unions were adversaries. The main adversary role was in
negotiating employee entitlements. The unions’ focus on procedural justice was to
engage with employers when employee entitlements expectations were not met. The RC
found in Victoria that union officials of the CFMEU followed their own agreements,
namely the Victorian Building Industry Agreement and the National Building and
Construction Industry Award 2000 (NBCIA), rather than the regulators’ Workplace
Relations Act 1996 (C’wth) (Cole 2003, vol. 7, p. 177). As a result, the unions adopted
an aggressive stance with employers and represented the biggest fallout from procedural
injustice regarding employee entitlements. The RC investigations into employee entitlements found that employers were “routinely insulted, abused, harassed and intimidated, often for the purpose of pressing employers to make corrective payments to employees, and with the premature assertion that the employer’s records were not in order” (Cole 2003, vol. 7, p. 177). Commissioner Cole here is suggesting that the unions tended to skip over the processes of procedural justice and jumped straight to the fallout step, assuming, perhaps incorrectly, that all employers were underpaying employee entitlements. This adversarial approach, outside the regulatory framework, meant that the end process of employee entitlements, managing fallout, was not begun in good faith by both parties.

Further evidence that the unions approached this issue as an aggressor was provided by an industry group, the Housing Industry Association Limited (HIA), which claimed the unions sought to recover superannuation or redundancy contributions by often acting outside the legal system (Cole 2003, vol. 9, p. 33). The HIA claimed that the “unions commonly use industrial pressure to enforce payment of what they regard as workers’ entitlements”; including over-award “entitlements” which the employer has in point of fact never agreed to pay (Cole 2003, vol. 9, p. 33). This is an example of the unions claiming overentitlement, which employers would claim was procedural injustice, particularly because the industrial pressure was not really about the protection of the unions member “legal rights but rather part of the bargaining process between employers and employees” (Cole 2003, vol. 9, p. 33). The unions were using the pretence of unpaid employee entitlements to leverage better working conditions for their members.
5.2.2.9 Competitors Network Density

Within the context of the analysis presented in this chapter, competitors are other construction companies. The analysis of owners/managers outlined above, therefore, applies to competitors. The best way to understand the peculiar nature of the interaction between competitors in the construction industry is to consider the complex contracting system, consisting of head contractors, contractors, and sub-contractors, who despite being competitors, often worked together on projects. The behaviours found by the RC were so widespread they were often described as industry culture. An example of the impact of this finding is provided by phoenix company activity. Commissioner Cole noted that phoenix behaviour even affects competitors. “Companies that fail to pay taxes, superannuation contributions and employee entitlements can undercut prices in tenders made by law-abiding companies, which may be induced to act in a similar manner if phoenix activity is not detected and prosecuted” (Anderson 2012, p. 413). This indicates that the role of competitors was imitators.

5.2.2.10 Customers Network Density

Customers interacted regularly with owners/managers, and also project managers. This interaction was frequent and in high volumes with many individuals in these other stakeholder groups. Therefore, customers had a high density within the construction industry’s social networks. However, this level of interaction was not a positive factor in the industry’s social networks. As outlined above, high density should generate more opportunity to build and maintain relationships, resulting in increased communication, trust, and social dependency. In many ways, this was the case in relationships between customers and construction companies. Strong relationships would certainly have helped companies get work. However, there was also a dark side to the interaction with
customers, which exhibited the characteristics of low density, that is, mistrust and conflict.

In their interactions with construction companies, the role of customers was bargain hunter. An example of this was the way that construction companies “bought work”. The RC reported that representatives of governments and other industry clients said that major contractors may sometimes “buy” work (Cole 2003, vol. 6, p. 40). Governments and clients will accept a tender price which is seen to be very low, if that tenderer is known to understand the scope of the project and to be otherwise considered “reliable” by the client (Cole 2003, vol. 6, p. 40). As a result, “for a head contractor to ensure profit at the end of a project, considerable pressure is often applied by the head contractor with the aim of reducing the costings provided by tendering subcontractors” (Cole 2003, vol. 6, p. 40); and “this same process is then replicated down the chain of sub-subcontractors” (Cole 2003, vol. 6, p. 40). This flow-on affect illustrates how cut throat the construction industry is. Large companies tender for projects at prices so low that profit is very difficult with the sole objective of ensuring cash flow and employment for staff. To make a profit, they exert their power over sub-contractors, who depend upon the large contractors for their own survival, who then must also lower their prices to win the work.

Subcontractors told Commissioner Cole that “bid shopping is commonplace, and creates enormous problems and, given that tenders are usually prepared on the basis of slim profit margins, requires subcontractors to, in turn, put pressure on the tender prices they seek from sub-subcontractors” (Cole 2003, vol. 6, p. 41). It leads contractors to “take short-cuts in order that they are able to retain a profit at the end of the work” (Cole 2003, vol. 6, p. 41). The use of this word “short-cuts” is particularly interesting. While reducing the quality of work (for example, through time spent) or quality of materials
are obvious short-cuts, it is also very possible that this was not properly reported in profit and loss statements. These short cuts were a “practice which is commenced at the top level and, by necessity, pushed down through each of the levels in the chain of contracting” and Commissioner Cole found that it “goes all the way down the chain”, because “to survive, a subbie has to do it to the next person below them in the chain” (Cole 2003, vol. 6, p. 41).

Subcontractors face pressure to underbid competitors when quoting for jobs. This can result in a subcontractor quoting a price lower than cost, making it impossible for the subcontractor to make a profit. “Cash flow problems can lead to the subcontractor avoiding paying group tax, payroll tax, and workers compensation premiums so that they can pay their employees” (Cole 2003, vol. 8, p. 133). Subcontractors can delay making payments as they are only required to remit tax payments periodically. The subcontractors “can pay some wages in cash to its employees, as did a number of formworking company operators in Sydney, who were audited by the ATO in early 1999” (Cole 2003, vol. 8, p. 133).

5.2.2.11 Industry Associations Network Density

Industry associations or employer groups interacted regularly with owners/managers, and less regularly with regulators. Their role was as an advocate for construction companies, in the same way that unions were advocates for staff. Industry associations were typically defensive about allegations of unlawful behaviour, such as tax evasion, by their members. Mr Wilhelm Harnisch, Chief Executive Officer of Master Builders Australia Inc (MBA Inc) stated that: “Any allegation that there is widespread practice of avoidance needs to be properly tested. MBA Inc is not aware of any endemic problem of avoidance in the building and construction industry” (Cole 2003, vol. 9, p. 55). The
Housing Industry Association (HIA) submitted that: “As evidence to date before the Commission has demonstrated, evasion of tax is undoubtedly attempted by some employers, some employees and some contractors, and there is no reason and no evidence to suggest that one group is in general worse or better than any other” (Cole 2003, vol 9, p. 55). The HIA are admitting here that tax evasion occurs but aimed to deflect blame or further enquiry by saying it would be difficult to identify who engages in the unlawful behaviour, one group or the other. However, other industry groups could identify industry sectors for investigation. The Civil Contractors Federation (CCF) stated that “the extent of income tax evasion in the industry is unknown in our opinion” (Cole 2003 vol. 9, p. 55). However, the CCF was in agreement with the unions that there has been misuse of Australian Business Numbers (ABN’s) and that cash was still an issue in the industry, although likely to be more so at the “smaller end of the market” (Cole 2003, vol. 9, p. 55). By the smaller end, they meant small subcontractors rather than larger companies.

5.2.2.12 Suppliers Network Density

Suppliers are organisations who provide services related to employee entitlements such as superannuation funds. One of the larger funds is Cbus. In their submission to the RC, Cbus stated that “ultimate compliance levels for Cbus employers was close to 90 per cent, although it was noted that this cannot be said to be indicative of the industry as a whole” (Cole 2003, vol. 9, p. 29). “About 28 per cent of the building and construction industry workforce had their superannuation entitlements paid into Cbus” (Cole 2003, vol. 9, p. 30). This finding indicates that there was a high proportion of superannuation paid for about a third of the industry’s employees; although 100% compliance would be better than 90%.
There was also positive news in terms of how employers responded to non-compliance of employee entitlements. In the case of Cbus, if superannuation payments fall into arrears, that is, are not paid on time, then arrears letters are sent. Cbus’s credit control manager takes action to obtain the missing payments, presumably by contacting the accounting staff at the construction company. In their submission to the RC, Cbus explained that arrears letters are sent to construction industry employers on average in 10% of cases, which is significantly less when compared to other industries (up to 40%) (Cole 2003, vol. 9, p. 30). Cbus offers further positive feedback:

Our company has been able to recover a significant portion of that 10 per cent. So our actual default rate, I believe, is very low for any fund, let alone a fund that is operating in an industry that presents a number of challenges to try to recover employees’ entitlements, where there are a very small number of employees, where they are not using, in most cases, electronic facilities, and where there is a very high level of mobility (Cole 2003, vol. 9, p. 30).

This suggests that suppliers of financial services associated with employee entitlements in the construction industry may have been fairly satisfied in their dealings with the industry. Further, that employers tended to try to comply and to do the right thing by their employees in terms of employee entitlements.

5.2.2.13 Summary of Social Network Interaction

In conclusion, the following figure summarises the types of interactions between the construction industry stakeholders.
The text boxes underneath each connecting line describe the role of each stakeholder in this interaction. The figure shows that the construction industry’s social networks were dominated by interaction between a few stakeholders, such as owners/managers, trade unions, and regulators, who had high density within these networks. However, in the next section it can be seen that high network density is not always a positive factor.

5.2.3 Social Behaviour

5.2.3.1 Introduction

This section examines the social behaviour of the construction industry using the stakeholder ethical perspective. If relationships were characterized by cohesion and harmony within the social network, generated by equality, democracy and participation
amongst all stakeholders, then the construction industry would be considered to have ethical social behaviour. However, if relationships were characterized by fragmentation and discord, generated by inequality, repression, and exclusion, then the industry would demonstrate unethical social behaviour. This unethical behaviour will be explained by ST’s managerial perspective.

SNA’s heterogeneity and homogeneity constructs will be used to examine behaviour between these stakeholder groups, with a particular focus on their harmony and cohesion. This is to examine stakeholder behaviours when they interacted in terms of their heterogeneity and homogeneity. The aim is to further explore the harmony and cohesion of social relationships within the construction industry. Harmony would indicate tolerance and respect between stakeholder groups. Cohesion would indicate efficient teamwork. The analysis will identify the overall network behaviour. It will also highlight differences in behaviour between stakeholders, that is, which groups seek harmony and cohesion and which do not. This analysis is looking for common themes in terms of homogeneity in actor attitudes, beliefs and practices. If inclusive (heterogeneous), the social network welcomes different types of members and is tolerant of different views, if exclusive (homogenous), it allows membership only to people who are similar (Stone 2001). Heterogeneity is a positive factor in social networks because it identifies the subjective nature of diversity in opinions. The more heterogeneity, the more tolerance and respect for different stakeholders. This results in ethical behaviour in terms of harmony. This analysis is looking for common themes in terms of constraints, which explores the extent to which a network membership is democratic; if democratic, decisions will be taken horizontally; if non-democratic, decisions will be taken vertically (Anklam 2005). Democracy is a positive factor in social networks because it helps in controlling the activities. The more shared control
within the network, the more efficient the group is because it allows divergent thought, creativity, and innovation; which ultimately results in ethical behaviour in terms of cohesion.

5.2.3.2 Overall Social Network Harmony

In general, there is a strong homogeneity in terms of stakeholder attitudes, beliefs and practices within the construction industry’s social networks. This meant that the social networks allowed membership only to people who were similar. This created disharmony because the social networks excluded people who did not accept and follow the norms of behaviour, which in turn caused conflict between stakeholders.

Evidence for the heterogeneity of the social networks is found in the construction industry’s unlawful behaviour. There was a culture of unlawful behaviour within the industry that made certain activities part of normal social behaviour. Stakeholders were encouraged to cooperate and participate in this unlawful activity. Harmony was maintained while stakeholders agreed to the unlawful activity. However, conflict emerged when stakeholders refused to participate.

The first cultural behaviour found in stakeholders’ unlawful activities was “an attitude of resigned acceptance” amongst contractors (Cole 2003, vol. 3, p. 28). There was a widespread perception amongst industry stakeholders that inappropriate behaviours had existed for many years and that these would not change. There was a common “feeling that the industry, as it presently exists, has not changed in any material respects for a long period, and that there is effectively nothing which they (contractors) can do to improve the industry” (Cole 2003, vol. 3, p. 28). Commissioner Cole found that contractors, as business people, were pragmatists in that “they will conduct business in the existing conditions in whatever way they can, which is most profitable for their
enterprise” (Cole 2003, vol. 3, p. 28). However, they were also accepting of the power exerted by unions over the industry.

Industry structure was used as an excuse for inappropriate behaviour in the construction industry. Commissioner Cole argued that contractors felt powerless to respond. In other words, to act appropriately, rather than, inappropriately. While they were “frustrated” by the power of the unions and that the unions had essentially “usurped aspects of control of their businesses”, contractors know that there was no “unified approach by business, whether head contractors or subcontractors, towards resisting demands by the unions” (Cole 2003, vol. 3, p. 28). This meant that contractors knew they stood alone against the unions and they could not exert any power as individual companies against the unions.

The RC also found that contractors feared “being singled out by unions because of the great loss which can occur to an individual contractor, and thus accede to industrywide arrangements” (Cole 2003, vol. 3, p. 28). They preferred to “accept restrictive practices affecting the flexibility and productivity of their businesses than to seek to improve productivity by arrangements which would attract the ire of unions” (Cole 2003, vol. 3, p. 28). This suggests that inappropriate behaviours affecting profit and loss disclosure would have been tolerated by employers who felt they had no choice. However, they would have been also unwilling to record this inappropriate behaviour in financial statements, which suggests that some form of manipulation occurred in profit reporting.

The strong homogeneity within the construction industry’s social networks created an industry culture which tolerated unlawful activity. The second cultural behaviour found in stakeholders’ unlawful activities was the widespread use of cash payments. This was done to help individuals and companies avoid paying tax. In the construction industry, if
an individual is paid cash in return for goods or services there is the possibility that they will not disclose this payment to the taxation authorities and, therefore, avoid paying income tax. This practice was commonplace in the construction industry.

The following example from Tasmania illustrates how employers and head contractors, could “pretend” employees were contractors to help them both avoid tax.

Atkins gave the example of a foreman, for example, engaged by a small commercial builder, who he said as a matter of law was clearly an employee, but who was paid an hourly rate of $25 as a subcontractor. Atkins said the correct hourly rate under the relevant award for such a person was $25.72 an hour. He said that, in addition, the employer was evading its obligations as to superannuation, redundancy, long service leave, holiday leave, sick leave and public holidays. The employer was also saving on the cost of workers’ compensation insurance, public liability insurance, payroll tax and administrative overheads. He said the advantage to the foreman of being treated as a subcontractor was an increase in the gross amount received each week, the opportunity to split income with his partner, and the greater availability of tax deductions relating to depreciation and office expenses (Cole 2003, vol. 12, pp. 445-446).

In its submission to the RC, the ATO explained the extent and nature of cash payment activity in the construction industry; primarily as tax evasion. ATO audit activity between 1990 and 1995 “regularly identified undeclared cash payments to contractors, payments of cash to employees claiming social security benefits and undeclared cash payments for weekend work by employees legitimately employed on weekdays” (Cole 2003, vol. 9, p. 56). Starting in 1996, “the ATO conducted an Olympics project which examined activities on all Olympic related construction sites which uncovered undeclared cash payments, particularly to formworkers and steelfixers working on Olympic projects”. (Cole 2003, vol. 9, p. 56). Between 1997 and 1999 the ATO investigated “cash in hand” payments in labour intensive sub-industries and “undertook audit activity in the formworking and steelfixing sub-industries to identify cases involving untaxed cash payments to workers” (Cole 2003, vol. 9, p. 56). “Audits
completed on 13 formworkers and steelworkers identified untaxed cash payments in 11 of the cases” (Cole 2003, vol. 9, p. 56). This suggests a very high proportion of companies involved in tax evasion (85% in this example). “The cash payments were for overtime, RDO’s (rostered days off) and bonuses” (Cole 2003, vol. 9, p. 57). “In two cases, records were falsified by attempting to pass off cash payments as purchase of materials” (Cole 2003, vol. 9, p. 57).

The ATO’s Assistant Commissioner, Mr Ian Read, gave evidence to the RC that cash transaction analysis of banking industry data confirmed that “payment of cash is a common practice in the industry, particularly in the labour intensive sectors” (Cole 2003, vol. 9, p. 57). Analysis by the ATO in the period from July 2000 to September 2002 showed that “most cash transactions occur in New South Wales (54 per cent) followed by Victoria (22 per cent), with the rest of Australia making up the balance” (Cole 2003, vol. 9, p. 57). This information provided by the ATO identified the main industry sectors and locations of cash payment activity associated with tax evasion. It suggests that smaller companies, and even sole traders, were most involved. These types of companies would not have employed internal accountants and would probably limit their use of accountants to doing annual income tax returns. However, this still implicates external accountants, that is, chartered accountants who would have completed tax returns for these individuals who were engaged in tax evasion. Further, the complex contracting system within the construction industry meant that larger companies would have been involved in this type of activity because they would have been paying the smaller companies the cash payments. These larger companies would often employ internal accountants who may have been involved in classifying cash payments as something else, for example, purchasing materials or sponsorship.
The cooperation of companies and individuals to engage in unlawful activity was highlighted with widespread tax evasion within the construction industry. An example was fraudulent claims for GST Input Tax Credits. The ATO Assistant Commissioner Read gave evidence to the RC that the introduction of the GST in Australia represented an emerging risk in terms of tax evasion. ATO Assistant Commissioner Read gave this example of these schemes:

- Company A accumulates a tax debt. Company B is formed in anticipation of Company A being unable (or unwilling) to pay its debts.
- Company A sells its fixed assets to Company B at a reasonable market price. Tax invoices are provided. The type of assets transferred would include equipment.
- Company B claims the GST paid on the purchase price of the equipment as an input tax credit in the next BAS [Business Activity Statement] that it lodges with the ATO. This would ordinarily result in a refund of GST being paid to Company B, unless this amount was offset against some other tax liability of Company B.
- Company A may or may not lodge a BAS. In any event it simply adds the GST debt to the already growing list of debts it owes the ATO.
- Company B may not actually pay for the equipment despite what is indicated on tax invoices and other relevant documentation held by Company A and Company B.
- Company A uses the voluntary administration process as a safe refuge from its creditors.
- If the equipment is not paid for in full by Company B, and Company A goes into liquidation it is up to the liquidator to either recover the assets from Company B or chase the debt owed by Company B to Company A.
- If the ATO confirms that Company B has received a GST refund as a result of fraudulent intent, then action will be taken to recover the tax refunded and refer the matter for prosecution investigation.
- The obvious scenario may well be that Company B will have, or will claim to have, suffered some economic misfortune and will not be able to pay its debt to Company A or to the ATO.
- In time, Company B will fail and Company C will be formed to continue the cycle. (Cole 2003, vol. 9, p. 61).

In reviewing this example provided by the ATO Assistant Commissioner Read, the importance of cooperation between stakeholders can be seen in this unlawful activity. It shows how companies and unscrupulous individuals helped one another to avoid paying tax.
The third cultural behaviour found in stakeholders’ unlawful activities was a shared agreement on the need to cut costs. Given the small profit margins, some companies felt they could gain an edge over the competition by decreasing their expenses. A typical method for achieving this goal was to underpay employee entitlements. The RC found that construction companies avoided “the proper payment of employee entitlements to obtain a competitive advantage over businesses which comply with their obligations” (Cole 2003, vol. 8, p. 106). The inference was that companies had to engage in this unlawful activity, that is participate in this cultural norm, or risk having lost competitive advantage due to high costs.

The fourth cultural behaviour found in stakeholders’ unlawful activities was social dependence on financial viability. The complex nature of contracting within the construction industry means that companies depend upon one another for work. Large companies, that is, head contractors, will outsource parts of their construction projects to smaller companies, sub-contractors. Sub-contractors may also outsource part of their contract to other companies, which are their sub-contractors. Three themes emerged. The first theme was providing misleading financial information. This web of outsourcing creates business risk. A significant risk is whether the sub-contractor is paid for the work they complete for another company. In order to manage this risk, the construction industry uses a method called prequalification. “Prequalification involves assessing the financial viability and the capacity of firms to undertake various types of building and construction work” (Cole 2003, vol. 1, p. 113). This assessment assists clients and contractors to select firms for projects (Cole 2003, vol. 1, p. 113). “Prequalification can reduce the risk that the contractors chosen for the project will experience financial difficulty and then fail to pay subcontractors” (Cole 2003, vol. 1, p. 113).
The problem in the construction industry is that some unscrupulous individuals provide false information at prequalification which fails to disclose the true financial health of the company. This misleading information is designed to help the company win the contract. The RC described this problem as “the operation of ‘rogue’ builders who deliberately delay or avoid the payment of subcontractors” (Cole 2003, vol. 8, p. 231).

The second theme in this cultural behaviour was lack of capability to assess financial health. Many construction companies, particularly small companies, are led by individuals with limited business training or education. Many of these individuals are tradesmen who have set up their own business to provide a specific trade or other service. It would be challenging for many of these individuals to assess the financial health of other companies they deal with. Commissioner Cole found that many of these individuals “lack business and financial understanding” (Cole 2003, vol. 4, p. 98). It would be relatively easy for unscrupulous individuals to hide information or mislead others.

Commissioner Cole felt that the solution to this problem was education. He argued that “education and training would improve the expertise of subcontractors, and the ability of companies to assess the commercial risk of those they deal with” (Cole 2003, vol. 1, p. 115). He recommended that “the Commonwealth initiate an education campaign, aimed primarily at small subcontractors, to explain the Commonwealth’s security of payments arrangements and improve subcontractors’ understanding of the various mechanisms, including state mechanisms, which they can use to protect their interests and their understanding of their rights and obligations under common forms of contract” (Cole 2003, vol. 1, p. 115).
The third theme in this cultural behaviour was the construction industry’s complex contracting system created opportunities for unscrupulous individuals to exploit inadequate security of payments. Commissioner Cole explained that the hierarchical chain of contracts means that “non-payment of one subcontractor can affect payments to other subcontractors or suppliers down the contractual chain” (Cole 2003, vol. 3, p. 223). The financial failure of any one party in the contractual chain often caused a “domino effect” on other parties, which meant that inadequate security of payments had an impact that could spread throughout the industry.

The domino or knock-on effect of contracting within the construction industry created other problems. The RC found that security of payment problems were not confined to projects undertaken by rogue or insolvent builders, and they could “arise on projects involving some of the largest contractors in Australia” (Cole 2003, vol. 8, p. 231). The CCF submission to the RC stated that “unfortunately, tactics of deliberately delaying payments in this industry is not limited to rogue builders or head contractors in the industry and is now in fact common practice throughout the contract chain commencing with the client, and this in turn creates ever increasing cash-flow problems throughout the contract chain” (Cole 2003, vol. 8, p. 231). This explains that security payment was not restricted to those who could not pay, due to legitimate business failure, or who would not pay, such as rogue contractors, it also involved those who could pay but chose not because they had the power to do so. This latter group involved large successful construction companies which would certainly been able to provide security payment for any of their subcontractors, to demonstrate their capacity to pay for work. However, this group sometimes chose not to pay, perhaps to improve their cash flow or other financial goals, and to delay payment, that is, pay when they chose to rather than when the work was completed. They could do this because the small companies had
little funds to fight them in court, and they depended upon the larger companies for future work.

Commissioner Cole found that unscrupulous individuals were using “non-payment of existing claims as a bargaining tool to reduce subsequent claims” (Cole 2003, vol. 8, p. 231). These individuals were essentially exploiting non-payment in order for the small company to receive future work and the possibility of future payment.

In summary, the homogenous nature of the behaviour of social networks in the construction industry was found in a culture of unlawful behaviour. The analysis found that this culture was shaped by the complex contracting system. Owners/managers of construction companies at each stage of the system, that is head contractors (large companies), contractors (medium sized companies), and sub-contractors (small companies), tended to cooperate in cultural behaviours seen as the normal way of doing business. Failure to participate in these cultural behaviours often meant higher costs which placed companies at a serious competitive disadvantage in an industry with small profit margins.

5.2.3.3 Overall Social Network Cohesion

While at face value it may seem that the social networks within the construction industry’s contracting system achieved a sense of harmony via cooperation, it actually generated disharmony within the industry’s overall social network. This disharmony was caused by conflict with other stakeholders, particularly unions and regulators, who had different views and did not want to cooperate with the contracting system’s cultural behaviours. The outcome of this disharmony between the contracting system and other stakeholders was lack of democracy in the overall social network. Undemocratic
behaviours emerged in power differentials between stakeholders. This caused poor cohesion and inefficiencies in the network’s social behaviours. This was best illustrated by industrial disputes where one stakeholder, the unions, opposed the behaviours of other stakeholders, the owner/managers. Inefficiencies emerged in work delays and lost profitability. These problems can be examined by looking at the behaviours of the two most vocal opponents of the contracting system: unions and regulators.

The unions played a positive and negative role in shaping social behaviour within the construction industry. While the RC tended to focus on the negative behaviour of the unions, and painted the unions as the industry’s villains, the unions certainly played a positive role as well, particularly in acting as advocates for their members. The unions’ positive social behaviour occurred when advocating for their members to owners/managers, usually about employee entitlements; and in acting as a whistle-blower to the regulators to highlight injustices on behalf of their members. Unions negotiated favourable employment conditions for their members; such as increased wages to contractors’ employees’ entitlements and also increased wages for subcontractors’ employees. In both cases, the RC found that head contractors agreed to improved conditions as a means of avoiding costly industrial disputes (Cole 2003, vol. 5, p. 116). “Subcontractors employed the bulk of labour on a building site and consequently most of the costs associated with these favourable conditions were borne by subcontractors in the short term” (Cole 2003, vol. 5, p. 116). In the longer term these costs were passed onto the contractor and then onto the customer. This subtle distinction between the short term and long term cost burden is important because owner/managers could deny subcontractors’ employees their wages increase if they delayed or withheld payment (see processes 3c and 3d in figure A1.5 in appendix 1). The unions could play a positive role here by ensuring contractors met their obligations both for their own
employees, in relation to employee entitlements and for subcontractors’ employees, in the latter case by paying on time.

The unions also played a positive role as whistle-blower to the regulators. However, much of this was bluff. Transcripts of the RC hearings showed that union officials could only estimate the extent of tax evasion in the industry. When pressed for facts, documents or other evidence of these claims, the union officials typically used broad industry statistics to estimate the proportion of employers and subcontractors involved in tax evasion. When pushed further, officials often blamed the ATO for being uncooperative and either not acting on information forwarded by the unions or not providing the unions with information. The following extract illustrates this point:

Mr Bentleigh Carslake, President of the Construction, Forestry, Mining and Energy Union, Construction and General Division, South Australian Divisional Branch (CFMEU South Australian Divisional Branch), while complaining that public authorities, such as the ATO, are ineffective in dealing with tax evasion in the industry said that he had given away phoning the ATO about four years ago, apparently because nothing had changed as a result of the calls (Cole 2003, vol. 9, p. 54).

It may be argued that the unions had heterogeneous and democratic social behaviours in their social networks with their members. Union members would come from a diverse demographic background and often from different vocational groups and working for different organisations. Yet these differences were tolerated and a sense of belonging or union solidarity was encouraged. Similarly, unionism is based on collective decision making, for example communism, and decisions would have to be agreed to by members. The construction industry’s union movement, therefore, had the behaviours of harmony and cohesion.

The unions did not have the same type of social behaviour with other construction industry stakeholders; particularly owners/managers. When whistle-blowing for
members, union officials played a negative role by using tax evasion as a threat to intimidate and coerce employers. Union officials would threaten to tell the ATO about tax evasion if employers did not cooperate with them. The unions sometimes played the role of industry regulator. The RC heard evidence that union officials carried out audits of construction companies’ books in the self-appointed role of industry regulator. Officers of the CFMEU Victorian Building Unions Divisional Branch, Construction and General Division, carry out two different types of “audits” of various contractors, described as “wages claims” and “book audits” (Cole 2003, vol. 15, p. 55). When they contacted companies to be audited, union officials would fax a pro-forma which outlined the type of information they required for the audit. The pro-forma stated “that, if all of the material listed is not brought to the audit, the audit will not be started” (Cole 2003, vol. 15, p. 55). The 13 types of records required by the pro-forma for audit were:

1. Official wage records…
2. Cash payment book…
3. C+Bus Returns from…
4. Redundancy (Incolink) returns…
5. Long Service Leave (Co Invest) returns…
6. WorkCover payments from…
7. Payments to Taxation Office payee…
8. Reconciliation to Taxation PPS…
9. Cheque Butts…
10. Bank Statements…
11. Copies of Group Certificates – Financial year…
12. Delete Tax File No. [from any of the foregoing records]

These activities would have involved accountants to prepare and provide the information for audit. The union official had directed contractors who attended a book audit without all 13 types of records to leave and return with them (Cole 2003, vol. 15, p. 56).
An illustration of the coercive pressure placed on employers by unions acting as industry regulatory when conducting book audits is provided by the following case study found in the RCR:

Kenoss Contractors received two requests for time and wage book inspections from Primmer. The first time and wage book inspection took place on 13 April 2000 in response to a request made on 29 March 2000. Mr Peter Zaboyak, Assistant Secretary of the Construction, Forestry, Mining and Energy Union, Construction and General Division, New South Wales Divisional Branch, attended the inspection with Primmer on behalf of the CFMEU. Mr Frank Gillingham, Director Industrial Relations of the Master Builders Construction and Housing Association of the Australian Capital Territory, attended on Kenoss Contractors’ behalf, with Brendas and Mr Bruce Ford, Kenoss Contractors Pty Ltd site engineer for the Moruya project. Also in attendance were Brown and Mr Andrew Burns of Allied Constructions Pty Ltd. Throughout the inspection, Primmer and Zaboyak were generally aggressive and threatening. At one point, Zaboyak said words to the effect, ‘You’ll never get any work in NSW. The NSW Government will never give Kenoss any work. I will call the taxation department. I’ll call the Long Service Leave Board. I’ll call superannuation and workers’ compensation. We’ll get a subcontractors’ compensation audit. We’ll make you pay back pay for all the contractors as though they were employees.’ After the meeting ended, Zaboyak came up to Brendas and spoke to him in a quiet and friendly voice. Zaboyak told Brendas that if Kenoss Contractors signed an EBA, the company would not have any more problems (Cole 2003, vol. 19, p. 353).

Commissioner Cole found that this case study illustrates:

a. the unauthorised and unnecessary stoppage of work by a union organiser;

b. the continuous and unrelenting campaign by a union organiser to have a contractor sign a union-endorsed EBA. The campaign included:
   (i) repetitive wage book inspections;
   (ii) the raising of safety allegations;
   (iii) the threat to report the company to taxation, insurance, workers’ compensation and other authorities;
   (iv) the threat to prevent the company from obtaining work in New South Wales;
   (v) stoppage of work; and

   (vi) the threat to a head contractor engaging the contractor that it would be responsible for moneys allegedly not paid by the contractor (Cole 2003, vol. 19, p. 358).

The case also illustrates the responsiveness of employers to the pressure applied by a union official. This pressure was described as ‘unrelenting, by Commissioner Cole.
The regulators opposed the cultural behaviours associated with unlawful activity in the construction industry. However, they were heavily criticised for not sufficiently engaging with other industry stakeholders. Commissioner Cole was critical of the lack of regulation of several unlawful activities conducted by the construction industry. For example, security of payments was a particular problem in the construction industry. Earlier it was shown how Commissioner Cole portrayed small companies as powerless victims of inadequate security of payments. One way to give victims power is appropriate opportunities to pursue legal action. However, Commissioner Cole argued that the security of payment problem in the construction industry was “exacerbated by the absence of an effective adjudication and enforcement mechanism in relation to disputes over progress payments, and the high cost and long delay in pursuing payment claims through the court system” (Cole 2003, vol. 3, p. 223). Given the companies who were victims of inadequate security of payments were often too small to be able to fight larger companies in the courts, this meant that few would bother to take legal action.

5.3 Accountants Behaviour

In analysing the behaviour of accountants within the construction industry’s social networks, the focus is on the accounting practices associated with unlawful behaviour identified by the RC. As noted in section 5.1 of this chapter, the RC found the following unlawful activities which may have involved accounting practice: (1) tax evasion, (2) underpayment of employee entitlements, (3) non-compliance with payroll tax, (4) creation of phoenix companies, (5) making of and receipt of inappropriate payments, (6) absence of adequate security of payments for sub-contractors, and (7) profit manipulation. The analysis is to examine accounting practice within the context of these
seven activities. That is, it to identify whether accountants were involved in these activities, and if so, to what extent; and who they interacted with in these activities.

The following table presents the characteristics in respective categories from the analyses. Section 1.5.3 (see chapter 1) explained how these codes were derived. These business processes are listed in the table. Only unlawful activities and their processes are included in the analysis. The numbers are part of the numbering for the total processes involved in each activity such as tax evasion. These are listed in the figures in appendix 1. The processes listed in the table below are only the unlawful processes involving accountants.
## Table 5.2: Accountants’ Behaviour in Construction Industry Social Networks

<table>
<thead>
<tr>
<th>Process</th>
<th>Interaction</th>
<th>Harmony</th>
<th>Cohesion</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Tax Evasion (see figure A1.1)</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2a. Treatment of tax losses</td>
<td>High density - Lead</td>
<td>Heterogeneity - Respect</td>
<td>Democratic Expert -</td>
</tr>
<tr>
<td>3a. Minimising tax payments</td>
<td>High density – Lead</td>
<td>Heterogeneity - Respect</td>
<td>Democratic Expert -</td>
</tr>
<tr>
<td>3b. Revaluation of non-current assets</td>
<td>High density – Lead</td>
<td>Heterogeneity - Respect</td>
<td>Democratic Expert -</td>
</tr>
<tr>
<td>3c. Offsetting deferred tax assets</td>
<td>High density – Lead</td>
<td>Heterogeneity - Respect</td>
<td>Democratic Expert -</td>
</tr>
<tr>
<td>3d. Offsetting deferred tax liabilities</td>
<td>High density – Lead</td>
<td>Heterogeneity - Respect</td>
<td>Democratic Expert -</td>
</tr>
<tr>
<td>3e. Making tax payments</td>
<td>High density – Lead</td>
<td>Heterogeneity - Respect</td>
<td>Democratic Expert -</td>
</tr>
<tr>
<td><strong>Employee Entitlements (see figure A1.2)</strong></td>
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<td></td>
</tr>
<tr>
<td>1b. Record entitlements in income statement as an expense</td>
<td>Low density - Alone</td>
<td>Heterogeneity - Respect</td>
<td>Democratic Expert -</td>
</tr>
<tr>
<td>1c. Manipulate entitlements to lower expenses</td>
<td>High density – Lead</td>
<td>Heterogeneity - Tolerance</td>
<td>Democratic Expert -</td>
</tr>
<tr>
<td>1e. Declaring insolvency to avoid payments of entitlements</td>
<td>High density – Lead</td>
<td>Heterogeneity - Tolerance</td>
<td>Democratic Advisor -</td>
</tr>
<tr>
<td><strong>Payroll Tax(see figure A1.3)</strong></td>
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</tr>
<tr>
<td>1a. Recognise the payroll tax liability</td>
<td>Low density - Follow</td>
<td>Heterogeneity - Respect</td>
<td>Democratic Expert -</td>
</tr>
<tr>
<td>1b. Calculate threshold figure</td>
<td>Low density - Alone</td>
<td>Heterogeneity - Respect</td>
<td>Democratic Expert -</td>
</tr>
<tr>
<td><strong>Inappropriate Payments(ss figure A1.5)</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>1b. Identify supplier invoice</td>
<td>Low density - Alone</td>
<td>Heterogeneity - Respect</td>
<td>Democratic Expert –</td>
</tr>
</tbody>
</table>
Table 5.2: Accountants’ Behaviour in Construction Industry Social Networks

<table>
<thead>
<tr>
<th>Process</th>
<th>Interaction</th>
<th>Harmony</th>
<th>Cohesion</th>
</tr>
</thead>
<tbody>
<tr>
<td>1c. Match invoice with purchase order from purchasing department</td>
<td>Low density - Alone</td>
<td>Heterogeneity - Respect</td>
<td>Democratic Expert</td>
</tr>
<tr>
<td>1d. Check proof that goods have been received from receiving department</td>
<td>Low density - Alone</td>
<td>Heterogeneity - Respect</td>
<td>Democratic Expert</td>
</tr>
<tr>
<td>1e. Authorize payment</td>
<td>Low density - Alone</td>
<td>Heterogeneity - Respect</td>
<td>Democratic Advisor</td>
</tr>
<tr>
<td>2b. Transfer funds from the company to the supplier</td>
<td>Low density - Alone</td>
<td>Heterogeneity - Respect</td>
<td>Democratic Expert</td>
</tr>
<tr>
<td>2c. Record as an expense on the income statements</td>
<td>Low density - Alone</td>
<td>Heterogeneity - Respect</td>
<td>Democratic Expert</td>
</tr>
<tr>
<td>2d. Record as a cash outflow on the cash flow statements</td>
<td>Low density - Alone</td>
<td>Heterogeneity - Respect</td>
<td>Democratic Expert</td>
</tr>
</tbody>
</table>

Phoenix Company Activity (see figure A1.4)

<table>
<thead>
<tr>
<th>Process</th>
<th>Interaction</th>
<th>Harmony</th>
<th>Cohesion</th>
</tr>
</thead>
<tbody>
<tr>
<td>1c. Voluntary closure: bankruptcy</td>
<td>High density - Follow</td>
<td>Homogeneity - Outsider</td>
<td>Democratic Advisor</td>
</tr>
<tr>
<td>2a. Assets transferred to the new company</td>
<td>High density - Follow</td>
<td>Heterogeneity - Tolerance</td>
<td>Democratic Expert</td>
</tr>
<tr>
<td>3a. Liabilities of the failed company NOT paid to creditors</td>
<td>High density - Follow</td>
<td>Heterogeneity - Tolerance</td>
<td>Undemocratic Challenged</td>
</tr>
<tr>
<td>4a. Avoid punishment from creditors</td>
<td>High density - Follow</td>
<td>Homogeneity - Outsider</td>
<td>Democratic Advisor</td>
</tr>
</tbody>
</table>

Security of Payments (see figure A1.6)

<table>
<thead>
<tr>
<th>Process</th>
<th>Interaction</th>
<th>Harmony</th>
<th>Cohesion</th>
</tr>
</thead>
<tbody>
<tr>
<td>1a. Financial performance</td>
<td>High density - Follow</td>
<td>Homogeneity - Enemy</td>
<td>Undemocratic Challenged</td>
</tr>
<tr>
<td>1c. Prequalification scrutiny</td>
<td>High density - Follow</td>
<td>Homogeneity - Enemy</td>
<td>Undemocratic Challenged</td>
</tr>
<tr>
<td>2a. Recovering payments</td>
<td>High density - Follow</td>
<td>Homogeneity - Enemy</td>
<td>Undemocratic Challenged</td>
</tr>
<tr>
<td>2b. Code of practice</td>
<td>Low density - Alone</td>
<td>Homogeneity - Enemy</td>
<td>Democratic Expert</td>
</tr>
<tr>
<td>Table 5.2: Accountants’ Behaviour in Construction Industry Social Networks</td>
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</tr>
<tr>
<td><strong>Process</strong></td>
<td><strong>Interaction</strong></td>
<td><strong>Harmony</strong></td>
<td><strong>Cohesion</strong></td>
</tr>
<tr>
<td>Profit Manipulation (see figure A1.7)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2a. Exceptions to accounting standards</td>
<td>Low density - Alone</td>
<td>Homogeneity - Enemy</td>
<td>Democratic Expert</td>
</tr>
<tr>
<td>2d. Falsely representing the long-term capacity of the firm to generate earnings</td>
<td>High density – Follow</td>
<td>Homogeneity - Outsider</td>
<td>Undemocratic Challenged</td>
</tr>
<tr>
<td>3a. Creative accounting</td>
<td>High density – Lead</td>
<td>Heterogeneity - Respect</td>
<td>Democratic Expert</td>
</tr>
<tr>
<td>3b. Differences between book and tax profits</td>
<td>High density – Lead</td>
<td>Heterogeneity - Respect</td>
<td>Democratic Expert</td>
</tr>
<tr>
<td>3c. Impression management</td>
<td>High density – Follow</td>
<td>Homogeneity - Outsider</td>
<td>Democratic Advisor</td>
</tr>
<tr>
<td>3d. Accrual accounting: delaying expenses</td>
<td>High density – Follow</td>
<td>Heterogeneity - Respect</td>
<td>Democratic Expert</td>
</tr>
<tr>
<td>4a. Fraud</td>
<td>Low density - Follow</td>
<td>Homogeneity - Outsider</td>
<td>Undemocratic Ignored</td>
</tr>
<tr>
<td>4b. Falsifying or altering documents</td>
<td>Low density - Follow</td>
<td>Homogeneity - Outsider</td>
<td>Undemocratic Challenged</td>
</tr>
<tr>
<td>4c. Deleting transactions from records</td>
<td>Low density - Follow</td>
<td>Homogeneity - Outsider</td>
<td>Undemocratic Challenged</td>
</tr>
<tr>
<td>4d. Recording forged transactions</td>
<td>Low density - Follow</td>
<td>Homogeneity - Enemy</td>
<td>Undemocratic Challenged</td>
</tr>
<tr>
<td>4e. Concealing significant information</td>
<td>Low density - Follow</td>
<td>Homogeneity - Outsider</td>
<td>Undemocratic Challenged</td>
</tr>
</tbody>
</table>
High density – Lead; Heterogeneity – Respect; Democratic - Expert

Social networks with these characteristics are situations where the accountant initiates interaction, where the accountant’s participation is valued by other stakeholders, and where the accountant’s opinion is more important than any other stakeholders. In this type of social network, the accountant would have a strong influence in controlling the behaviour of other stakeholders involved in the activity. Therefore, unlawful behaviour would have been allowed by the accountant. There are six processes which have these characteristics (16% of all unlawful processes listed in table 5.2). Four of these processes are in tax evasion (2a, 3b, 3c, and 3d) (66% of this activity’s processes); and two are in profit manipulation (3a and 3b) (19% of this activity’s processes). Common to these processes is that they are all core accounting work.

The following table presents a simple classification of the work accountants do.

<table>
<thead>
<tr>
<th>Table 5.3: The Process of Accounting</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Identifying</strong></td>
</tr>
<tr>
<td>Transactions that affect the entity’s financial position are taken into consideration. They must be able to be reliably measured and recorded</td>
</tr>
</tbody>
</table>

Source: (Birt, Chalmers, Byrne, Brooks & Oliver 2010, p. 5).

Using this table, the tax evasion activities are mainly measuring, and the profit manipulation activities are mainly communicating. The measurement role mainly involved classification of assets with the aim of reducing the amount of tax payable. In the communication role, the accountant needs to consolidate financial information and produce regular reports (Birt et al. 2010). Therefore, if the accountant was involved in
unlawful behaviour associated with these activities, it mainly involved financial reporting.

When the processes characterised by this behaviour are examined, it is clear that only accountants are qualified to do this type of work. Therefore, accountants would have assumed a leadership role in social networks involved in these unlawful activities because others depended upon them to do this work. This has implications for this study in the examination of the role of accounting. Given the nature of the social behaviour in processes with these characteristics, accountants were heavily involved in these unlawful activities. Given the nature of these activities, the decision makers must have sought the involvement of accountants. The question then emerges: did accountants respond by telling decision makers that they must follow accounting standards at all times? If so, this would support the argument for accounting as objective practice. Or did accountants respond by doing creative accounting to help their employers’ goals? If so, this would support the argument for accounting as subjective practice. In order to examine these questions further, some of the processes are discussed in more detail.

The role of accountants in the processes associated with tax evasion will vary depending upon two factors: firm size and the nature of the activity. As discussed in chapter 3, the construction industry is divided into large firms, known as head contractors, and small firms, known as sub-contractors. In large firms routine matters would typically be handled by an accountant, and more complex matters by a tax expert, sometimes an internal staff member but often an external expert from a taxation firm or accounting firm. Small firms would not employ a full-time accountant, nor tax expert, so both routine and complex matters would be referred to external experts. This implicates external accountants who would have led social networks associated with complex taxation matters for all firms, and also routine matters for small firms.
Profit manipulation involved nine of the unlawful processes listed in table 5.2. Of these, only two: 3a. creative accounting and 3b. differences between book and tax profits, had the characteristics of high density – lead; homogeneity – respect; democratic – expert. Creative accounting was the domain of the accountant. Whereas other stakeholders may have asked accountants to ‘be creative’ in the way they identified, measured and communicated the numbers, how they did it was up to the accountant. On the other hand, companies report book and tax profits differently because they are communicating to different audiences. This is a common accounting activity and accountants would have led this activity as a part of normal way of doing their work. Where the social behaviour becomes suspicious is when the process was to manipulate rather than report profit.

Profit manipulation includes falsifying information and trying to mislead readers of financial reports. In this case, whereas owner/managers may have directed accountants to manipulate differences between book and tax profits, only the accountant would have known how to do this. Given this process is classified in this behaviour, accountants would have taken the lead role, which implicates them, and provides further evidence for accounting as a subjective process. This activity provides evidence of subjective accounting.

*High density – Follow; Heterogeneity – Respect; Democratic - Expert*

Social networks with these characteristics are situations where the accountant responds to a request from others to interact, where the accountant’s participation is valued by other stakeholders, and where the accountant’s opinion is more important than any other stakeholders. In this type of social network, the accountant would have some influence in controlling the behaviour of other stakeholders involved in the activity. Therefore, unlawful behaviour would have been tolerated by the accountant. There are three processes which have these characteristics (8% of all unlawful processes listed in table 5.2).
5.2). Two of these processes are in tax evasion (3a and 3e) (33% of this activity’s processes); and one is in profit manipulation (3d) (9% of this activity’s processes). Using table 5.3 again to classify these processes in terms of accounting practice, the tax evasion activities are decision making, and the profit manipulation activity is about measurement. In decision making, the accountant provides information to assist owners/managers to take action. In this case, it was to evade tax. In measurement, the accountant delayed expenses to help improve the financial position.

The reason why accountants played a reactive role in social networks involved in these unlawful activities, despite it being accounting work, was that these processes were not routine or normal accounting practice. While it may be argued that minimising tax and making tax payments are routine accounting tasks, unlawful behaviour in these areas would have been led by others, for example owners/managers. It is unlikely that an accountant would seek to minimise tax or delay expenses on their own initiative. It is more likely they would be directed to do so. Given the widespread tax evasion in the construction industry and the RC’s finding that this activity was unlawful, accountants must have been directed to provide information to assist owners/managers in this activity. Similarly, while accrual accounting is normal accounting practice, doing it for the purposes of profit manipulation would have been initiated by others, for example owners/managers, and would not have been routine accounting practice. This activity provides evidence of subjective accounting.

*High density – Follow; Heterogeneity – Tolerance; Democratic - Expert*

Social networks with these characteristics are situations where the accountant responds to a request from others to interact, where the accountant’s participation is tolerated by other stakeholders, and where the accountant’s opinion is more important than any other
stakeholders. In this type of social network, the accountant would have little influence in controlling the behaviour of other stakeholders involved in the activity. Therefore, while unlawful behaviour may have been discouraged by the accountant, this would have had little effect. There are two processes which have these characteristics (5% of all unlawful processes listed in table 5.2). One of these processes is in employee entitlements (1c) (33% of this activity’s processes); and one is in phoenix company activity (2a) (25% of this activity’s processes). Using table 5.3 again to classify these processes in terms of accounting practice, the employee entitlement activity is about identifying, and the phoenix company activity is about decision making.

The first process, 1c. manipulating entitlements to lower expenses, would have required the accountant to identify business transactions, specifically payment of wages and salaries. If the owner/managers were not paying wages and salaries at the correct rate, it is not the accountant’s role to challenge this decision. It is likely accountants would respond to a request for information, their advice would be tolerated, and they would be asked to amend expenses because that was part of their job.

The second process, 2a. assets transferred to a new company, would have required reporting on the balance sheet (BS). Commissioner Cole reported on how companies did this to avoid paying GST. In this case, accountants would have been asked to do the assets transfer. If the accountant challenged the decision, it is likely they would have been tolerated due to their expert status. It is likely that accountants would have been heavily involved in this activity because it required financial skills and capabilities. As this activity was considered unlawful by the RC, it implicates accountants and is further evidence of the subjective role of accounting.
Given that process 1c. manipulating entitlements to lower expenses was the process with the most scope for unlawful behaviour associated with employee entitlements, further analysis is presented in this section. The analysis has shown that the recording of entitlements was identified as an activity where unlawful behaviour could occur (see process 1b in figure A1.2 in appendix 1). The analysis suggested that employee entitlement should be recorded as an expense on the income statement (IS). However, employee entitlement liabilities might also be recorded as provisions in BS’s (Davis & Burrows 2003). Non-accountants may interpret this action as reserving specific assets or cash flows to meet the eventual claims. However, these provisions simply represent claims against assets in general and are vulnerable to any reduction in asset values in the event of financial trouble (Davis & Burrows 2003).

Employee entitlements might be classified as a source of company finance, particularly of working capital (see measuring business transactions: classifying, in table 5.3). Davis and Burrows (2003) argued that employee entitlements are a cheap source of funding. Like trade credit, entitlements ostensibly represent a free source of capital, that is, they are available at a zero explicit interest rate (Davis & Burrows 2003). However, this ignores the impact of nominal-wage growth (Davis & Burrows 2003). Davis and Burrow (2003, p.174) provide an example of a week of long service leave which accrues in year 0 but which is taken in year 10, will be paid at the remuneration level applying in year 10. “Hence, the implicit cost of entitlements as a source of capital (and equivalently, the rate of return to the providers of such finance) is approximately the annual rate of remuneration growth” (Davis & Burrows 2003, p. 174). Davis and Burrows are explaining how employee entitlement, long service leave in this example, still has a cost, although it is still a very inexpensive source of capital compared to other forms of debt.
De Fazio (2009) argues that there are differences in financial and taxation accounting, which may explain why accountants had limited involvement in tax evasion associated with the construction industry. The following is an extract from De Fazio (2009) which explains the subjective nature of accounting, more specifically, the role accountants typically play in some of the seven unlawful activities, particularly tax evasion, profit reporting, and employee entitlements:

Financial and tax accounting both record income and expenses over a period of time to arrive at some measure of profit. However, despite this commonality, there is a significant lack of conformity between the two measures of profit determined under both the systems. In fact, studies have indicated profit discrepancies amounting to billions of dollars. In a number of countries, especially within Europe, the tax accounting system has to some extent been aligned with the financial accounting system; however, in Australia, the two systems remain independent of each other. Nonetheless, the desire for conformity and the inevitable divergence of the two systems has been the topic of much debate over the years. The matter has been described by researchers as "perennial and pervasive - perhaps even eternal and universal". However, what has emerged from the literature is a set of generally accepted reasons which explain why the two systems will treat the same transaction or event in two completely different ways. The primary reason is that the two systems have different objectives; other reasons relate to the principles and practices which are used to ensure these overall objectives are achieved, including the different levels of discretion allowed by both systems and the different methods used to allocate income and expenses to the correct accounting period (p. 29).

This extract provides several themes which may be used to explore accountants’ role in employee entitlement avoidance and in tax evasion. First, identify the goals of the organisational systems, that is, stakeholder interaction. Second, identify the level of discretion available to accountants by accounting principles and standards. Third, identify the method for allocating income and expenses in terms of employee entitlement. This next extract from De Fazio (2009) provides further insight:

The level of discretion permitted in the systems is the next reason considered to explain why certain transactions are dealt with differently under the two regimes. The rules of financial accounting are incapable of producing a single profit figure because they allow accountants a considerable degree of discretion; therefore, different accountants may arrive at different figures. There are several qualitative
characteristics which are fundamental to financial accounting. Due to the nature of these characteristics, accountants are often required to reach a trade-off between them - a balancing exercise which is largely a matter of professional judgment. In tax accounting there is a requirement to derive one single figure on which to base an assessment, and it is therefore an inherent requirement that a higher level of precision and certainty exists. Once a taxpayer is assessed and his/her tax liability determined for a period, it is essentially of a conclusive nature and will be subject to a reassessment only in limited cases. Especially in light of the fact that tax laws result in compulsory tax obligations upon taxpayers, the inherent uncertainty of financial accounting is both "undesirable and inappropriate in the context of the enforced confiscation of property". This need for greater certainty is further enforced in light of the fact that fines and penalties can be imposed upon taxpayers who get it wrong (p. 31).

This extract provides several further themes for analysis in the role of accountants in unlawful activity associated with tax evasion and employee entitlements. First, financial accounting is described as “qualitative” (De Fazio 2009, p. 31). This word suggests a level of interpretation and judgment used by accountants to report on numbers, in other words, subjectivity. Second, tax accounting is described as requiring “precision” and “certainty” (De Fazio 2009, p. 31). These words suggest a level of accuracy by accountants and objectivity. It requires accuracy because of the consequences of mistakes, such as fines. Third, financial accounting’s “inherent uncertainty” (De Fazio 2009, p. 31) is seen as a bad thing; “undesirable and inappropriate” (De Fazio 2009, p. 31). De Fazio (2009) is arguing that accounting should be objective and subjective accounting is poor practice. She also highlights the inherent problem in objective accounting, here represented as tax accounting, and subjective accounting, here represented as financial accounting: the possibility of arriving at two separate numbers or set of accounts based on the same raw financial data. If accounting is to assist the construction industry restore society’s confidence, the public must trust their numbers and their reporting of financial data.

This next extract from De Fazio (2009) examines the role of accountants and employee entitlements:
Employee leave entitlements are also generally recognised as a liability and expense within the financial statements of an entity to the extent they are probable, capable of a reliable estimate and relevant for the decision-making needs of users. However, unlike accounting for warranties, employee leave entitlements are not classified as provisions; rather, they are accruals, another classification of liabilities. Accruals are distinctly different from provisions because, although some estimation may be required in terms of the amount and timing, financial accounting considers that there is not the same level of uncertainty as that inherent in provisions (p. 34).

This extract defines employee entitlements in terms of leave. It explains how accountants typically treat employee leave entitlements as accruals or a liability. It also suggests a defence of subjective accounting in the estimation of employee leave entitlements by claiming they do not require the same level of certainty as provisions because they are placed in accruals.

De Fazio (2009) next looks at employee leave entitlements in more detail:

Two types of leave entitlements will be considered. The first is short-term leave which falls due within 12 months after the period in which the employee renders the related service - this includes annual leave and sick leave. The other is long-term employee benefits which do not fall due within a 12-month period and which include long-service leave. Short-term employee benefits may be either accumulating or non-accumulating. Accumulating leave will include amounts which may be carried forward to subsequent periods when the employee has any unused amounts. Accumulating leave may in turn be vesting or non-vesting - in both cases, as the employee renders the related service, an obligation generally arises which leaves the entity with a present liability and therefore both an accrual and expense must be accounted for. Accumulating vesting leave is unconditional and therefore will entitle the employee to a cash payment equal to the accumulated leave when they cease employment - it is appropriate to account for the entire amount of this leave as an accrued liability and as an expense. The progressive entitlement to the leave is an additional cost of employment; as the employee renders service to the entity, his/her entitlement to the leave increases and becomes an irrevocable obligation upon the entity. Thus, it is probable that the entity will be required to make a payment in the future upon the employee using the leave or upon his/her resignation (p. 34).

This extract highlights the significance of employee leave entitlements as a cost of doing business. Long-term leave, such as leave accumulated over more than twelve months, can represent a very significant cost. Organisations often try to persuade employees to
take their annual leave so that it does not accumulate. If this leave does accumulate, organisations can be liable to pay employees substantial funds if they resign or retire. These may be funds the organisation does not have available, particularly in the case of construction industry companies who may be operating under severe financial constraints.

The next extract from De Fazio (2009) looks at how accounting standards are meant to treat employee leave entitlements:

In terms of the accounting treatment of long-service leave, it is practical to consider the former guidance section which was part of the accounting standard AASB 119 Employee Benefits, where three categories of long-service leave entitlements are identified:

1. Pre-conditional period: This period will not create a legal entitlement for long-service leave. Therefore, if the employee ceases employment during this period, he/she will not receive any benefit in relation to this type of leave.
2. Conditional period: Following from the pre-conditional period, the employee will now have an entitlement to long-service leave, accrued from the commencement of employment. Although the employee is not eligible to take long-service leave during this period, he/she is entitled to a payout of any accrued amounts upon ceasing employment.
3. Unconditional period: At this stage, the employee is entitled to use his/her long-service leave. If he/she ceases employment during this period, like the conditional period, he/she will receive payment for any accrued entitlements (p. 35).

The extract provides guidelines in terms of how to classify employee leave entitlements, in this case long service leave, and then how to treat these classifications in terms of accrual accounting. It is quite straightforward and accountants who follow it may simply be classifying employees into one of these three time periods. This suggests the accrual accounting of employee leave entitlements should be objective because the accounting standards are unambiguous and do not need much interpretation or judgment. This raises the questions of why these standards were not always followed and why accrual accounting of employee leave entitlements became a subjective practice in the construction industry.
De Fazio (2009) next examines these questions:

Similar to the financial accounting of short-term employee benefits discussed above, long-service leave is also recognised for the periods in which the employee provides service to the entity; the rendering of service is taken to give rise to a liability even when the benefit is non-vesting, as is the case during the pre-conditional period. These amounts of leave are conditional upon the employee's future employment. However, they still give rise to a constructive obligation because, after each successive reporting date, the future service that the employee will have to render for the entitlement to be vested is reduced. It is required that the entity factor into the calculation of accrued long-service leave the fact that some employees may never reach the vesting stage. This, however, will only affect the measurement of the obligation and not whether a present liability is taken to exist. The ultimate payment associated with long-service leave is based on the salary of the employee at the time the leave is taken or, alternatively, paid out. Most of the time this, will not equal to the salary of the employee at the time when the benefit accrues to them. Therefore, projections must be made in respect of future salary rates, inflation rates and any promotion prospects. Further, there is a requirement to measure and recognise long-service leave at its present value - thus a consideration must be made as to the appropriate discount rate to use. The reliability aspect of recognition is met with short-term employee benefits without the need to apply actuarial assumptions or discounting since it is appropriate to base measurement on current salary rates. However, there is still a requirement, as already stated, to factor in the possibility that the employee may not continue employment and thus his/her entitlement to accumulating non-vesting leave (p. 35).

This extract explains how the accrual accounting of employee leave entitlements is not as straightforward as the accounting standard suggests. The reality of accounting practice associated with this activity is quite complex. There is considerable need for judgement and interpretation suggesting a need for subjective accounting. Judgements must be made about the proportion of employees who reach the various time periods, referred to as the ‘vesting stage’, the likely salary of these employees when they wish to take leave, the proportion of employees who will leave and take their entitlements with them. Some might even call this guess work. It certainly requires subjective opinion and allows opportunity for arriving at different numbers or creative accounting. It also creates opportunity for unscrupulous individuals to persuade accountants to make incorrect judgements leading to unlawful behaviour and ultimately denial of employees’
rights to leave payments. This could happen when unscrupulous individuals tell employees they cannot afford to pay their leave because they did not put enough funds aside.

Accountants would be unlikely to be involved in negotiating salary or non-salary entitlements for employees. These negotiations would most typically involve managers, human resources, and unions. In this case, it is unlikely that accountants were involved in this unlawful behaviour, other than to record the outcome of negotiations as an expense on the IS. In most activities associated with this matter, accountants would probably have followed accounting rules, that is the accounting standards. However, some of the processes involved in the employee entitlements process generate doubt about the role of accountants. While accountants are unlikely to have been involved in negotiations about levels of employee entitlements or whether this was applied equitably, they would have been involved in activities associated with identifying, measuring and reporting financial transactions associated with employee entitlements. After all, this is the work that accountants do. The issue is how much involved were they in unlawful behaviour associated with this activity.

Our first clue is to look at the type of information accountants provided to others associated with underpaying employee entitlements, that is, company directors. The Corporations Act 2001 provides guidance on how directors must act if a responsible person gives them information to suspect insolvency. The responsible person, in this case, must be accountants. This provides evidence of the social practice of insolvency and the role of the accountant. In section 588H (2) of the Corporations Act 2001, company directors are provided with several defences to protect them against legal action for not paying employee entitlements. Firstly, there is a defence if the director can prove that, at the time the debt was incurred, “the director had reasonable grounds to
expect (and did expect) that the company was solvent and would remain so” (Symes 2003, p. 138). It is important to note that the legislation uses the phrase “reasonable grounds to expect solvency” and not “reasonable grounds to suspect insolvency” (Corporations Act 2001, s. 588H (2)). This means that the director should have information that he/she could trust. The director is not expected to guess or suspect; they are only expected to know or expect. This language is important because it places more responsibility on the provider of the information, the accountant, rather than the director. It is the role of the accountant to ensure the director knows rather than guesses that the company is solvent. It also suggests an escape clause for directors to avoid their responsibilities in terms of employee entitlements. They can blame their accountants for not making them fully aware of the company’s financial position.

The second clue, and the director’s second defence provided by the Corporations Act 2001, is if he/she had “reasonable grounds to believe and did believe that a competent and reliable person was responsible for providing the director with adequate information about whether the company was solvent (s588H(3))” (Symes 2003, p. 139). This language is important in establishing a power differential in the relationship between the directors and accountants. It essentially provides legislative authority for company directors to assess the competence of accounting staff; whether employed by the director as full-time staff (internal accountant) or as an accounting consultant (external accountant). The words “competent and reliable person” place authority with the director to assess the ability of the accountant to provide trustworthy information. The following phrase “adequate information” is also loaded with power allocated to the director. The director may use this to argue their accountant was incompetent and provided inadequate accounting information, therefore laying blame on the accountant, and avoiding responsibility for underpaying employee entitlements.
The third clue, and the director’s third defence provided by the *Corporations Act 2001*, is whether “that other person was fulfilling that responsibility” (s588H (3), Symes 2003, p. 139). Once again, this language provides evidence of the power allocated to company directors over accounting staff in managing employee entitlements and in insolvency activities. The phrase “fulfilling that responsibility” invests company directors with the scope to evaluate how well the person providing them with financial information, that is, the accountant, was doing their job. In summary, the legislation not only gave directors three escape clauses to avoid their responsibilities in regards to employee entitlements, it placed responsibility with accountants and directors with authority to evaluate the quality of accountants’ information, their competence, and their performance.

In summary, accountants would have been involved in work associated with the employee entitlements process. There are three specific employee entitlements processes that were unlawful and involved accountants:

- 1b. Record entitlements in the IS as an expense.
- 1c. Manipulate entitlements to lower expenses
- 1e. Declaring insolvency to avoid payments of entitlements

More specifically, recording entitlements as an expense would have been reporting on the IS. Manipulating entitlements to lower expenses would have required identifying business transactions, specifically payment of wages and salaries. Declaring insolvency to avoid payments of entitlements would have involved decision making about paying debts. This activity provides evidence of subjective accounting.

*High density – Follow; Heterogeneity – Tolerance; Democratic - Advisor*

Social networks with these characteristics are situations where the accountant where the accountant responds to a request from others to interact, where the accountant’s
participation is tolerated by other stakeholders, and where the accountant’s opinion is advice. In this type of social network, the accountant would have little influence in controlling the behaviour of other stakeholders involved in the activity. Therefore, while unlawful behaviour may have been discouraged by the accountant, this would have had little effect. There is one process which has these characteristics (3% of all unlawful processes listed in table 5.2). This process is in employee entitlements (1e) (33% of this activity’s processes). Using table 5.3 again to classify these processes in terms of accounting practice, the employee entitlement activity is about decision making.

The process, 1e. declaring insolvency to avoid payments of entitlements, would have involved decision making about paying debts. This decision would be made by owners/managers. Accountants’ involvement would have been to advise on whether the company was solvent, and also to provide figures on employee entitlements liabilities. It is unlikely that accountants would have contributed to decisions to deliberately wind the company up in order to avoid paying employees. Therefore, it may be concluded this activity is evidence of objective accounting. However, as discussed in the previous section, activities associated with employee entitlements provide scope for creative accounting and subjectivity.

High density – Follow; Heterogeneity – Tolerance; Undemocratic - Challenged

Social networks with these characteristics are situations where the accountant responds to a request from others to interact, where the accountant’s participation is tolerated by other stakeholders, and where the accountant’s opinion is disputed by other stakeholders. In this type of social network, the accountant would have very little influence in controlling the behaviour of other stakeholders involved in the activity. Therefore, while unlawful behaviour may have been challenged by the accountant, this would have had
little effect. There is one process which has these characteristics (3% of all unlawful processes listed in table 5.2). This process is in phoenix company activity (3a) (25% of this activity’s processes). Using table 5.3 again to classify these processes in terms of accounting practice, the employee entitlement activity is about decision making.

The process, 3a. Liabilities of the failed company not paid to creditors, would have involved decision making about paying debts. This decision would be made by owners/managers. Accountants’ involvement would have been to provide information about liabilities and creditors. It is unlikely that accountants would have agreed with decisions not to pay creditors as it would seem unethical, and objections by accountants would have been challenged by owners/managers. Therefore, it may be concluded this activity is evidence of objective accounting. Accountants engaging in this practice would have clearly stepped over the boundary from creative accounting to unethical behaviour and would have been aware of these boundaries.

High density – Follow; Homogeneity – Outsider; Democratic - Advisor

Social networks with these characteristics are situations where the accountant responds to a request from others to interact, where the accountant’s participation is excluded by other stakeholders, and where the accountant’s opinion is advice. In this type of social network, the accountant would have almost no influence in controlling the behaviour of other stakeholders involved in the activity. Therefore, while unlawful behaviour may advised against by the accountant, this would have had little effect. There were three processes which had these characteristics (8% of all unlawful processes listed in table 5.2). Two of these processes are in phoenix company activity (1c and 4a) (50% of this activity’s processes); and one is in profit manipulation (3c) (9% of this activity’s
processes). Using table 5.3 again to classify these processes in terms of accounting practice, the employee entitlement activity is about decision making.

The first process, 1c. voluntary closure: bankruptcy, would have involved decision making about business viability. This decision would be made by owners/managers. Accountants’ would have been excluded from decisions. However, if accountants were asked an opinion on financial matters, it would have been considered as advice due to their expertise.

The second process associated with phoenix company activity, 4a. avoid punishment from creditors, would have involved decision making about not paying creditors. Once again, this decision would have appeared unethical to accountants and, as a result, owner/managers would probably have tried to hide this activity from them. However, if accountants did become aware or involved, it is likely their opinion would have been considered as advice due to their expertise.

The third process, 3c. impression management, was associated with profit manipulation. It would have involved communicating company performance. This is a normal and important part of what accountants do; they report on company financial performance. However, this process becomes unlawful when company performance is falsely reported and external stakeholders, particularly investors and regulators, are intentionally misled. In these circumstances, accountants would have objected to presenting false information and been excluded from the reporting. If accountants did become aware or involved, it is likely their opinion would have been considered as advice due to their expertise. Given 50% of phoenix company processes were listed in this behaviour, further analysis is included in this section.
It is very clear from the RCR that the unlawful behaviour associated with phoenix company activity was driven by self-interest. Indeed, Commissioner Cole makes a statement which provides excellent insight into the social practice of unlawful behaviour within the construction industry:

There are extreme examples of self-interest, exercised in disregard of the effect on others. Phoenix companies epitomise the problem of a culture of self-interest (Cole 2003, vol. 3, p. 208).

The main driver in phoenix company activity was company directors. These individuals were motivated to avoid paying debts and to establish a new business to replace their failed business. The self-interest described by Commissioner Cole was the goal of these directors to preserve their personal wealth at the expense of others; including their employees, creditors and taxation authorities. The insight provided by the word “self-interest”, is that it suggests that other industry stakeholders, including accountants, were not to blame. The directors did this for their own benefit. It is also important to recognise that directors were legally obliged to act in a lawful manner when facing insolvency or when engaging in phoenix activity. The following extract from the Corporations Act 2001 explains these obligations:

The directors’ duties powers contained in ss 180–184 of the Corporations Act can be used by ASIC or the company’s liquidator against company directors who misuse their powers by engaging in phoenix activity. Under s 181(1), directors must exercise their powers in good faith in the best interests of the company and for a proper purpose. Under s 182(1), directors must not improperly use their position: to gain an advantage for themselves or someone else, or to cause detriment to the corporation. Many of the actions of directors who engage in phoenix activity would amount to breaches of these duties, which have criminal equivalents under s 184 or may be actioned by ASIC as civil penalty breaches under pt 9.4B of the Corporations Act (Anderson 2012, p. 420).

However, Commissioner Cole found that some directors were misusing their power to gain advantage for themselves over others, for example subcontractors and other
creditors. Therefore, these individuals were breaking the law under the *Corporations Act 2001*.

Company directors cannot act in complete social isolation. They need to work with others to achieve their goals. Almost all of the phoenix company processes involve financial information. The directors must have worked with accountants, either individuals employed as full-time staff, that is internal accountants, or staff from an accounting firm, that is external accountants, in gathering information associated with phoenix company processes. More specifically, voluntary closure: bankruptcy (process 1c) would have required reporting on the IS and CFS; assets transferred to the new company (process 2a) would have required reporting on the BS; liabilities of the failed company not paid to creditors (process 3a) would have involved decision making about paying debts; and avoiding punishment from creditors (process 4a) may have involved communication via reporting, that is, falsifying reports. This activity provides evidence of subjective accounting.

*High density – Follow; Homogeneity – Outsider; Undemocratic - Challenged*

Social networks with these characteristics are situations where the accountant responds to a request from others to interact, where the accountant’s participation is excluded by other stakeholders, and where the accountant’s opinion would be disputed. In this type of social network, the accountant would have almost no influence in controlling the behaviour of other stakeholders involved in the activity. Therefore, while unlawful behaviour may have been challenged by the accountant, this would have had little effect. There is one process which has these characteristics (3% of all unlawful processes listed in table 5.2). This process is in profit manipulation activity (2d) (9% of this activity’s
processes). Using table 5.3 again to classify these processes in terms of accounting practice, the employee entitlement activity is about decision making.

The process 2d., falsely representing the long-term capacity of the firm to generate earnings, would have involved decision making about business viability. This decision would be made by owners/managers. Accountants’ would have been excluded from decisions. If accountants became aware or involved, it is likely they would have challenged the figures, and their opinion would have been disputed. This activity provides evidence of objective accounting.

**High density – Follow; Homogeneity – Enemy; Undemocratic - Challenged**

Social networks with these characteristics are situations where the accountant responds to a request from others to interact, where the accountant is denied any contact with other stakeholders, and where the accountant’s opinion would be disputed. In this type of social network, the accountant would have no influence in controlling the behaviour of other stakeholders involved in the activity. Therefore, while unlawful behaviour may have been challenged by the accountant, this would have had no effect. There are three processes which have these characteristics (8% of all unlawful processes listed in table 5.2). All of these processes are in security of payments (1a, 1c, and 2a) (75% of this activity’s processes). Using table 5.3, the security of payments activities are mainly communicating.

In conducting the communication role, the accountant needs to consolidate financial information and produce regular reports (Birt et. al 2010). Therefore, if accountants were involved in unlawful behaviour associated with these activities, it mainly involved financial reporting. The reason that the accountant was excluded from social interaction associated with security of payments was that unscrupulous individuals and companies
were trying to hide information. Given 75% of security of payments processes were listed in this behaviour, further analysis is included in this section.

In order to examine these questions further, some of the processes are discussed in more detail. The first unlawful process associated with security of payments, 1a. financial performance involves prequalification. “Prequalification involves assessing the financial viability and the capacity of firms to undertake various types of construction work” (Cole 2003, vol. 8, p. 245). It reduces the “risk that the contractors chosen for the project will experience financial difficulty and then fail to pay subcontractors” (Cole 2003, vol. 8, p. 245). This is at the start of the security of payments process. At this stage, accountants might be involved in two ways. If they are employed as an internal accountant for a large company, for example a head contractor, they might be asked to request financial information from subcontractors tendering for a part of a construction project managed by the head contractor. In this interaction, the accountant might deal with internal stakeholders: management and project manager; and external stakeholders such as suppliers, who would be subcontractors in the case of labour. It is unlikely that any unlawful behaviour would involve internal accountants at this stage.

Subcontractors will have to provide head contractors with financial information. Two decisions are made at this point by the owner/manager of the subcontractor. The first decision is about who should prepare the financial statements. Many mid-sized companies would be large enough to employ an internal accountant and, therefore the accountant would prepare the financial information. Small companies would not be able to afford to pay an internal accountant, but they could use their external accountant (for example, tax agent) to prepare the financial information. However, paying an accountant would cost money that small companies often did not have, so the financial information might often have been prepared by the owner/manager. It is assumed that security of
payments are not requested in reverse, that is, that subcontractors ask head contractors for financial information about their capacity to pay!

There were two types of unlawful behaviour at this stage. First, honest mistakes were made by people who submitted financial information which was incorrect. This was particularly the case if the information was not provided by accountants, but rather by owners/managers. Second, false information was deliberately submitted with the intention to mislead others. This misleading information was often designed to help the company win the contract. It is unclear from the RCR who submitted this false information, other than it is known that it was done by unscrupulous individuals often called ‘rogue builders’. This phrase suggests false information was provided by owners/managers, therefore the inclusion of the word ‘builder’, however, this could refer to a company, which means that accountants might have been involved in submitting false information. However, it is most likely it was owner/managers who engaged in this unlawful behaviour.

In the second process associated with security of payments, 1c. prequalification scrutiny, the company requesting the financial information, that is, the head contractor, examined the information to assure that the contractor was financially healthy and capable of paying its bills through the life of the contract. This analysis would have been done by accountants. It was done unlawfully because companies who apparently ‘passed’ the scrutiny test were later found not to be able to pay their bills. This raises the question: how could accountants get this wrong? Was this financial analysis prepared incorrectly with deliberate intent or did it contain honest mistakes? The answer to these questions lies in the complex nature of the contracting system in the construction industry. Head contractors themselves would have to provide financial information to their customers, being the owner of the construction project. In this interaction, accountants at the
customer would request and then scrutinise the financial information of the head contractor. The head contractor accountants would be required to submit financial information to the customer’s accountant.

Numerous case studies in the RCR show how head contractors were sometimes at the centre of security of payment problems. Does this mean that accountants interacting about the scrutiny of prequalification financial information engaged in unlawful behaviour? Did the customer accountant ask for the wrong information or interpret it incorrectly? Did the head contractor supply wrong information (honest mistake) or misleading information (intent)? The answer to these questions lies with the head contractor’s defence. In the Multiplex case, the head contractor argued that they delayed or withheld payment to subcontractors because the customer had not paid them progress payments. If the head contractor’s testimony is accepted, then the fault lies at the start of the contracting value chain with the customer. This suggests that there was no unlawful behaviour between the accountants in the head contractor’s submission of financial information to the customer and their scrutiny. However, it does suggest a flaw in the contracting system. Whereas the system works so that the company trying to win work is required to submit security of payment, financial information, there is no requirement for the company awarding the work to provide its contractors with security of payment.

The process of scrutiny becomes more problematic further down the value chain. The head contractor’s accountant would have scrutinised the financial information of the subcontractors. In the case of mid-sized companies, this would have involved interaction between the head contractor’s accountant and the subcontractor’s accountant. In small companies, the head contractor’s accountant would have interacted with the owner/manager as they would not have employed an internal accountant. The problem in this interaction was that some unscrupulous individuals provided false information at
prequalification which failed to disclose the true financial health of the company. If the provider of the false information was accountants, then it may be concluded that accountants were involved in unlawful behaviour. However, accountants might also have engaged in inappropriate behaviour if they ignored (intent) or misinterpreted (honest mistake) financial information provided for scrutiny.

In terms of examining the behaviour of the social networks surrounding the unlawful processes involving accountants and security of payments, two conclusions are drawn. First, the social networks were heterogeneous. The people making decisions about these processes would have been relatively large in number. Therefore, the network would have been relatively large. It might have included a number of accountants from firms at various stages in the value chain, including the customer, head contractor, subcontractor, and other smaller subcontractors, as well as management in the larger companies, owner/manager for smaller companies, and perhaps suppliers from the legal system if matters went to court. The accountant would have held some power in this network as the processes involved reporting and interpreting financial information and this would give them expert status. This power would be differentiated by the accountant’s position in the value chain. The further up the chain, for example head contractors, the more power the accountant would have held over other accountants. Management in large companies and owner/managers in smaller companies would have also held considerable power over the other network members as they controlled whether the others were employed. The shared mental model of this network would have been to win work and maintain cash flow, perhaps at any cost, as it represented their employment. It is likely the network would have operated with low trust as individuals tried to hide information.

The social network operated under high constraint. Decisions would have been vertical, that is top down, and non-democratic, in the sense that the manager in large companies
and the owner/manager in smaller companies would have told the other network members what he/she wanted and that they were to implement that decision. Under these circumstances, accountants would have been under considerable pressure to scrutinise financial information about security of payment with a creative accounting approach. Their role would have been to scrutinise in a way that helped the other network members. This activity provides evidence of subjective accounting.

**Low density – Follow; Heterogeneity – Respect; Democratic - Expert**

Social networks with these characteristics are situations where the accountant responds to a request from others to interact, where the accountant’s participation is valued by other stakeholders, and where the accountant’s opinion is more important than any other stakeholders. In this type of social network, the accountant would have influence in controlling the behaviour of other stakeholders involved in the activity. The accountant is only involved if invited, but then unlawful behaviour would have been challenged by the accountant, and this would have had some effect. There was one process which had these characteristics (1b) (3% of all unlawful processes listed in table 5.2). This process – a. recognise the payroll tax liability - was in payroll tax (1b) (50% of this activity’s processes). Using table 5.3 again to classify this process in terms of accounting practice, the payroll tax activity was about identification.

This involves identifying transactions that affect the entity’s financial position, so that they able to be reliably measured and recorded. This process would have involved small social networks, largely the accountant working with one or two others, for example taxation authorities, asking for information. These activities required the expertise of an accountant and, therefore, other stakeholders would have respected their capability as experts, and allowed them to do this work largely without interference. Given that 50%
of payroll tax processes were listed in this behaviour, further analysis is included in this section.

In reconstructing the reality of how accountants were involved in payroll tax activity, it is necessary to determine whether accountants acted objectively and stood above all other organisational activity and acted as a type of guardian of the public interest or whether they acted subjectively because they were influenced by the social interactions within their organisational setting.

The case for acting objectively is based on two assessments. First, what proportion of the payroll tax process involved accountants? Weak involvement in an activity associated with unlawful behaviour, such as payroll tax, supports the case that accounting is objective. It suggests this was carried out independently of accounting. This implies that the inappropriate behaviour may not have occurred if accounting was involved. Strong involvement in an activity associated with unlawful behaviour, such as payroll tax, supports the case that accounting is subjective for it suggests that accountants had to change their behaviour in response to those who desired the behaviour. Second, to what degree would accountants working in these processes have followed the rules, that is, the accounting standards, with no adjustment or interpretation? No adjustment supports the case for accounting as objectivity; whereas adjustment supports subjectivity.

On the first point, the proportion of payroll tax processes which involved accountants was 56% (5 of 9). This suggests that accounting was involved. On the second point, accountants working in these processes would have followed the rules more often than not. Only two of the five payroll tax processes involving accountants were associated with unlawful behaviour (see bold red processes in figure A1.3 in appendix 1). There is
evidence that construction companies complied with one of these processes, 1a. Recognise the payroll tax liability, when the PTA contacted them, and this often occurred through honest mistake rather than deliberate intent to avoid paying tax. The other process, 1b. calculate threshold figure, may have involved accountants using false information. It is likely that accountants would have had to adjust their behaviour in this process. Overall, this activity provides evidence of objective accounting.

**Low density – Alone; Heterogeneity – Respect; Democratic - Expert**

Social networks with these characteristics are situations where the accountant where the accountant does the activity largely in isolation from others, where the accountant’s participation is valued by other stakeholders, and where the accountant’s opinion is more important than any other stakeholders. In this type of social network, the accountant would have strong influence in controlling the behaviour of other stakeholders involved in the activity. Therefore, if unlawful behaviour occurred, it would have been approved, and perhaps even encouraged by the accountant. There are eight processes which have these characteristics (22% of all unlawful processes listed in table 5.2). The majority of these processes (six) are in inappropriate payments activity (86% of this activity’s processes). One process is in employee entitlements (33% of this activity’s processes). One process is in payroll tax (50% of this activity’s processes). Using table 5.3 again to classify this process in terms of accounting practice, the inappropriate payments processes are mainly about identification.

This involves accountants identifying business transactions. A business transaction is “an event that affects the financial position of an entity and can be reliably measured and recorded” (Birt et al. 2010, p. 4). Business transactions include: withdrawals of cash by the owners/investors, payment of wages and salaries, earning of fees revenue, and
payment of taxes and expenses. The accountant needs to keep track of events involving money at the entity. This is a core business activity for accountants. If there is unlawful behaviour associated with this activity, as found by the RC, this means that accountants must have been involved. This suggests that accounting was a subjective process and that accountants would have been under pressure from other stakeholders to engage in inappropriate payments. Given 86% of inappropriate payments processes were listed in this behaviour, further analysis is included in this section.

The RC found inappropriate behaviour in the way the construction industry made and received payments. In an industry with such complex contractual arrangements, and the subsequent power differentials, along with higher than normal incidence of insolvency, there was significant cause for inappropriate payment behaviour and it became part of the industry culture.

The construction industry’s inappropriate behaviour regarding making and receiving payments may be summarised into five issues:

1. Buying industrial peace
2. Including inappropriate payments in industrial agreements
3. Delaying payments to employees, for example wage increases or other entitlements
4. Unions demanding payment during industrial action
5. Unions exerting pressure to ensure employee entitlements are paid

For the purposes of this study, accounts payable is most interesting in terms of accountants’ role in authorizing payment. The RC identified the making and receipting of inappropriate payments as inappropriate behaviour by the construction industry. This means that someone within construction firms decided to pay for goods and services that were inappropriate, in other words, to give cash to a supplier for something the firm should not be purchasing. It also means that someone, in all likelihood accounts payable
staff, authorized the transaction, and recorded the payment as an expense. In this case, step two in the accounting process is being considered and the murky area of classifying expenses for recording in financial reports. It is called murky because it is unclear what exactly accounts payable staff did here, other than employ creative accounting to describe a transaction involving an inappropriate payment as something else, perhaps something appropriate, in the classification of expenses for the IS.

The case for acting objectively is based on two assessments. First, what proportion of the payments process involved accountants? Weak involvement in an activity associated with unlawful behaviour, such as payments, supports the case that accounting is objective. This would mean the activity was carried out independently of accounting. On the other hand, strong involvement in an activity associated with unlawful behaviour, such as payments, supports the case that accounting is subjective. It reveals that accountants had to change their behaviour in response to those who desired the behaviour. Second, to what degree would accountants working in these processes have followed the rules, that is the accounting standards, with no adjustment or interpretation? No adjustment supports the case for accounting as objectivity; whereas adjustment supports subjectivity.

The proportion of payments processes which involved accountants was 64% (9 of 14) (see appendix 1). This indicates that accounting was involved at a high level. Accountants working in these processes would have rarely followed the rules. All of the nine payments processes involving accountants were associated with unlawful behaviour. It is very likely that accountants would have had to adjust their behaviour in these processes. This supports the case for subjectivity.
The issue is whether accountants interacted with others in doing the tasks associated with payments or whether they did this work alone. The analysis suggests accountants would have been involved in nine of the fifteen processes associated with payments. Of these fifteen processes, our main interest is with those fourteen processes identified as involving unlawful behaviour. Of these fourteen processes, nine involved accountants. Therefore, it may be assumed that none of the nine processes involving accountants and payments were always conducted lawfully following accounting standards. This activity provides strong evidence of subjective accounting.

**Low density – Alone; Heterogeneity – Respect; Democratic - Advisor**

Social networks with these characteristics are situations where the accountant does the activity largely in isolation from others, where the accountant’s participation is valued by other stakeholders, and where the accountant’s opinion is advice. In this type of social network, the accountant would have some influence in controlling the behaviour of other stakeholders involved in the activity. Therefore, if unlawful behaviour occurred, it would have been approved, and perhaps even encouraged by the accountant. There was one process which has these characteristics (3% of all unlawful processes listed in table 5.2). The process was in inappropriate payments activity 14% of this activity’s processes). Using table 5.3 again to classify this process in terms of accounting practice, the inappropriate payments processes are mainly about identification.

The process was 1.e Authorize payment. This is an important part of inappropriate payments because it represents the approval step. If accountants were approving inappropriate payments, this implicates them in unlawful behavior. However, the analysis shows that this process was slightly different from the other six inappropriate
payment processes listed in table 5.2 (see above). In this case, the accountant’s role is as an advisor, whereas in the other processes they are seen as experts. This means that in process 1e. accountants have less power and, therefore, less influence over unlawful activities. It suggests that accountants may be less involved in authorizing payment and that other stakeholders made final decisions. This activity provides evidence of objective accounting.

*Low density – Alone; Homogeneity – Enemy; Democratic - Expert*

Social networks with these characteristics are situations where the accountant does the activity largely in isolation from others, where accountants are denied any contact, and where the accountant’s opinion is more important than any other stakeholders. In this type of social network, the accountant would have little influence in controlling the behaviour of other stakeholders involved in the activity. Accountants were excluded from social networks associated with these activities, because other stakeholders knew they would disapprove, and that they would be justified as they were experts. Therefore they had little effect on this unlawful behaviour. There were two processes which had these characteristics (5% of all unlawful processes listed in table 5.2). One process, 2b. code of practice, was in security of payments (25% of this activity’s processes). The other process, 2a. exceptions to accounting standards, was in profit manipulation (9% of this activity’s processes). Using table 5.3 again to classify this process in terms of accounting practice, these processes were about identification.

This involves identifying transactions that affect the entity’s financial position, so that they are able to be reliably measured and recorded. These processes involved accountants developing appropriate ways to prepare financial statements. This was work only an accountant could do and, therefore, other stakeholders would have respected
their capability as experts, and allowed them to do this work largely without interference. However, these processes would have caused problems for unscrupulous individuals who wanted to engage in unlawful processes associated with the two activities – security of payments or profit manipulation (see table 5.3). These individuals would have seen accountants as the enemy and would have excluded them from social interaction involving these other processes. Accountants who tried to impose standards onto these unscrupulous individuals would have been avoided. This activity provides evidence of objective accounting.

*Low density – follow; Homogeneity – Outsider; Undemocratic - Challenge*

Social networks with these characteristics are situations where the accountant responds to a request from others to interact, where secrets are held from the accountant, and where the accountant’s opinion is disputed by other stakeholders. In this type of social network, the accountant would have little influence in controlling the behaviour of other stakeholders involved in the activity. If accountants tried to discourage unlawful behaviour they would be challenged, and therefore they had little effect. There were three processes which had these characteristics (8% of all unlawful processes listed in table 5.2). These processes were all in profit manipulation (27% of this activity’s processes). Classifying this process in terms of accounting practice, using table 5.3 again, the profit manipulation processes were about measurement, communication, and decision making.

These processes would have involved small social networks, largely the accountant working alone with owners/managers who wanted to manipulate profit reporting. These activities would have been secretive. Decisions and information would have been withheld from the accountant. If the accountant became aware or involved and disagreed
with other stakeholders, the accountant’s opinion would have been challenged. Under these circumstances, it is likely the accountant would have been directed to cooperate. Given the high proportion of profit manipulation processes with these characteristics, further analysis is included in this section.

The cases of Enron, Tyco, and Xerox provide evidence of the role of accountants in profit manipulation. They are useful for this study because the practice of profit manipulation was made publicly available through legal investigations by regulators, and also because their practices are considered widespread (Desai 2005, p. 171). In all three cases, the main stakeholder was management. Management engaged in self-deception and the ability to disengage oneself from responsibility (Desai 2005, p. 190). This unethical behaviour at the top has the tendency to cascade throughout the organisation, in other words, to reach accountants. However, as Commissioner Cole did with the RC findings, investigators of these cases in the United States blame the system. Whereas Commissioner Cole criticises society for providing insufficient power for authorities to deal with inappropriate behaviour, in the United States investigators found a “system that allows managers to characterize income differently depending on the audience legitimizes earnings manipulation and permits managers a certain license” (Desai 2005, p. 190). While the inappropriate behaviour cannot be condoned, in both circumstances investigators have included society, here represented as the system, for allowing profit manipulation to occur.

The proportion of profit manipulation processes which involved accountants was 64% (12 of the 13 processes) (see appendix 1). This suggests that accounting was involved at a high level; which supports the case for subjectivity. Accountants working in these processes have rarely followed the rules. 10 of the 12 profit manipulation processes involving accountants were associated with unlawful behaviour (see appendix 1). It is
very likely that accountants would have had to adjust their behaviour in these processes. This further supports the case for subjectivity.

The problem processes would be included in several activities normally conducted by accountants. More specifically, in terms of identification, the accountant would have to keep track of payment of tax. In measurement, the accountant would need to continually assess payment of wages as it would increase expenses and reduce cash. In terms of communication this would have required reporting on the IS and CFS. In terms of decision making this would have involved advice to owners/managers about paying debts and may have involved communication via reporting (that is, falsifying reports) to investors. This analysis shows that this problem process heavily involved accountants. The fact that this process was manipulated via creative accounting provides evidence for the case of accounting as subjectivity. Further evidence is provided by the amount of pressure exerted on accountants to be creative with this process. This activity provides evidence of subjective accounting.

*Low density – follow; Homogeneity – Outsider; Undemocratic - Ignored*

Social networks with these characteristics are situations where the accountant responds to a request from others to interact, where secrets are held from the accountant, and where the accountant’s opinion is ignored by other stakeholders. In this type of social network, the accountant would have no influence in controlling the behaviour of other stakeholders involved in the activity. If accountants tried to discourage unlawful behaviour they would be ignored, and therefore they had no effect. There was one process which had these characteristics (3% of all unlawful processes listed in table 5.2). This process was in profit manipulation (27% of this activity’s processes). Classifying
this process in terms of accounting practice, using table 5.3 again, the profit
manipulation process was about decision making.

The process was 4a fraud. This is discussed in more detail later in section 6.3.2.2:
Societal Contract Breach. This activity provides evidence of subjective accounting.

*Low density – follow; Homogeneity – Enemy; Undemocratic - Challenged*

Social networks with these characteristics are situations where the accountant responds
to a request from others to interact, where the accountant is denied any contact with
other stakeholders, and where the accountant’s opinion would be disputed. In this type
of social network, the accountant would have little influence in controlling the behaviour
of other stakeholders involved in the activity. Therefore, while unlawful behaviour may
have been challenged by the accountant, this would have had no effect. There was one
process which had these characteristics (3% of all unlawful processes listed in table 5.2).
This process was in profit manipulation (9% of this activity’s processes). Classifying
this process in terms of accounting practice, using table 5.3 again, the profit
manipulation process was about decision making.

The process was 4d. Recording forged transactions. This activity may be described as
fraudulent and it would not be acceptable behaviour in the view of accountants. This is
discussed in more detail later in section 6.2.5: Owners/Managers and General Public.
This activity provides evidence of objective accounting.

From this discussion, the main issue which emerges is whether accountants interacted
with others in doing the tasks associated with profit manipulation, for example, or
whether they did this work alone. The analysis suggests that accountants would have
been involved in twelve of the 20 processes associated with profit manipulation. Of
these twelve processes, our main interest is with those eleven processes identified as involving unlawful behaviour. Of these eleven processes, ten involved accountants. Therefore, it may be concluded that only two of the twelve processes involving accountants and profit manipulation were always conducted lawfully following accounting standards.

This analysis shows that accountants would have been heavily involved in profit manipulation activities. This activity provides strong evidence of subjective accounting. The analysis has identified four types of social practice involving accountants and other stakeholders in the construction industry.

Figure 5.2 presents a conceptual model of this social practice. Four quadrants are identified based on the three themes of interaction, harmony and cohesion used as the analytical framework for this section.
Figure 5.2: Conceptual Summary of Accountants’ Social Practice

Ideally, accounting social practice should be in the top right hand quadrant, trust. In this quadrant, the social networks are high density, strong harmony, and strong cohesion.
The relationships within this quadrant are close and the social network is efficient. The accountant works with other stakeholders to achieve mutual goals.

The social practice described in the three remaining quadrants is less than ideal. In the top left hand quadrant, isolated, the social networks are low density, strong harmony, and weak cohesion. The relationships within this quadrant are distant and the social network is inefficient. The accountant is left alone but is respected if asked for an opinion. In the bottom right hand quadrant, police, the social networks are low density, weak harmony, and strong cohesion. The relationships within this quadrant are remote and the social network is efficient. The accountant is avoided, but others will follow their direction, if the accountant becomes aware or involved. In the bottom left hand quadrant, hostile, the social networks are low density, weak harmony, and weak cohesion. This is the worst case scenario of accounting social practice. The relationships within this quadrant are remote and the social network is inefficient. The accountant is excluded, and others will reject their direction, if the accountant becomes aware or involved.

Next, the seven unlawful activities are mapped into the conceptual framework to summarise the nature of unlawful social practice involving accounting in the construction industry.
Figure 5.3: Summary Map of Unlawful Behaviour Involving Accountants
The percentages are the proportion of unlawful processes involving accountants for that activity. Figure 5.3 highlights the high proportion of accountant involvement. The figure helps identify where the seven unlawful activities most fit within the four types of accounting social practice identified by this study (see figure 5.2). For example, the two activities tax evasion and employee entitlements sit within the ‘trust’ quadrant. This means that these unlawful activities occur within the context of accountants’ traditional role as trusted expert. This is particularly concerning because it shows that even in circumstances where the role of accounting would be expected to be objective, that is follow the standards without any adjustments, unlawful behaviour still occurred.

The findings will be examined further in chapter 7 and form the basis of the practical and policy guidelines produced by this research. Why this social practice involved unlawful behaviour is examined next.

5.4 Conclusions

The purpose of this chapter was to reconstruct the social reality of how accountants work within the construction industry. The chapter has examined the first of three constructs adopted from ST, relationships, to explore the social practice of accounting in the construction industry. From the analyses, this chapter provides three groups of findings: (1) understanding the nature of social interaction involving accountants and other stakeholders within the construction industry using SNA theory; (2) discussing whether social practice in the construction industry was ethical or managerial using ST; and (3) drawing conclusions about accountants’ relationships which lead to chapter six and further exploration of the impact and expectations.
The first findings relate to the nature of social interaction. Two dimensions of SNA theory were applied: explanatory mechanisms, which refer to how network ties are seen to function; and explanatory goals which refer to network outcomes. Explanatory mechanisms include patterns of interconnection. One of the characteristics used was density. Density is a positive factor in social networks because it measures frequency of interaction. The more density, the more opportunity to build and maintain relationships, which results in increased communication, trust, and social dependency. By contrast, low density indicates separateness, which results in isolation, mistrust, and conflict.

The construction industry’s social networks were dominated by interaction between a few stakeholders, the owners/managers, trade unions, and regulators, who had high density within these networks. The remaining stakeholders, including accountants, had lower density. The research found that social interaction within the construction industry contradicted previous research on network density (Stone 2001; Anklam 2005). Sections 2.2.4 (chapter 2) and 5.2.2.1 (chapter 5) provide details of this literature. SNA allows measures of social quality and social structure. Density is part of network structure. The structural measures are based on measuring connections. Density, is used to examine the interconnectedness of social networks (Stone 2001; Anklam 2005). Density is a positive factor in social networks because it measures frequency of interaction. The more density, the more opportunity to build and maintain relationships, which results in increased communication, trust, and social dependency. In contrast, low density indicates separateness, which results in isolation, mistrust, and conflict.

The findings from chapter 5 contradicted previous research because it showed that high network density was not always a positive factor; rather it often had a negative impact on social relations. This contradiction with previous research is explained by differences in interacting with people and positions. When interacting with people, high network
density will often lead to positive social interactions, as individuals get to know one another and build a sense of trust and reciprocity. However, when dealing with positions, the individual becomes somewhat obsolete, particularly in adversarial situations such as the construction industry. People see the person they are interacting with as being from management or from the trade unions and they immediately adopt an adversarial position irrespective of their frequency of interaction. Their positions means they are not allowed the opportunity to like each other on a personal level.

This finding is explained further by the different types of interaction between stakeholders identified by this research (see figure 5.1). It describes the social roles played. Whereas unions play multiple roles as advocates (for members), adversaries (for owners/managers), and whistle blowers (for regulators), the owners/managers are negotiators (for staff), and avoiders (for regulators), as well as adversaries (for trade unions). Accountants play the role of providing information and reporting. The study, therefore, contributes to understanding of explanatory mechanisms within SNA theory by explaining that high network density can create negative social interaction; and this is conceptualised by different social roles which distinguish positional interaction rather than people interaction.

Explanatory goals include actor attitudes, beliefs and practices, as a function of social ties. Two measures were used: harmony and cohesion. These measures combined to explain the social behaviour of accountants associated with the unlawful activities identified by the RC. The first measure, harmony, was defined by levels of homogeneity and heterogeneity within the social network. Harmony indicates tolerance and respect between stakeholder groups. Strong harmony creates homogeneity. Homogenous networks generate equality, democracy and participation amongst all stakeholders. By contrast, weak harmony and cohesion creates heterogeneity. Heterogeneous networks
are characterized by fragmentation and discord, generated by inequality, repression, and exclusion. The list of processes associated with the unlawful activities identified by the RC had more heterogenous than homogeneous social networks. Almost two thirds (62%) of the 37 processes listed in table 5.2 were heterogenous, while about one third (38%) were homogeneous. This finding indicates that accountants’ social networks, defined as the social practice around each process outlined in table 5.2, were more likely to have harmony because they were respected or tolerated by other stakeholders. This was evident in certain unlawful activities including tax evasion, employee entitlements, payroll tax, and inappropriate payments. A significant proportion of accountants’ social networks had disharmony and lacked cohesion because they were seen as outsiders or the enemy. This was evident in phoenix company activities, security of payments, and profit manipulation. The analysis which follows table 5.2 varies in length in terms of the 15 configurations of social behaviour presented. The longer sections refer to specific unlawful behaviours, such as inappropriate payments, which dominate a configuration. It provides opportunity to explore the nature of the behaviour within the social behaviour construct in more detail. Other configurations with one or two processes only are, understandably, much briefer discussions, and some, like fraud, are mentioned briefly and referred other sections which explore it in much more detail.

The study here makes an important contribution to SNA theory. Whereas, previous research argues that harmony is a positive social practice, this study’s findings show that it can be a negative factor, particularly if the rest of the network is behaving unlawfully. In these circumstances, traditional measures of harmony such as homogeneity are actually a bad thing because it reveals that accountants, in this case, are accepting of the unlawful behaviour of the others within their social network. Therefore, the finding that two thirds of the accountants’ social networks are homogenous is actually a bad result. It
suggests that accountants did comply with unlawful behaviour in the following activities: tax evasion, employee entitlements, payroll tax, and inappropriate payments. Unlawful behaviour in these activities could not have occurred without accountants’ knowledge and, the findings suggest, without their cooperation.

There is some defence for accountants doing the right thing. More than one third of social networks were heterogeneous, which means that accountants were excluded, mainly because unscrupulous individuals knew accountants would not cooperate with their unlawful behaviour. This suggests that in the following activities, phoenix company activities, security of payments, and profit manipulation was hidden from accountants or their advice was ignored. The second measure, cohesion, indicates efficient teamwork. It is defined by the democracy of accountants’ social networks in each process. High cohesion means shared control with other stakeholders involved in the unlawful activity. Low cohesion means no shared control. This measures how much accountants’ opinions were listened to by other stakeholders. Almost three quarters (73%) of the 37 processes listed in table 5.2 were democratic, while about one quarter (27%) were undemocratic. This finding indicates that accountants’ social networks, defined as the social practice around each process outlined in table 5.2, were more likely to have democracy because they were considered experts or advisors by other stakeholders. This was evident in certain unlawful activities including tax evasion, employee entitlements, payroll tax, and inappropriate payments. A significant proportion of accountants’ social networks were undemocratic and lacked efficiency because their opinion was challenged or ignored. This was evident in phoenix company activities and security of payments. Profit manipulation had elements of both but was slightly more undemocratic.
The study makes a further important contribution to SNA theory. Whereas, previous research argues that cohesion is a positive social practice, this study’s findings show that it can be a negative factor, particularly if the rest of the network is behaving unlawfully. In these circumstances, traditional measures of cohesion such as democracy are actually a bad thing because it reveals that accountants, in this case, are agreeing with the unlawful behaviour of the others within their social network. Therefore, the finding that three quarters of the accountants’ social networks are democratic is actually a bad result. It suggests that accountants did agree with unlawful behaviour in the following activities: tax evasion, employee entitlements, payroll tax, and inappropriate payments. Unlawful behaviour in these activities could not have occurred without accountants’ participation and, the findings suggest, without their agreement.

The findings then presented several social network scenarios which summarised the three measures of accountants’ social practice: interaction, harmony, and cohesion. Fifteen scenarios were presented, each illustrating different combinations of the three measures. Of these fifteen scenarios, nine provided evidence for subjective accounting, and six for objective accounting. Overall, the analysis provides support for the argument that accounting is a subjective practice.

The analysis identified four types of social practice involving accountants and other stakeholders in the construction industry, which was conceptualised as four quadrants: trust, police, isolated, and hostile (see figure 5.3). The four quadrants are identified based on the three themes of interaction, harmony and cohesion used as the analytical framework for this section. Ideally, accounting social practice should be in the top right hand quadrant, trust. In this quadrant, the social networks are high density, strong harmony, and strong cohesion. The relationships within this quadrant are close and the social network is efficient. The accountant works with other stakeholders to achieve
mutual goals. However, as discussed above, the strong social networks in this quadrant are very concerning in terms of the role of accountants. The two unlawful activities mapped in this quadrant, tax evasion and employee entitlements (see figure 5.3), mean that accountants were interacting, complying, and agreeing with other stakeholders engaged in inappropriate behaviour associated with these activities. The trust role was abused by accountants who instead used this trust to work with, rather than against, stakeholders who breached the societal contract.

The social practice described in the three remaining quadrants is less than ideal. In the top left hand quadrant, isolated, the social networks are low density, strong harmony, and weak cohesion. The relationships within this quadrant are distant and the social network is inefficient. The accountant is left alone but is respected if asked for an opinion. The unlawful activities mapped in this quadrant, inappropriate payments and payroll tax, are done in isolation from accountants. There is evidence that accountants try to correct inappropriate behaviour if they become aware, but it is often kept hidden.

In the bottom right hand quadrant, police, the social networks are low density, weak harmony, and strong cohesion. The relationships within this quadrant are remote and the social network is efficient. The accountant is avoided, but others will follow their direction, if the accountant becomes aware or involved. The unlawful activities mapped in this quadrant, phoenix companies, are done by owners/managers for specific purposes. If necessary, owners/managers will consult accountants for advice and will follow that advice as their aim is to manage their financial situation. However, much of the processes associated with phoenix companies can be done without accountants.

In the bottom left hand quadrant, hostile, the social networks are low density, weak harmony, and weak cohesion. This is the worst case scenario of accounting social
practice. The relationships within this quadrant are remote and the social network is inefficient. The accountant is excluded and others will reject their opinion if the accountant becomes aware or involved. The unlawful activities mapped in this quadrant, security of payments and profit manipulation, are done by excluding accountants. Stakeholders who engage in these activities probably know accountants will not cooperate or agree with unlawful behaviours. Therefore, while this social practice is undesirable for accountants because they are excluded from the organisation’s financial activities, it is also a good result. On the positive side, the study found that accountants are not significantly involved in these unlawful activities. On the negative, if they were involved, they may have been unable to persuade unscrupulous individuals not to engage in unlawful behaviours.

In summary, the chapter provided understanding of the relationships within the construction industry. It provided evidence for the managerial perspective of ST which argues that management will be likely to respond to the expectations of particular (typically powerful) stakeholders. This does not, however, support the ethical perspective of ST, which proposes that all stakeholders should be treated equally and that the (economic) power of various groups should not allow them to have differential influence over the firm. The outcome of this analysis is the social contracts which are ‘negotiated’ with different stakeholder groups. The results argue that accounting is a subjective rather than objective process. Ideally, the seven unlawful activities mapped in figure 3 should be in the top right hand quadrant – trust – and accountants should be working closely with other stakeholders to ensure these activities are performed lawfully. Unfortunately that was not the case in the construction industry. In chapter 6 the two remaining stakeholder constructs, impact and expectations, will be examined to
understand why accountants behaved this way and the outcomes in terms of the different social contracts.
CHAPTER 6: ACCOUNTING AS SOCIAL PRACTICE - IMPACT AND EXPECTATIONS

6.1 Introduction

This chapter will examine the second and third constructs, impact and expectations. It builds on chapter 5 by exploring why stakeholders behave the way they do in social relationships, which is impact, and then the outcomes of this behaviour, which is expectations. Impact is defined in terms of management’s willingness to listen to various stakeholder groups and adjust their behaviour accordingly (Gray, Owens & Adams 1996). It examines the power or level of influence of each group. Chapter 5 introduced democracy as a measure of cohesion within social networks. Democracy indicates shared power or influence. It creates cohesion because decision making is efficient. Stakeholders show one another trust, respect, and tolerance creating equity within group dynamics. It allows people to find convergence, which is agreement, more quickly. Chapter 5 found that three quarters of the accountants’ social networks are democratic. However, it also found that this is actually a bad result. It suggests that accountants did agree with unlawful behaviour in the following activities: tax evasion, employee entitlements, payroll tax, and inappropriate payments. Unlawful behaviour in these activities could not have occurred without accountants’ participation and, the findings suggest, without their agreement.

Chapter 6 explores the impact of these findings from chapter 5. It examines how accountants have been persuaded to comply with unlawful behaviours. The study looks at this from three perspectives. First, impact which is about management’s willingness to
listen to other stakeholders. In this study, this means whether people involved in unlawful behaviours were willing to accept accountants’ advice. This raises questions about accountants’ level of influence in the construction industry. If accounting is an objective practice, it may be inferred that unscrupulous individuals received advice from accountants but chose to ignore it. This assertion is based on the assumption that objective practice would always uphold appropriate financial behaviour, for example following accounting standards or taxation law. This places the blame for unlawful behaviour solely with other stakeholders and not accountants. If accounting is a subjective practice, this means that some accountants would have changed their advice depending upon their circumstances. This means some accountants would have adjusted their advice to assist management, with creative accounting, or they would have even actively participated in the unlawful behaviours, for example by aiding management in tax evasion. This suggests that accountants share the blame for unlawful behaviour.

Chapter 5 found that a majority of social practice scenarios associated with the seven unlawful activities identified by the RC provided evidence that accounting is a subjective practice. Therefore, chapter 6 proceeds on that basis and focuses on the latter position: accountants changed their advice and/or actively participated in unlawful behaviours. This means that accountants were listened to and they did have a degree of influence in the construction industry. Chapter 5 found this was true, certainly in the case of tax evasion, employee entitlements and payroll tax. In some of the other unlawful activities, it may be argued that unscrupulous individuals tried to keep inappropriate behaviour hidden from accountants or chose to ignore their advice. However, chapter 5 certainly indicated that accountants were involved and most likely actively participated in social networks conducting unlawful activities. Therefore, ST’s perspective on impact is proven. While accountants had less influence than some other
stakeholders, they were listened to. Why accountants were willing to change their advice or actively participate in these unlawful activities is now examined.

Commissioner Cole explained the cultural problems which led to the construction industry’s unlawful behaviours were being driven by self-interest. He was quite accepting of this self-interest and describes it as “understandable” (Cole 2003, vol. 2, p. 12). In pursuing their individual interests, he felt stakeholders were behaving normally in the sense that it is to be expected. Indeed, Commissioner Cole concluded that in pursuing their different interests, these stakeholders “would not act inappropriately in any objective sense” (Cole 2003, vol. 2, p. 12). This then raises the question why the RC found behaviour associated with this self-interest unlawful and inappropriate conduct, and if so, why this had been allowed to continue. Commissioner Cole found that the switch from appropriate to inappropriate behaviour occurred due to conflicting time perspectives. Customers and companies had a short-term focus and the unions had a long-term focus. This created conflicts which exerted considerable pressure on these stakeholders, and an emerging power differential created opportunities to engage in unlawful behaviour. The measures used to explore Commissioner Cole’s perspective of self-interest are, therefore, short-term versus long term interests.

The third perspective is provided by theory on power and politics. Whereas chapter 5 used SNA theory to extend ST’s construct of relationships, chapter 6 uses power and politics theory to extend ST’s construct of impact. Power is traditionally defined as the ability to change other people’s behaviour so that they do what they want them to do (Myers, Hulks & Wiggins 2012). There are two views on power in the literature: power as an individual property and power as embedded in organisational structures and processes (Buchanan & Badham 2008). This is best expressed by defining the cause of power:
- Positional power: derived from your personal position, for example owners/managers would have strong positional power
- Coercive power: your ability to threaten others and carry out your threats, for example trade unions would have strong coercive power
- Expert power: derived from knowledge and experience, for example accountants would have strong expert power
- Reward power: your ability to reward others for example human resource management have strong reward power
- Personal of referent power: based on others liking you for example this may be close personal relationships necessary to win contracts.
- Information power: derived from access to data, for example regulators would have strong information power.

Power translates into organisational politics. Political behaviour sometimes takes the form of two or more parties publicly fighting their differences. However, it is usually much more subtle (Myers, Hulks & Wiggins 2012). In many cases politics occurs completely under the surface of public dialogue (Kotter & Schlesinger 1979). Aristotle advocated politics as means of reconciling need for unity in the community with recognition there were diverse interests (Myers, Hulks & Wiggins 2012). The operationalization of political behaviour in this chapter is how stakeholders persuaded others to comply with unlawful activities, to achieve unity within their social networks.

The third construct from ST is expectations. Expectations may be defined in terms of the social contract for each stakeholder group. It answers questions about what each of the groups expect of accounting, and how these expectations differ. This study proposes that the construction industry’s stakeholder groups will have different social contracts with
accountants employed by the industry. This will be manifested in differences compared with the overall social contract, that is, the RC and between the expectations of the various groups.

In summary, ST identifies the various groups with a vested interest in the industry, but also their different expectations of accounting practice, manifested as multiple social contracts. The unlawful behaviour associated with other construction industry activities suggests that the industry tended to adopt a managerial rather than ethical perspective on stakeholder expectations. Clearly, not all stakeholder groups are equal in the construction industry. Questions raised include whether differences in power within these groups create conflict over accounting practice. If so, who was in control and what were their expectations of accounting within the industry. ST allows an opportunity to further examine the tension between accounting as an objective rule-based system versus a subjective reality. It allows comparison of the role of accounting in the construction industry, whether the role was based on a sense of responsibility, that is, doing the right thing or whether it was about demand, that is, meeting the interests of the most powerful stakeholders. SNA will be used to enhance ST by examining the macro level interactions of the stakeholder groups in some more theoretical detail.

6.2 Impact

6.2.1 Introduction

This section examines the impact of the social relationships between the construction industry’s stakeholders. Impact may be defined in terms of management’s willingness to listen to various stakeholder groups and adjust their behaviour accordingly. It measures the power or level of influence of each group. The managerial perspective of ST argues
that management will be likely to respond to the expectations of particular (typically powerful) stakeholders (Gray, Owens & Adams 1996, p. 45). A fundamental cause of the problems that led to the RC was that the industry’s management were influenced by the demands of different stakeholders, the unions in particular. The RC also found non-industrial relations issues such as tax evasion and unlawful acceptance and reporting of commissions/cash payments. This raises the question of which stakeholder groups influenced these behaviours and why.

The construction industry is a complex industry, with significant interaction between external stakeholders due to the nature of the contracting process. This complexity generated conflicting stakeholder interests. Fundamental to this conflict was self-interest, particularly the desire for survival, often at the expense of others. Commissioner Cole stated: “representatives of certain segments of the industry naturally endeavour to maximise the interests of the sector they represent” (Cole 2003, vol. 2, p. 12). For example, unions seek to advance the interests of their members; companies seek to maximise their profits; and governments see their interests from their role as major clients of the industry, but they are also important regulators (Cole 2003, vol. 2, p. 12).

This then raises the question why the RC found behaviour associated with this self-interest unlawful and inappropriate conduct, and if so, why this had been allowed to continue. Commissioner Cole found that the switch from appropriate to inappropriate behaviour occurred due to conflicting time perspectives. Customers and companies had a short-term focus and the unions had a long-term focus. This created conflicts which exerted considerable pressure on these stakeholders, and emerging power differential created opportunities to engage in unlawful behaviour.

The RC found that:
The unlawful and inappropriate practices occur because of a clash between the short term project profitability focus of the providers of capital, clients, head contractors and subcontractors on the one hand, and the long term aspirations of the union movement, especially the CFMEU, to dominate, control and regulate the industry for its benefit and what it perceives to be the benefit of its members, on the other hand (Cole 2003, vol. 3, p. 10).

Those stakeholders with long-term interests, that is the unions, were aware that those with a short term focus were vulnerable to project delay and cost. Those stakeholders with a short-term focus knew that to “surrender to demands” was “the better immediate economic alternative to long drawn out conflict” (Cole 2003, vol. 3, p. 10). This created an “inequality of bargaining power” (Cole 2003, vol. 3, p. 10) which led to “quick fix solutions” driven by “commercial expediency” which “supplanted insistence on legal rights, adherence to ethical and legal norms and the pursuit of legal remedies” (Cole 2003, vol. 3, p. 10). In other words, the contractors felt they had no choice but to comply with union demands. The quick fix solutions were where self-interest spilled over into unlawful and even illegal behaviour. This was relevant to profit reporting because contractors were under enormous pressure to make a profit. Their willingness to succumb to the quick fix solutions was not fully disclosed in their profit reporting. Much of the inappropriate behaviour was a result of pressures on the profit and loss statement created by conflicting self-interest amongst these industry stakeholders.

The analysis which follows will examine who had power, the nature of this power, and how they used it to persuade other stakeholders to do what they wanted. The focus in this analysis is on understanding the interaction between owners/managers and other stakeholders. The aim is to establish which stakeholders held power over whom.
6.2.2 Unions and Owners/Managers

The main battle for power between stakeholders was between owner/managers and unions. The RC contains considerable evidence that the unions tried to exert power over owners/managers. The first impact of this behaviour was unions threatening to expose employers to regulators. The most common threat was to expose tax evasion. There is considerable evidence throughout the RCR about the unions threatening employers with exposure to the ATO. In effect, the unions coerced employers to cooperate with industrial demands. Failure to cooperate meant the unions would go to the ATO and claim that the company was doing something illegal regarding taxation payments. This was a type of industrial extortion or blackmail. The widespread use of this threat, and the frequency of cooperation by employers in response to the threat, indicates that tax evasion was common. The unions knew that construction companies engaged in tax evasion and they used this knowledge to intimidate and threaten employers with disclosure. The unions’ behaviour is strong evidence that tax evasion was commonplace. The following extract illustrates a typical exchange between a union official (Ferguson) and an employer (Hackett):

In the Hackett Laboratory Services Pty Ltd (Hacketts) case study, that company did not have a union-endorsed enterprise bargaining agreement. In May 2000 Ferguson attended a meeting with representatives of Hacketts and said he wanted Hacketts to take up a CFMEU endorsed enterprise bargaining agreement. He said ‘I want a deal and I want it today’, that he had friends in the Australian Taxation Office (ATO), and could have the company ‘go down the tube’ and have Mr Hackett, a director of the company, put in gaol on tax matters (Cole 2003, vol. 3, p. 17).

In this extract, the strength of the threat by the unions is found in the emotive language used. Not only was the union official threatening accusations of tax evasion to the ATO, he was reinforcing the consequences of enforcing the threat. The use of the phrase ‘go down the tube’ threatens business closure. The failure of a business must be one of the
serious fears of any employer at it affects their livelihood and reputation. The threat of going to jail is also designed to evoke the greatest possible reaction from the employer, Hackett, as it threatens an individual’s personal freedom. In this extract, the union official has not only threatened to make accusations of tax evasion to the authorities, but also the employer’s livelihood and freedom. The use of language and threats are intimidating and designed to gain maximum benefit for the person issuing the threat, being the union official.

The case involving Hackett Laboratories and the CFMEU further illustrates the aggressive language used by union officials to coerce compliance with their demands. This case was about getting Hackett to agree to sign a new EBA. The CFMEU official, Ferguson, told the company’s owner, Hackett, that “I want a deal and I want it today” (Cole 2003, vol. 13, p. 59). This is very uncompromising language and asserts the union official’s dominance in this relationship and how he used his power to demand cooperation. “Ferguson then said he had friends in the Australian Taxation Office (ATO) and he could have the company ‘go down the tube’ and have Hackett put in gaol on tax matters” (Cole 2003, vol. 13, p. 59). These are very hostile threats to Hackett’s business survival, livelihood, and personal freedom. He must have been under considerable pressure to comply with the union. Ferguson supported his threat by stating that he “had information from the ATO that Hackett Laboratory had tax problems” (Cole 2003, vol. 13, p. 59). It is unlikely that the ATO would provide such information to Ferguson. Other union officials complained to the RC that the ATO did not cooperate with them by exchanging information about tax evasion. Nevertheless, Ferguson exerted this pressure on Hackett. Ferguson then introduced money into the exchange. Not satisfied with an EBA agreement, Ferguson said “that a claim that the CFMEU had put in for workers’ compensation and a wage claim from a past employee on a previous contract still had to
be paid” (Cole 2003, vol. 13, p. 59). A witness told the RC that “the CFMEU had put in
the ‘usual exaggerated claim’ of $24 000 for the past employee”, which Ferguson said
“he would reduce that to $5 000 if his demands were met” (Cole 2003, vol. 13, p. 59).
The use of the phrase “usually exaggerated claim” suggests that unions often engaged in
making exorbitant financial claims; and the reduction in financial demands reveals the
capacity to negotiate on these false claims.

The unions were aware of tax evasion activity at least thirteen years before the RC as
early as July 1990, when the Royal Commission into Productivity in the Building
Industry in New South Wales (Gyles 1992). The National Secretary of the Building
Workers' Industrial Union of Australia (BWIU) later complained that “From day one …
the union called upon Commissioner Gyles to investigate … illegal behaviour in relation
to tax avoidance, ‘cash in hand’ payments, under-payments of wages and breaches of
safety and award regulations” (Cole 2003, vol. 3, p. 37). Gyles (1992) had ignored the
claims. This incident shows that union officials were willing to disclose tax evasion and
other unlawful behaviour at this time; well before the RC. It suggests that the use of
coercion by the unions was probably very well established industry behaviour in the
decade before the RC and also that tax evasion was common behaviour well before the
RC.

Commissioner Cole found that the “culture of lawlessness” was so embedded within the
construction industry that “participants in the industry instinctively succumb to the
exercise of industrial muscle in the interests of commercial expediency and survival”
(Cole 2003, vol. 3, p. 211). These employers “prefer to capitulate to unlawful or
otherwise inappropriate demands or to allow unlawful or otherwise inappropriate
practices to continue, rather than resort to the law to enforce their rights” (Cole 2003 vol.
3, p. 211). Commissioner Cole explains that if employers try to enforce their legal rights,
they will “risk, at best, raising the ire of other participants in the industry and at worst, making a martyr of oneself and putting one’s business and livelihood at risk” (Cole 2003, vol. 3, p. 211). This means the risks outweigh the benefits of seeking to enforce legal rights. Commissioner Cole portrays employers as the victims. This language is very sympathetic towards employers and the use of words such as “succumb” and “capitulate” suggests the pressure being exerted on employers. The description of the unions as “industrial muscle” illustrates the use of force. The word “martyr” is very evocative and suggests strong support for employers in the face of union pressure.

Commissioner Cole found that one of the reasons that unions tried to coerce employers with threats about taxation disclosure was so that they agreed to EBA’s. Commissioner Cole found “a number of subcontractors who have refused to enter in EBA’s with the CFMEU have been the subject of unwarranted occupational health and safety complaints and complaints to taxation, environmental, workplace safety and workers compensation authorities” (Cole 2003, vol. 5, p. 15). He added that “those complaints, or threats of complaints, have been made by union officials for the purpose of applying pressure on subcontractors to enter into EBA’s with the CFMEU” (Cole 2003, vol. 5, p. 15). There are numerous examples and case studies in the RCR. The following analysis highlights some of the main findings. The following case involves The Civil Management Group Pty Ltd (Civil Management Group) in New South Wales.

Mr Peter Primmer, an organiser employed by the CFMEU in its Construction and General Division, New South Wales Divisional Branch, sought entry to a site without prior notice to look around and inspect the machinery. He produced a union card which identified him as a union official. The site foreman, Mr Russell Larkham, refused to allow the organiser to enter the site and asked him to leave. Primmer then asked whether the workers on site had Australian Business Numbers (ABNs) or whether they were paid wages. Larkham told Primmer that as far as he was aware, the workers were on ABNs. Primmer told Larkham he would ensure the Australian Taxation Office (ATO) and WorkCover visited the site. Larkham asked Primmer to leave three more times and threatened to call the police. Each time, Primmer started ranting. He asked Larkham if Larkham was
preventing him from performing a safety inspection. Primmer told Larkham he was going to shut the site down and shut down other sites where the company was working. Primmer finally left after Larkham told him he had called the police. On his way out, Primmer again told Larkham he would have the ATO and WorkCover attend the site. He asked Larkham what other sites Civil Management Group was working on and said he would close down all other Civil Management Group jobs. Primmer told Larkham to ‘get your boss down here and tell him to bring his cheque book. You’ll lose your job over this; I’ll see that you’ll lose your job’ (Cole 2003, vol. 7, pp. 176-177).

In this case, the issue surrounds the right of the union official, Primmer, to enter the building site. Primmer wanted to enter the site to inspect the machinery; presumably for occupational health and safety concerns. The employer representative, Larkham, did not want Primmer to enter the site; because he (Primmer) had not made an appointment and he (Larkham) wanted time to prepare for an inspection of equipment. There were a number of serious threats made by both parties. Primmer began with threats associated with tax evasion, whether the workers had ABN’s. This inferred that the employer was doing business illegally. In response, Larkham threatened to call the police. Both parties were using threats based on having the law on their side. Primmer argued the authorities, the ATO, were on his side, and that Larkham risked getting into trouble with the ATO because his workers were doing something illegal: not having an ABN was a means to avoid paying tax, due to cash payments instead. Larkham, on the other hand, was saying the police were on his side and that if he called them they would visit the site and eject Primmer. As the owner of the building site, Larkham felt he had the right to deny Primmer entry and that the police would support him. Primmer then resorts to threat to livelihood and attacks both the company’s survival, he would close the company down, and also Larkham’s livelihood, “you’ll lose your job”. The exchange reveals the level of animosity in the relationships between employers and contractors and the extent of threats both sides were willing to raise.
Commissioner Cole found numerous threats by union officials to employers had recurring themes across different sized companies and across all states of Australia: threat to company survival and/or employers’ livelihood or job and the use of the ATO as the tool used for coercion. The following was a typical exchange:

The Australian Building Construction Employees and Builders’ Labourers’ Federation (Queensland Branch) Union of Employees (BLF Q), Mr Jamie McHugh, told a contractor, in relation to a single employee who was not a union member, ‘If you don’t have him in the union you’ll be off this job’. When later challenged about the worker’s right to freedom of association, McHugh said: *Well, I’m going to speak to [the head contractor] so you won’t have any work of theirs on the Gold Coast; and I’m going to get the taxation department to go through [the contractor’s] books. That’ll fix you* (Cole 2003, vol. 7, p. 243, emphasis in the original).

There were numerous examples scattered throughout the RCR of union officials using tax evasion as a form of coercion. On some occasions when rights of entry were challenged and entry to a building site denied, CFMEU organisers “resorted to making threats to get the site foreman sacked or the subcontractor removed from the site, or to call in the Australian Taxation Office, WorkCover NSW or other government bodies” (Cole 2003, vol. 12, p. 52).

The Cables at Cammeray site case study in volume thirteen of the RCR provides an opportunity for detailed analysis of the union official’s behaviour regarding tax evasion and coercion. The aim is to identify whether accountants would have been involved in these types of situations. The case study describes that Mr Wayne Holland was the Construction Manager for Manu Enterprises Pty Ltd (Cole 2003, vol. 13, p. 33). The case describes Holland’s interaction with union official Mitchell, when Manu Enterprises was engaged on the Cables at Cammeray site to construct 23 residential apartments and three retail shops. “The project was valued at $5.5 million” (Cole 2003, vol. 13, p. 33). Ball was a subcontractor employed by Manu on the project.
On 11 February 2002 Holland met Mitchell at the site. Mitchell told Holland he wanted Ball off the site and out of business. Holland replied that he had no reason to terminate Ball’s contract. Mitchell told Holland that Manu had to get rid of Ball or the union would see that Manu ‘went down too’. Mitchell told Holland that Ball was a ‘shonk’; did not pay his workers or have any insurance and had been run off the Promenade site at Manly. Mitchell conducted a site safety inspection. Mitchell told Holland he could arrange for a range of audits of workers compensation, tax, immigration and insurance. While on site, Mitchell telephoned Mr Brian Parker, Branch Assistant Secretary of the Construction, Forestry, Mining and Energy Union, Construction and General Division, New South Wales Divisional Branch, and handed the telephone to Holland. Parker asked to speak to Holland about Enterprise Bargaining Agreements (EBAs) at a meeting at the union’s offices at 2.30 pm on 12 February 2002. Parker talked about coming on site and addressing safety issues, wages books, workers compensation certificates, superannuation and a range of other matters. On 12 February 2002 at about 2 pm Holland telephoned Parker and told him that he would not be attending the proposed meeting because Ball’s statutory requirements were in order. Parker told Holland if he did not attend the meeting, there would be consequences. Parker said the CFMEU would stop all Manu’s jobs; stop all the subcontractors on site; call WorkCover out on site; call the Department of Immigration out to the site; and call the Taxation Office to conduct audits on Manu and all its subcontractors. Parker said Ball was a ‘shonk’ and the CFMEU was going to get rid of him (Cole 2003, vol. 13, pp. 33-34).

Commissioner Cole concluded that the case study illustrates:

a. the role that a union, through an organiser, seeks to play as the arbiter of who should work in the industry;

b. the methodology employed by a union organiser to achieve the industrial objectives of the union, namely, to:
   i. raise safety issues; and
   ii. threaten inspections regarding workers compensation, tax, immigration and insurance. This threat is made not because of any true concerns regarding these matters, but because the organiser knows that such inspections will cause disruption to the work, involve cost and loss to the builder, and the likelihood that the builder will acquiesce in the union’s demands, rather than suffer the disruption and loss (Cole 2003, vol. 13, p. 37).

It is an interesting case as it shows the language and behaviour of union officials to achieve their goals. It is threatening and intimidating. Unions would exert industrial pressure on employers to ensure their members were paid; including employee entitlements such as superannuation payments (see section 6.3.3: Employee Entitlements...
for more). While this is a legitimate activity, the unions often went about achieving this aim illegitimately. The RC found that “unions often disclose details about a subcontractor’s arrears in superannuation contributions … to a head contractor, as a means of causing the head contractor to exert pressure on the subcontractor to bring contributions up to date” (Cole 2003, vol. 7, p. 22). The unions had power over the contractors because they could exert industrial pressure, for example strike action causing project delays. The unions also knew that the contractors held power over subcontractors because they could withhold progress payments from a subcontractor. Even though their subcontractors’ superannuation payments may not appear to be any business of the contractor, the unions made it their business by threatening industrial action. The contractors had no choice but to respond by exerting pressure on their subcontractors to make payments. This created a difficult situation for struggling subcontractors. Should they risk not being paid by their contractor due to union pressure, or should they delay or withhold their own payments to their employees by not making superannuation payments? In either case the subcontractor’s cash flow is negatively impacted, and the best decision is to comply with super payments to ensure they are paid by the contractor.

The RC provided an excellent case study, Lavarack Barracks, for examining how unions used project agreements in an unlawful way. The following extract summarises the case:

Lavarack Barracks in Townsville, Queensland, has the largest population of any Army Base in Australia. It was almost entirely rebuilt during the 1990s. There were four stages in the redevelopment. Stage two was approved in mid-1998, with a budget of $139 million, and work began on the project late-1999. Thiess was engaged as the managing contractor. The Code and the Implementation Guidelines applied to the project. A fundamental premise of the Code and Guidelines is that the terms and conditions of employment on the site are worked out at the enterprise level. The Queensland Statement of Intent, which was and is not a registered agreement, requires employers to make weekly contributions to named superannuation and redundancy schemes on behalf of each of their employees.
From the beginning of Stage two of the project there was explicit union pressure to make such payments in relation to Stage two. The unions contended that such payments were ‘standard’ and thus required to be made. The CFMEU said that it wanted to use Lavarack as a test case in relation to the Code. The managing contractor, Thiess, was not itself opposed to a project agreement but it recognised that it needed Commonwealth approval to enter into a project agreement.

The initial response of the Commonwealth, through the Department of Defence, was that a project agreement was unacceptable. A substantial nationwide union campaign against Thiess, then ensued putting Thiess under considerable pressure and also resulting in considerable delays on the Lavarack Barracks site itself. The expressed union view was that the Code was only a policy with no legal force, and that its experience throughout Australia was that generally there was a ‘way around’ the Code. The threat was also made that Lavarack Barracks would become a political battle ground over this issue, to the detriment of Thiess and the project itself. Thiess therefore sought to argue that there was a demonstrable benefit to the Commonwealth in having a project agreement, even though this might result in increased costs of up to $3.62 million. Defence decided to authorise Thiess to negotiate a project agreement, provided it otherwise complied with the Code and the Implementation Guidelines. Defence also advised that in general ‘the Queensland Statement of Intent is not an appropriate basis for negotiating a project agreement’. This was, and was said to be, because of the inconsistencies between the Statement of Intent, and the Code and the Implementation Guidelines.

The union’s demand that Thiess depart from the Code was known to Defence to be a recurrent feature of the dispute, and despite the fact that Thiess was openly putting pressure on the subcontractors for them to make the redundancy and superannuation payments, which the Code prohibited (Cole 200, vol. 7, pp. 126-128).

This case provides several findings in terms of the political power of the construction industry trade unions and how union officials exerted this power. The unions did not use this power to direct owners/managers to conduct unlawful financial activities. The construction companies engaged in unlawful behaviours in response to union pressure however these activities were decisions taken by the companies themselves. The unions would argue they were only exerting pressure to ensure their members, employees of the construction companies and sub-contractor, were paid what they were entitled to. The case also highlights how regulators’ attempt to improve unlawful behaviour in the industry was largely unsuccessful.
Another means used by unions to demand financial contributions was a practice called “dual ticketing”. This practice begins with coercion to ensure employees are union members. For example, a contractor was told by an organiser for the CFMEU, Construction and General Division, Victorian Building Unions Divisional Branch, “that if his employees wanted to work in the city they had to join the union, and that it did not matter how small the job was” (Cole 2003, vol. 7, p. 241). A response from some employers was to purchase “casual tickets as a means of avoiding industrial disruption is a problem” (Cole 2003, vol. 7, p. 241). Commissioner Cole provided an interesting case study to illustrate:

The evidence in relation to Westfield Design and Construction Pty Ltd (Westfield) in Victoria is a good illustration. The evidence was that, as a rule of thumb, Westfield purchases two CFMEU tickets per shop in its shopping centre developments to minimise the risk of the CFMEU causing industrial unrest during the fit-out stage, when any disruption will be likely to delay completion and the opening of the shopping centre. In November 1998, for example, Westfield paid $18 500 to the CFMEU for 100 union tickets, notionally for workers on the Airport West project. No individuals became members as a consequence of the payment. Similar payments were made on other Westfield redevelopment projects (Cole 2003, vol. 7, p. 241).

This is a particularly interesting case because it reveals evidence about accounting practice associated with making and receiving payments. The $18 500 funds would have been authorised as a legitimate expense (see process 2c in figure A1.5 in appendix 1) and may even have been in response to a legitimate invoice from the union (see process 1b in figure A1.5 in appendix 1), with both recorded as union membership fees. However, what happened when it was realised that no actual employees became members? Was the payment made with an awareness that employees would not actually join the union, or did this awareness come afterwards? These are important questions in reflecting upon the role of accountants in this type of activity.
The RC also found that this behaviour was long-standing. Since about 1997 some head contractors had implemented a “no union-endorsed enterprise bargaining agreement, no start policy” (Cole 2003, vol. 5, p. 11). The major reason head contractors apply pressure on subcontractors to make such EBA’s was to avoid industrial action, which would “result in heavy liquidated damages payments where contractual deadlines are not met, and to avoid difficulties and delays due to minor, trivial or spurious occupational health and safety breaches being repeatedly raised by unions thus causing disruption or loss” (Cole 2003, vol. 5, p. 11). This finding illustrates how much power the unions exerted over the complex contractual arrangements in the construction industry. The unions coerced EBA’s onto contractors who, in turn, demanded that their subcontractors also complied with the EBA. The EBA extorted inappropriate payments from contractors and subcontractors in return for industrial peace.

Making inappropriate payments was a mechanism for unions to exert their power over owners/managers. Associated with buying industrial peace, some unions negotiated workplace agreements with contractors which included inappropriate payments in the agreements. Although unregistered, these agreements were the unions’ mechanism for enforcing their demands upon the contractors. The RC found that unregistered agreements between some large contractors and some unions were made in two States. “In Victoria the agreement was known as the Victorian Building Industry Agreement and in Queensland (VBIA) the document was known as the Queensland Construction Sector Statement of Intent” (Cole 2003, vol. 5, p. 10). These agreements fulfil many of the functions of project or site agreements, and “are prescriptive on a range of matters including working hours, rostered days off, leave entitlements, redundancy payments, dispute resolution and the payment of site allowances” (Cole 2003, vol. 5, p. 10). A framework of site allowances, operated in New South Wales, known as the “Sydney
“Matrix” (Cole 2003, vol. 5, p. 11). “Each site in the Sydney CBD and many in the suburbs and beyond attract payments at rates specified in the Matrix, according to the dollar value of the project, regardless of what other industrial instruments are in place” (Cole 2003, vol. 5, p. 11).

If the union engages in industrial action such as work stoppage, union members involved in the stoppage are not paid for that time period. For example, if the union directs its members not to work on Friday, those employees who follow the union’s directions and do not work on Friday will not be paid for that day. However, the RC found that the unions had identified a loophole where they could ensure their members were paid even while absent from work during industrial action. Commissioner Cole found that there were situations where safety has been claimed merely to justify the payment of wages for the duration of stoppages over other unrelated workplace issues (Cole 2003, vol. 15, p. 42). In these circumstances, the unions have claimed that occupational work and safety issues mean the worksite is unsafe for their members. By declaring the site unsafe, employees are still entitled to be paid. However, when this occurs during a period of industrial action, then it raises questions about whether the site is really unsafe or whether the unions are using it as an excuse to ensure their members are still paid whilst taking strike action.

6.2.3 Owners/Managers and Staff

The relationship between owners/managers and staff was different. In this case, owners/managers held power over staff and exploited them for financial gain. Owners/managers had three types of relationships with staff. First, full-time employees were exploited by owners/managers by withholding or refusing to pay employee entitlements.
There was legislative protection of subcontractors to be paid employee entitlements by the employer (known as the head contractor) as a way of addressing deliberate underpayment of employee entitlements. In New South Wales, the *Industrial Relations Act 1996* (NSW), s127, provides that “a principal may be liable for payment of remuneration to employees who have not been paid for work done in connection with a business undertaking of the principal contractor” (Cole 2003, vol. 7, p. 26). This gave employees scope to take legal action against employers for unpaid employee entitlements, even if they were considered subcontractors. The type of employee entitlements includes “superannuation and in some cases redundancy fund, income protection fund, and long service leave fund contributions” (Cole 2003, vol. 7, p. 26).

The problem was that this legislative protection was not uniform across the other states. Only Queensland had something similar, but there employers, head contractors, were only liable for wages of the employees of subcontractors in some circumstances, but this did not extend to other entitlements (*Industrial Relations Act 1999* (Qld), Chapter 11, Part 2).

Inappropriate payment activity involved delaying or withholding payments and incorrect recording of transactions. The former mainly involved external interactions, that is, contractors delaying or withholding payments from subcontractors. However, it also included delays in payments to employees. Commissioner Cole found that EBA’s was a forum for contractors to delay payments of employee entitlements, for example wage increases. He argued that “it is in the interests of all parties for agreement to be reached on the terms of a new enterprise bargaining agreement before any existing agreement reaches its nominal expiry date” (Cole 2003, vol. 5, p. 64). In order to be able to achieve this, Commissioner Cole indicated a need for legislative provisions for new EBA’s to be concluded prior to the expiry date of existing EBA (Cole 2003, vol. 5, p. 64).
Some unscrupulous contractors delayed paying employees wage increases as a way of improving their cash flow. When employees engage in enterprise bargaining to protect and perhaps improve their working conditions the outcomes of the bargaining should commence as soon as possible so that employees receive their agreed entitlements. Commissioner Cole argued that an important incentive for the timely completion of enterprise bargaining negotiations would be “statutory prohibition on agreements providing for retrospective payments of any monetary benefits to employees” (Cole 2003, vol. 5, p. 64). In other words, Commissioner Cole wanted legislation which prevented owners/managers from delaying payment of employee entitlements. Delays added risk because construction companies regularly went out of business meaning employees were not paid what they were entitled to. Ideally, entitlements should be paid when they were due and when the company was solvent and in a position to pay.

The RC also found substantial evidence of “underpayment or miscalculation of workers’ wages and entitlements” (Cole 2003, vol. 7, p. 202). Underpayments and miscalculations may occur inadvertently or deliberately. However, good corporate governance requires any organisation to comply with statutory or award obligations, or obligations under workplace agreements (Cole 2003, vol. 7, p. 202).

While the RC identified superannuation underpayment as an issue, it was more about employers avoiding paying superannuation by encouraging employees to act as subcontractors. Both the unions and suppliers, superannuation funds such as Cbus, indicated that employers tried to comply with superannuation payments for their actual employees. In their submission to the RC, the CFMEU “gave evidence that compliance with superannuation in the industry was probably better than with most other areas of employee entitlements” (Cole 2003, vol. 9, p. 30). The unions indicated that “employers who may not pay other entitlements often choose to pay superannuation and, in some
instances, redundancy payments as well” (Cole 2003, vol. 9, p. 30). The unions took
credit for this arguing that they had to be on-site every day to pressure employers to do
the right thing.

The second type of relationship was with sub-contractors. Sub-contractors were also
exploited by owners/managers by withholding or refusing to make payments.
Commissioner Cole stated that he had “heard a deal of evidence about union demands
upon head contractors and subcontractors that did not, or did not obviously, relate to the
relationship between employers and their employees” (Cole 2003, vol. 7, p. 40). This
language placed the blame for inappropriate behaviour firmly with the unions. The
demands referred to by Commissioner Cole here suggest that the unions had stepped
outside the boundaries of normal industrial relations. In other words, they involved the
unions and union officials themselves, rather than issues affecting employees. “Much of
the evidence associated with these demands by the unions related to inappropriate
payments or enforced donations either to unions funds or charities” (Cole 2003, vol. 7,
p. 40). This raises questions about how these payments were classified and recorded, for
example see processes 1d. and 2b. in figure A1.5 in appendix 1, in particular. How
would an accountant respond if asked by their boss, the company director, to treat a cash
donation to a union official as something else?

The RC found that head contractors, in particular, were willing to “succumb to the
financial demands of unions to buy industrial peace” (Cole 2003, vol. 3, p. 206). This
language includes several very strong words loaded with meaning. The word “succumb”
suggests that the contractors were under considerable pressure; “demands” indicates the
unions expected the contractors to comply; “peace” implies the contractors and unions
were at war; and the combination of “financial” and “buy” leaves no doubt that money
was involved. This strongly worded statement by Commissioner Cole accuses the unions
of extortion, which is an illegal activity. If money was involved this raises the question: how was it transferred from the contractors to the unions? Commissioner Cole found that the money trail occurred this way:

- contractors agreeing to substantial increases in wages and salaries for employees (the unions’ members)
- paying strike pay
- paying donations to the union
- numerous other financial contributions that were demanded (Cole 2003, vol. 3, p. 206).

The RC found many examples of such payments. The following is a sample.

a. In New South Wales union officials sought a substantial ‘donation’ from an employer to help fund a union organiser’s salary to regulate a sector of the industry. A union required an employer to pay moneys to both union related and unrelated organisations in the form of ‘donations’ in return for the agreement to settle an industrial dispute, when in reality these so-called ‘donations’ were in fact penalties or fines imposed by the union.

b. In Victoria head contractors and subcontractors made inappropriate payments to unions and union-nominated funds because of demands by union officials. Union officials demanded that employers make contributions to union funds, linking a positive response to industrial peace.

c. In Queensland head contractors paid union membership fees for subcontractors’ employees to avert the risk of industrial action.

d. In Western Australia payments for casual tickets, ‘specialised training’ and strike pay were all made to unions with the expectation of buying industrial peace.

e. In the Northern Territory a subcontractor made payment for union membership for its employees in order to gain union support for the award of a contract (Cole 2003, vol. 3, p. 207).

One of the main mechanisms for implementing increased wages and salaries for employees as a result of union pressure was over award payments. Over award payment is defined as “any payment and/or benefit above that is set out in the relevant award, registered agreement and/or legislation” (Cole 2003, vol. 7, p. 60). This includes payments provided for in workplace arrangements (Cole 2003, vol. 7, p. 60). “Decisions on over award payments, including superannuation, redundancy, and workers’
compensation insurance, shall be made by the individual employer to suit the needs of
the enterprise” (Cole 2003, vol. 7, p. 60). The problem with over award payments in the
construction industry is that the unions often tried to exert industrial pressure forcing
contractors to pay above award. Commission Cole stated that “no employer may be
compelled to pay benefits above that prescribed in the relevant workers compensation
legislation, … redundancy or superannuation fund” (Cole 2003, vol. 7, p. 60). His
concern was that the unions coerced contractors to pay more than they were legally
required to.

Commissioner Cole found that some unions tried to force contractors to pay members
while on strike. This practice, known as strike pay, was considered unlawful.
Commissioner Cole recommended that “no payments shall be made to employees for
time spent in industrial action, unless payment is legally required or properly authorised
by an Industrial Tribunal where this is permitted by relevant industrial legislation” (Cole

Another way to pay employees more than they were entitled to is found in project
agreements. These are workplace agreements, negotiated between the employer and
employees, where the working conditions are available for the duration of that project
only. However, Commissioner Cole found that these project agreements were being
abused. Unions were negotiating increases in employee entitlements, such as redundancy
pay and superannuation contributions, which should not have been included in project
agreements because they have effect beyond duration of the project (Cole 2003, vol. 7,
p. 61). Commissioner Cole recommended that the only way to avoid this overpayment of
employee entitlement was to ensure the “integrity of individual enterprise agreements
must be maintained” (Cole 2003, vol. 7, p. 61). This means project agreements cannot
override the normal workplace arrangements of individual contractors, and the EBA must be followed.

The third relationship between owners/managers and staff was use of illegal workers. Illegal workers were exploited by owners/managers who paid them low wages. Field operations conducted by the Department of Immigration and Multicultural and Indigenous Affairs (DIMIA) found that “the majority of illegal workers are often paid less than legal entitlements; some were not paying tax, either at the correct rate or at all; and some were claiming social security benefits to which they were not entitled” (Cole 2003, vol. 3, p. 208). Commissioner Cole was highly critical of employers responsible for exploiting migrant labour and avoiding tax because they were using these workers to lower costs and, therefore, compete unfairly with law abiding businesses (Cole 2003, vol. 3, p. 209), as well as avoiding the social contract for paying tax.

Commissioner Cole “considered that the presence of illegal workers in the industry can constitute an instance of unlawful or inappropriate conduct” (Cole 2003, vol. 8, p. 11). He made this claim based on two reasons: foreign nationals who wish to work in Australia must obtain a valid visa with work conditions as “it is an offence under the Migration Act 1958 (C’wth) for foreign nationals to work without permission, or to work in breach of their visa conditions”; and “employers who employ someone without a legal right to work close the position to an Australian citizen or permanent resident” (Cole 2003, vol. 8, p. 11). Those who employ and underpay illegal workers have a competitive advantage, in the form of lower overheads, over those who employ legal workers (Cole 2003 vol. 8, p. 11).
6.2.4 Owners/Managers and Suppliers

The construction industry’s complex contracting system created socio-political power inequities between companies at the various levels of the system, head contractors (large companies), contractors (medium sized companies), and sub-contractors (small companies). In general, whoever wins the construction project holds the economic power and can outsource work to other companies who then acted as suppliers of labour and other project requirements. Power inequities emerged from this complex work relationship between companies. As was discussed in the section on unions and owners/managers, industrial relations was a major source of power disputes in the industry. Fundamental to these disputes was EBA’s, which were workplace agreements designed to ensure adequate working conditions, including employee entitlements were paid.

Owners/managers needed to be aware that some EBA’s made them liable for the employee entitlements of their subcontractors. The RC found that head contractors found project agreements a means of managing risk in respect of employment conditions for all workers on a site (Cole 2003, vol. 5, p. 107). In New South Wales, in some circumstances, “head contractors can be held legally responsible for payments to subcontractor employees that do not meet relevant award and agreement provisions” (Cole 2003, vol. 5, p. 107). Similar provision existed in Victoria and Queensland. This led to the following advice from Commissioner Cole: “accordingly, it is an advantage for head contractors to be aware of and control the work arrangements on projects in relation to employees of subcontractors” (Cole 2003, vol. 5, p. 107).

Commissioner Cole argued that “head contractors had contractual mechanisms available to them to ensure, before progress payments are made, that a subcontractor has paid its
employees” (Cole 2003, vol. 5, p. 107). This means that companies involved in the construction industry should be aware of whether other companies they are working with, such as subcontractors, are making payment to their employees. If a subcontractor is not able to pay its employees, it is technically insolvent, and the contractor should not be able to do business with it. Therefore, it is in the interests of both parties to share information about solvency, more specifically whether the company can pay its employees.

The construction industry’s contracting system also caused problems in the security of payments. The RCR provides several detailed case studies which enable analysis of the role of contractors in security of payment activity. The following case studies show how noncompliance occurred, with a focus on the contracting system. The first case is an example of the contracting system involved in a large construction project, for a shopping mall.

The RC investigated a large shopping centre development constructed by Multiplex Constructions Pty Ltd in Cairns in 1996 and 1997. The project was known as Cairns Central. The Cairns Central case study is particularly interesting for the investigation of security of payment because “a number of subcontractors that worked on the … project went into liquidation or administration, and others suffered severe financial hardship, as a result of payment disputes that arose during the course of that project” (Cole 2003, vol. 8, p. 232). The head contractor on the project, Multiplex, was a very large construction company. It is important to note that the RC did not find that Multiplex in fact owed the amounts claimed by the subcontractors in the case and that Commissioner Cole stated that he did not want to investigate the truth of these claims as it was not an appropriate use of the RC’s resources (Cole 2003, vol. 8, p. 232). However, the case is useful for this analysis because it demonstrated the “type of payment disputes that arise on building
projects, the absence of suitable mechanisms to resolve those disputes and the consequences for subcontractors of being unable to resolve disputes quickly and cheaply” (Cole 2003, vol. 8, p. 232). Therefore, it allows investigation of several of the problems associated with security of payment outlined above.

The evidence presented to the RC about Cairns Central demonstrated that:

- disputes existed between Multiplex and many subcontractors over whether very substantial sums of money were payable;
- these disputes extended over a significant period of time
- there were no suitable mechanisms available for resolving them satisfactorily (Cole 2003, vol. 8, p. 232).

As a result, several subcontractors either went out of business, or accepted amounts far less than they believed that they were owed in full settlement of their claims.

The evidence provided by five subcontractors who worked on the Cairns Central project highlighted problems which the RC was told was common throughout the construction industry. These included disputes about:

- non-payment for approved variations
- whether particular variations had in fact been authorised
- regular late payment or non-payment of progress claims (Cole 2003, vol. 8, p. 232).

These disputes are activities involving accountants. As Multiplex is a very large company, it would have had internal accountants who would have been involved in decisions about payments. Specific evidence presented to the RC by these subcontractors included:

- arbitrary deductions from the claimed amount that have not been discussed
- subcontractors continuing to work despite the non-payment or underpayment of progress claims, in one case because the subcontractor feared liquidated damages of up to $46 000 per day if it refused to do so
• completed extra work that were not paid (for example one subcontractor completed work on over 100 variations, with a total value in excess of $900,000). Not being paid for this work led to severe limitations on subcontractors’ cash flow and operating ability.

• non-payment of progress claims placed subcontractors under serious financial stress, and caused difficulties for them in paying suppliers further down the contractual chain, so there was a domino effect (Cole 2003, vol. 8, p. 232 & p. 236).

One of these five subcontractors tried to explain Multiplex’s behaviour by giving evidence on the reasons for non-payment;

Late payment varied, but: the pattern was that payments were always behind, and never reflected the true amount of work completed. It did not matter that we disagreed with Multiplex, because Multiplex had the money and would pay only what it decided to pay irrespective of the strength of the arguments against its decisions (Cole 2003, vol. 8, pp. 232-233).

In this extract, the problems are about payments and withholding payments. It is relevant in this section on security of payment because it illustrates the complexity of the security of payment problem caused by the construction industry’s contracting system. The problem here is that Multiplex is a very large company which should not need to demonstrate its financial capability to pay when awarded a construction contract. Multiplex could pay. It chose not to. The complexity emerges when the domino effect is considered. The five subcontractors may have been required to demonstrate security of payment to win their respective contracts to work on the Cairns Central project. Therefore, they would have been able to demonstrate their ability to pay their staff and any subcontractors they used on the project. However, the analysis shows that they were not able to meet their financial commitments during the project. This case shows how the subcontractors’ security of payment situation changed over the life of the project due to the behaviour of the head contractor.
In its defence, Multiplex explained that it chose to engage in non-payment or late payment because of not being paid by the client (Cole 2003, vol. 8, p. 233). Another reason given by Multiplex was that the amounts deducted from the progress claims were justified by back-charges (Cole 2003, vol. 8, p. 233). The RC found that:

In some cases the back-charges related to matters said to have occurred weeks or months earlier, and these matters had not been mentioned earlier, at the time they were said to have been incurred, making it impossible for the subcontractors to dispute the back-charges effectively (Cole 2003, vol. 8, p. 233).

Evidence for the abuse of power within the contracting system is provided by this extract from the RCR:

As subcontractors reached the end of their work on the Cairns Central project, many were told when they sought to collect their final progress payment either that none of it would be paid, or that only a small percentage of the amount claimed would be paid. If a small percentage was offered, that was sometimes done on a ‘take it or leave it basis’, with the offer open only for 24 hours, presumably in the knowledge that the subcontractors required cash flow to survive. One subcontractor gave evidence that Multiplex’s construction manager said, on offering $200,000 in final settlement of a claim by the subcontractor for $1,183,745; This is our final offer, that’s all you’re going to get. You can fight us for more if you want, but we have got a building full of lawyers and we can stretch this thing out for years. So even if by chance you were to win, the cost of winning will send you broke long before you get any money (Cole 2003, vol. 8, p. 233, emphasis in the original).

This extract suggests cruel behaviour by the head contractor. The language used is very aggressive and intimidating. The phrase ‘take it or leave’ it is an ultimatum. The pressure to accept the offer is emphasised with the 24 hour time limit. The language in the response from Multiplex, as quoted by the subcontractor, is defiant and inflexible. It indicates that Multiplex felt it had much more power than the subcontractor and that it would not hesitate to exercise this power. The threatening tone of the quote focuses on the emotional vulnerability in this relationship between head contractor and subcontractor caused by threats to financial security and livelihood.
The security of payment problems were highlighted by CCF, which is the peak industry body for all civil construction contractors, and represents more than one third of the civil construction industry, including companies ranging from small and medium to large civil construction, excavation and demolition companies (Cole 2003, vol. 8, p. 235). The CCF told the RC that security of payment problems:

> Are reported to the Federation almost daily where contractors or suppliers in the industry feel they are between a rock and a hard place, not knowing what to do in these circumstances where they have completed work or supplied goods or services in good faith, yet have not been paid (Cole 2003, vol. 14, p. 235).

Several industry groups presented testimony to the RC of the powerlessness of small companies to deal with non-payment or payment delays caused by head contractors. This powerlessness was often described in terms of contractors lacking the financial strength to fight large companies in the courts for payment for work done. Mr Michael Chesterman, the Compliance Manager of the Queensland Building Services Authority (BSA), had supervised several thousand investigations into the financial viability of building contractors, and he gave evidence to the RC “that suggested that the experience of the Cairns Central subcontractors was ‘far from unique’ ” (Cole 2003, vol. 8, p. 235). The National Electrical and Communications Association (NECA) made similar observations, stating that, “To proceed to legal action for a justifiable progress claim or variations would be met with spurious counter claims and endless delays and legal expenses” (Cole 2003, vol. 8, p. 236).

The industry groups explained that head contractors guilty of exploiting these security of payment issues, or what they called ‘rogue builders’, depended upon the financial vulnerability of smaller contractors and delaying tactics. In the latter case, the legal system did not help the victims. These rogue builders relied upon the fact that the
smaller contractors would most likely “run out of resources” before a legal judgment could be reached in the courts.

In summary, the cost for a small contractor to pursue a head contractor for non-payment/slow payment to them was so high that unless the payment dispute was of a very significant nature, in many instances the small contractor made a commercial decision not to take the matter further (Cole 2003, vol. 8, p. 235).

6.2.5 Owners/Managers and General Public

Profit reporting was one of the unlawful activities identified by the RC. This activity involved profit manipulation. This was done for several purposes and for different audiences. Owners/managers might seek to manipulate profit reporting to falsify the company’s financial position to persuade other companies of financial viability when tendering for work, or to mislead regulators and evade tax, or even to avoid the threshold for payroll tax. However, it has been included in this section on the relationship between owners/managers and the general public because profit manipulation has the potential to affect all members of society; particularly investors or shareholders.

The RC provides several detailed case studies which shed light on how employers engaged in inappropriate behaviours associated with profit reporting. The first case is the Sunshine Coast Regional Group Apprentices Ltd. (SCRGAL). The RC found that SCRGAL failed in its corporate governance. The case provides insight about how some construction companies were managed and that this did not meet the social contract. The social contract, in this sense, was to manage the business according to the standards and procedures expected. These standards were specified by the Corporations Act and enforced by the ASIC. The RC citing the New South Wales Court of Appeal made the following statement about a director’s duty:
A director, whatever his or her background, has a duty greater than that of simply representing a particular field of experience. That duty involves becoming familiar with the business of the company and how it is run in ensuring that the board has available means to audit the management of the company so that it can satisfy itself that the company is being properly run (Cole 2003, vol. 10, pp. 183-184).

Commissioner Cole found that the Directors of SCRGAL, and in particular Ms. Alison Grosse, as Chairperson, and Mr Robert Purvis, as Managing Director, failed in the discharge of that duty (Cole 2003, vol. 10, p. 184). The board clearly did not ensure that it had “available means to audit the management of the company so that it can satisfy itself that the company is being properly run” (Cole 2003, vol. 10, p. 184). “By failing to hold any (or any regular) Board meetings, the Directors of SCRGAL breached their duty to the company” (Cole 2003, vol. 10, p. 184). In any company, board meetings should be held regularly and part of those meetings should involve discussing financial statements, which would include profit and loss statements. The failure of SCRGAL to conduct board meetings raises questions about when and how profit and loss statements were discussed by this company. The social contract breach in this case was the failure of the Directors to follow the standards expected by the Corporations Act 2001 in its financial statements. More specifically, the way that debt was disclosed in the profit and loss statements was compromised by loans to directors and employees of the company. This is an example of profit manipulation because the company did not fairly and accurately report its financial performance.

The RC found that SCRGAL made a number of loans to directors or senior staff of the company (Cole 2003, vol. 10, p. 184). The loans were described in SCRGAL’s accounts as “short term investments” (Cole 2003, vol. 10, p.184). All of the loans were unsecured. Commissioner Cole found that “none of the loans were documented when they were made, although some have since been documented” (Cole 2003, vol. 10, p.184). “No
repayment schedules were put in place and no regular repayments” were made for the largest of the loans, (Cole 2003, vol. 10, p.184). “There was no evidence that Fringe Benefits Tax had been paid in relation to any of the loans” (Cole 2003, vol. 10, p.184). There was “no evidence that any of the loans made by SCRGAL to directors or employees were ever discussed or approved by the Board, or by the members of SCRGAL” (Cole 2003, vol. 10, p.184). At the conclusion of the review it was found that “no interest had been paid on any of the loans” (Cole 2003, vol. 10, p.184). Only the three largest loans made by SCRGAL to directors or employees were examined by the RC (Cole 2003, vol. 10, p. 184). Two of those loans were made to Purvis, and one was made to Mr Neil Wilkinson who was company secretary and solicitor (Cole 2003, vol. 10, p.184). The loan to Purvis is discussed as an illustration of inappropriate behaviour. The aim is to identify whether any of the unlawful processes would have been involved. The following is an extract from the RCR.

Purvis and Grosse jointly owned a property at 16 Church Street, Maroochydore. At some time late in 2000 or early in 2001 the decision was made that Purvis would purchase Grosse’s share of that property. The property at 16 Church Street had been valued at $300 000 in June 1999. There was a mortgage over the property with Suncorp Metway for $233 545, meaning that, accepting the $300 000 valuation, Purvis and Grosse held equity in the property of $66 455. In order for Purvis to buy Grosse’s share of the property, he therefore had to pay to her $33 227.50 (Cole 2003, vol. 10, p.184).

On 18 January 2001 three SCRGAL cheques were drawn. They were written out by Wilkinson and signed by Wilkinson and Purvis. The first was a cheque made out to Purvis for $233 545. The second was a cheque made out to Wilkinson for $25 000. The third was a cheque made out to Grosse for $33 227.50. Purvis’ account of the events on 18 January 2001 that led to the creation of those three cheques is as follows:

On 18 January 2001, Neil Wilkinson came to my office. He said to me, ‘Alison (Grosse) has just got off the phone. She wants to know what you’re doing about buying her out?’ I said, ‘I can’t afford it.’ Wilkinson said, ‘Not a problem. Alison and I have discussed it. The company is eligible under its Articles to lend the money. There is enough there – we’ve checked. The company can handle it easily at the moment.’ I said, ‘It might be OK for you and Alison to say this to me, however what about the rest of the Board, have they approved this?’ Wilkinson replied, ‘yes, it’s been approved. As Company Secretary and solicitor
I have advised the Board and Alison that everything is in order and the company is able to do this.’ When Wilkinson left my office, I rang my son who is employed by Suncorp and through whom I was negotiating the loan and said to him that I now didn’t need Suncorp’s loan as the company was now going to lend the money to me. I then got out the joint cheque account which Grosse and I had for the property and wrote out three (3) cheques. One (1) to Grosse for her profit on the property, one (1) to Suncorp to pay out the loan and one (1) for stamp duty. By doing this I was under the belief that the money would be paid to me by way of loan and enter this account as one lump sum. I then went to Wilkinson’s office and told him what I’d done in relation to the cheques and how the money was to be paid. He said to me, ‘No, we’re not going to do it like that. This is the easy way we’ll do it. I have some cheques here for you to sign. This is the way that Alison wants it done.’ I relied on his advice. I went through to sign the cheques and there I noticed in those cheques in the middle of two (2) of the cheques, one (1) being made out to Grosse and one (1) being made out to Suncorp Metway, a third cheque in the name of Wilkinson for $25,000.00. I said, ‘What’s this one for.’ He said, ‘When I was talking to Alison, I mentioned that I had some debts to pay and she said “Oh well, you may as well put them all in together” and I’ve drawn that cheque for that purpose.’ I said to Wilkinson, ‘Are you positive that this is correct’. He said, ‘Yes’ I said, ‘Why is it in the middle?’ He didn’t answer me. I then signed the cheques relying on his advice to me (Cole 2003, vol. 10, p. 185).

At face value, if Purvis’s account is believed, then this directly implicates an individual with a similar role to an accountant in the construction, Wilkinson who was the company secretary and the in-house lawyer, of inappropriate behaviour. The drawing of cheques to provide company directors with loans may involve problems associated with classifying items of expense and revenue; falsifying or altering documents, and concealing significant information. In any case, the claim by Purvis is an illustration of the behaviour of company directors in the construction industry; when faced with allegations of inappropriate financial behaviour they blame company secretaries. In the case outlined above Purvis suggests he only acted inappropriately because the secretary, Wilkinson, told him to.

Commissioner Cole, however, argued that Purvis cannot be believed at face value. Commissioner Cole concluded that “a number of aspects of Purvis’ account are not
credible” (Cole 2003, vol. 10, p. 185). The following evidence to support Commissioner Cole’s statement:

First, Purvis asserted that he asked Wilkinson whether the Board had approved the loan, and that Wilkinson told him that it had been approved and that everything was in order. Leaving aside the language that Purvis suggests Wilkinson used, which is extremely artificial, Purvis knew that Board meetings were almost never held. Purvis was one of just three directors, and he was in complete day to day control of SCRGAL. It is not credible for Purvis to assert that he believed the Board had approved the loan to him. He would necessarily have been aware of any meeting at which such approval may have occurred. He must, therefore, have known that the loan had not been approved by the Board (Cole 2003, vol. 10, p. 185).

Second, it is not credible for Purvis to assert that he signed a cheque to loan Wilkinson $25 000 simply on the basis of Wilkinson’s advice that Grosse had approved it, asking only, ‘Are you positive that this is correct’. It is not at all clear what was supposed to be ‘correct’. Leaving that aside, on his account Purvis claimed that, even though he was the Managing Director of SCRGAL, he did not ask why SCRGAL should lend a substantial amount of money to Wilkinson, nor did he make any attempt to discuss repayment terms, security or interest in relation to the loan. That is despite Purvis’ evidence that he expected his own loan to be documented, and that he would need to provide security. If that was the case, Purvis would have been expected to require the same of Wilkinson. Yet on his own evidence, he did not do so. That casts doubt not just upon Purvis’ claims in relation to the terms of his own loan, but also upon his claims as to the circumstances in which he came to agree to loan Wilkinson $25 000 of SCRGAL’s money (Cole 2003, vol. 10, p.186).

Wilkinson’s account of the events on 18 January 2001 was very different. Wilkinson stated that Purvis told him that all of the money advanced to Purvis by SCRGAL on that day was to be repaid the next week, after Purvis obtained a loan from Suncorp Metway. In other words, he said the loan to Purvis was simply a bridging loan. Wilkinson was not, however, able to give a satisfactory explanation of the need for SCRGAL to provide bridging finance to Purvis. He said Purvis wanted to buy Grosse out to take advantage of a rumoured rise in property prices in the area. A delay of one week, while waiting for finance from Suncorp Metway, would have been very unlikely to frustrate that objective, so that explanation does not explain the need for a loan from SCRGAL. Furthermore, if the loans to Purvis were intended to be for a duration of only one week, it is very unlikely that Purvis would have been prepared to sign a cheque advancing $25 000 to Wilkinson with no agreed repayment schedule, no interest and no security. He would have been treating Wilkinson more favourably than he was treating himself (Cole 2003, vol. 10, p.186).

Commissioner Cole rejected Wilkinson’s evidence that the loans to Purvis were intended to be of short duration (Cole 2003, vol. 10, p.186). Commissioner Cole argued that
“Wilkinson’s evidence that he signed cheques lending $266 772.50 to Purvis for the sole reason that Purvis told him to do so is similarly not credible, and is rejected” (Cole 2003, vol. 10, p. 186). Wilkinson must have been aware of his legal obligations in relation to the company as a practising solicitor. He is unlikely to have breached those obligations simply because Purvis instructed him to do so. His evidence that “he ‘didn’t believe it [the loan to Purvis] to be wrong’ is not credible. Nor is his evidence that ‘If I had my time over, I’d be a much wiser man’” (Cole 2003, vol. 10, p. 186). It must have been obvious to Wilkinson at the time that he signed the cheques that he should not sign them. They were cheques intended to pay a large amount of money for the personal benefit of a director, in circumstances where no board or member approval had been obtained and there was no possible benefit to SCRGAL. Commissioner Cole found that “Wilkinson’s statement that it was not his function to inform the Board about the transaction is unacceptable” (Cole 2003, vol. 10, p. 186). This was due to the fact that Wilkinson was employed by SCRGAL as an in-house solicitor and, in this role, he had a duty to refuse to sign the cheques, and to inform the board (Cole 2003, vol. 10, p. 186). Commissioner Cole concluded that “the probability is that Wilkinson agreed to sign the cheques loaning money to Purvis because Purvis had agreed to lend Wilkinson $25 000” (Cole 2003, vol. 10, p. 186). Commissioner Cole then cites a letter written by Purvis to Wilkinson copied to an internal accountant, Mr Des Robinson, which illustrates how accountants might have been involved in these types of activities. The following extract illustrates the exchange:

An attempt was made by Purvis and Hoiberg to give the above letter to Robinson in or about October 2001. Robinson was told by Purvis or Hoiberg that the letter had just been prepared and back-dated to 23 January 2001. He refused to be involved in the deception. Hoiberg told Robinson ‘Don’t worry, you won’t be asked if the contents of the memo are correct, you will only be asked if you received a copy of the memo.’ Purvis asserted that the letter dated 23 January 2001 was handed to Wilkinson on or about that date, and that he (Purvis) did not keep a copy. He then asserted that the letter that he tried to give to Robinson in or
about October 2001 ‘was not a direct copy of that letter but was prepared at a later date as a reproduction or facsimile of the original’. He stated that ‘the purpose of its reproduction was for Robinson to prepare a loan agreement’ (Cole 2003, vol. 10, p.187).

This is evidence of process 4b. falsifying or altering documents. It is also an important finding that Robinson, the accountant, refused to be involved in the deception. It is very difficult to find specific mention of accountants in the RCR or other publicly available information about the construction industry’s unlawful behaviour. This statement by Commissioner Cole provides support for the proposition that accountants would have been able to at least avoid step 4 in the profit reporting process (see appendix 1, figure A1.7). While accountants might have been involved in steps 1 to 3, they drew the line at fraud, at least from this evidence. This extract is also important for showing the pressure exerted on accountants to do the wrong thing. In this example, the accountant was actually told “don’t worry”, inferring that this was something to worry about, and advised how to behave to avoid detection, “you will only be asked…”.

There was further evidence of the pressure exerted on the accountant, Robinson, by the management and how the accountant refused to cooperate with unlawful behaviour. In preparing a loan agreement, there were several exchanges:

1. Purvis asked Robinson to agree that his signature on the Loan Agreement was conditional upon Wilkinson and Grosse signing similar agreements in relation to loans that SCRGAL had made to them. Robinson refused, saying that he believed Purvis had signed the agreement because it was the only way to do things properly (Cole 2003, vol. 10, p.188).

2. Robinson received a telephone call the next morning from Purvis’ solicitor in which he was told how important it was for Purvis to establish that the Loan Agreement was signed only to put pressure on Wilkinson and Grosse. Purvis’s solicitor also asked Robinson to sign a statutory declaration to that effect, but Robinson refused (Cole 2003, vol. 10, pp.188-189).
These incidents illustrate the pressure exerted on accountants to comply with inappropriate behaviour. It is particularly interesting that lawyers appeared willing to cooperate with management in inappropriate behaviour whereas accountants refused, however, this may reflect the different standards of the individuals involved in this case. A further incident occurred when management asked the accountants to write off the loan:

On about 5 October 2001, following Wilkinson’s refusal to sign a loan agreement, Grosse asked Robinson and Hoiberg whether they could write the loan to Wilkinson off and transfer the amount to a ‘salary bonus’. Wilkinson denied that this was done at his instigation. Hoiberg apparently objected to writing the loan off, because of the fringe benefits tax implications for SCRGAL of doing so. The loan was, however, written off, although that decision was subsequently reversed (Cole 2003, vol. 10, p.189).

This provides further evidence about how the accountants refused to cooperate with management instructions which they felt was inappropriate. In this case, the accountant refused because of FBT implications. However, it is interesting to note that the loan was written off, despite the accountants objections. This suggests that while accountants have objected to inappropriate behaviour, they were not always successful in preventing this behaviour. Although in the above case, the decision was later reversed, which implies that someone, perhaps the accountants, were successful in adjusting the financial statements to reflect appropriate behaviour rather than inappropriate behaviour.

The next situation was an illustration of how auditors were involved in this case. The following extract shows what happened when an auditor found the loan and how management responded:

On 11 October 2001 Purvis sent a memo to Wilkinson which read, in part:

Subject: Loan/Advance – N. Wilkinson
I refer to the above advance to you by SCRGAL. This was advanced to you by way of loan, but as no documentation exists on this, the auditor has asked how this amount should be shown. The accounting alternatives are as follows:

1. Disclose this as a secured loan from SCRGAL to an employee. To do this, you must comply with Loan Documentation which is acceptable to the Directors of this company. This is in keeping with every other person who received this type of advance and have agreed to submit documentation and security adequate to the Directors. It is only reasonable that the company have the same expectation of you.

2. However, you have stated that you do not have assets and you will not sign the appropriate Loan Documentation. Therefore the auditor question’s [sic] the recoverability of this debt and it will have to be treated as a non-recoverable amount.

Consequently, SCRGAL will have to recognise that you will not repay the sum and they will never receive the money back. Therefore, we are advised that we must show this amount as a fringe payment to you and the company will be liable to pay fringe benefit tax of approximately $26,000 (Cole 2003, vol. 10, p.190).

In this extract, management are following the instructions of the accountants, the auditors, to manage the loan appropriately. However, as was discussed above, management were as involved as Wilkinson in this loan agreement. These instructions, apparently drafted by the auditors, seem to be management pretending to be compliant.

It was impression management. The evidence continues:

As a result of this meeting with Alison Grosse, D Robinson and K Hoiberg it has become apparent that SCRGAL are exposed to certain Taxation complications because of your failure to sign Loan Documentation acceptable to this company. This is not acceptable and to protect this company’s interests I offer you the following options:

1. Comply with an Agreement prepared by SCRGAL which acknowledges your debt, provides SCRGAL with an acceptable security against that debt and a planned repayment program.

2. The money you received will be classified as an advance payment against your salary and no further salary will be paid to you until the advance is paid in full.

SCRGAL will pay the additional PAYG Tax on your behalf (Cole 2003, vol. 10, p.190).

Commissioner Cole concluded that:
Probably after the above memorandum was sent, a heated meeting took place between Wilkinson and Purvis. Robinson said that he could overhear part of that meeting, as he was in the next room. He said that Purvis was trying to get Wilkinson to agree that he would repay the money, but that he did not think Wilkinson had any intentions of doing that at all. Wilkinson did ultimately sign a loan agreement (Cole 2003, vol. 10, p.190).

The RC found that this case constituted unlawful behaviour because it contravened s182 of the *Corporations Act 2001* (C’wth). Commissioner Cole asserted that the individuals outlined in this case had a responsibility to distinguish between appropriate and inappropriate behaviour. More specifically, Commissioner Cole highlighted the following from the Act:

The section provided that:

(1) A director, secretary, other officer or employee of a corporation must not improperly use their position to:

   (a) gain an advantage for themselves or someone else; or
   (b) cause detriment to the corporation.

(2) A person who is involved in a contravention of subsection (1) contravenes this subsection.

By deciding to lend himself $266 772.50 of SCRGAL’s money, without providing any security, without agreeing to any repayment schedule, and on interest-free terms, Purvis improperly used his position as a director of SCRGAL to gain an advantage for himself (Cole 2003, vol. 10, p. 193).

Commissioner Cole found Purvis engaged in unlawful conduct. He found Wilkinson, the internal lawyer, equally at fault, because he “improperly used his position as either an officer or employee of SCRGAL to gain an advantage for someone else” (Cole 2003, vol. 10, p.193).

The next detailed case study provided by the RC involves Multiplex Constructions (NSW) Pty Ltd and payments to Comet Training Pty Ltd. In this case, an irregular payment classified as sponsorship was made to Comet. This analysis looks at how this
occurred, how it may have affected profit reporting, and the role of accountants. The following extract explains what happened:

From July 1997 to July 2002 Multiplex Constructions (NSW) Pty Ltd (Multiplex NSW) paid Comet Training a total of $1,245,484. An examination of the relevant accounts revealed that of that $1,245,484:

(a) $381,652 was paid for training services actually provided by Comet Training on a fee for service basis;
(b) $438,771 was paid through Comet Training to a safety consultancy company, HVG Enterprises Pty Ltd (HVG Enterprises); and
(c) the balance of $425,061 was retained by Comet Training for what is now described as payments by Multiplex NSW in the form of sponsorship (Cole 2003, vol. 13, p.257).

Commissioner Cole called for evidence “to examine the nature of the ‘sponsorship’ payments totalling $425,061 to Comet Training and examine why Multiplex NSW paid this amount and what it stood to gain from doing so” (Cole 2003, vol. 13, p.257).

The key players in this case were: Mr Ian Gavin, Director, HVG Enterprises Pty Ltd and a former senior union official (Cole 2003, vol. 13, p. 257); Mr David Higgon, the Employee Relations Manager for Multiplex Constructions (NSW) Pty Ltd (Cole 2003 vol. 13, p. 257); Mr Raymond Harty, the General Manager of Comet Training Pty Ltd; and Multiplex senior manager Mr Stagg (Cole 2003, vol. 13, p. 258). The background is explained by these extracts from the RCR:

In early 1997, Higgon approached Gavin to consider a long term occupational health and safety related role with Multiplex NSW. The primary role for Gavin as proposed by Higgon involved the auditing of safety on Multiplex NSW projects. Higgon asked Gavin to consider working as an independent contractor through Comet Training. Higgon said this arrangement would involve Gavin setting up his own company, entering into a subcontract arrangement with Comet Training, providing safety consultancy work for Multiplex NSW and being paid by Multiplex NSW through Comet Training (Cole 2003, vol. 13, p. 257).

It appears that Higgon broached the topic of Multiplex NSW sponsoring Comet Training at a meeting with Gavin in late 1996 or early 1997. Higgon told Harty that Multiplex NSW would like to sponsor Comet Training as part of its support for the industry initiative in relation to health and safety training. At this meeting Higgon told Harty that Multiplex NSW would pay Comet Training $16,000 per
month and that it could contract its audit and advice work for Multiplex NSW to Gavin, and pay him $6700 per month with the balance to be retained by Comet Training. Harty said that Higgon told him that the balance of the money would be sponsorship by Multiplex NSW for Comet Training’s general work to ensure that there were sufficient properly trained skilled labourers in the building and construction industry (Cole 2003, vol. 13, p. 258).

When questioned why the excess moneys paid to Comet Training would be retained by it, Higgon said he was aware that in all likelihood there would be moneys in excess of those paid to Gavin and was quite prepared to have those excess funds used by Comet ‘to promote their business’ and that the excess would ‘probably be something quite significant’. Harty said that it was always his understanding that the balance of the money paid by Multiplex NSW would constitute sponsorship of Comet Training. Stagg considered the balance of moneys paid to constitute a ‘profit component’ which could be described as ‘sponsorship or whatever’. Ferguson said that he was aware that Multiplex NSW provided ‘financial support for Comet’ but that was the extent of his knowledge (Cole 2003, vol. 13, p. 258).

Stagg made the decision to pay Comet Training the total figure of $16 000 each month. He said he had arrived at this figure by considering the costs that would be involved in employing someone directly, even though in excess of 50 per cent of the payment did not relate to the services to be provided by Gavin. Higgon said that Multiplex NSW did not have anything in writing at the time the arrangement was entered into suggesting that part of the payment was related to sponsorship of Comet Training. Stagg had never asked Higgon to prepare any proposal to put to the Multiplex NSW Board of Directors in relation to the provision of sponsorship to Comet Training (Cole 2003, vol. 13, p. 258).

At the RC hearings, a director of Comet Training, Mr Ferguson, indicated “he was aware that Multiplex NSW was making a substantial payment to Comet Training but did not know the exact amount of money being paid” (Cole 2003, vol. 13, p. 259). He said he was aware that “Multiplex NSW was paying a surplus amount to Comet Training which he regarded as a form of sponsorship although he said he could not recall when he first attained that knowledge” (Cole 2003, vol. 13, p. 259). He said he “did not recollect ever being advised that such sponsorship moneys were being paid in his position as a director of Comet Training” (Cole 2003, vol. 13, p. 259). This is evidence that directors were ignorant or pretended to be ignorant about financial details associated with inappropriate behaviour in the construction industry. If Ferguson is to be believed, then who was aware?
The first step in this process was when the first invoice for services rendered by Comet Training was forwarded to Multiplex NSW on 4 July 1997 (Cole 2003, vol. 13, p.259), when an administration officer for Comet Training, in all likelihood an accountant, wrote to Higgon advising that “Multiplex NSW would be invoiced on the first business day of each month as has previously been raised by the CFMEU” (Cole 2003, vol. 13, p. 259). This reveals that the unions were involved in this deal between the former union member, Gavin, and Multiplex (construction company) and Comet (training provider).

The second step in this process was payment of the invoice. To make this arrangement work, Comet invoiced Multiplex, and Gavin invoiced Comet, as a subcontractor via his own company HVG Enterprises. Comet Training paid HVG Enterprises from moneys received from Multiplex NSW upon receipt of HVG Enterprises’ invoice, (Cole 2003, vol. 13, p. 259). “The first payment of $16 000 from Multiplex NSW to Comet Training occurred on 4 July 1997” (Cole 2003, vol. 13, p.259). The description on the first invoice was “‘Occupational Audit/Safety Program, 4 weeks commencing 1 July 1997’” (Cole 2003, vol. 13, p.259). The RC found that “this description accurately described the service provided by HVG Enterprises to Multiplex NSW” (Cole 2003, vol. 13, p. 259). Therefore, the process of classifying items of expense and revenue, appears to be followed correctly. However, the RC found that the description of the invoice “did not distinguish between the component that was covering the cost of HVG Enterprises and that component representing sponsorship when invoicing Multiplex NSW” (Cole 2003, vol. 13, p. 259). Therefore, this is evidence that process 1d. was followed incorrectly. At worst, it could be claimed that the concealment of moneys as sponsorship is process 4e., concealing significant information, or even 4d., recording forged transactions; both of which are fraud.
In relation to the “sponsorship” arrangement, when explaining why the invoices did not properly describe the arrangement between Comet Training and Multiplex NSW, “Harty said that even if the word sponsorship had never been mentioned, the excess could simply have been a ‘mark-up’ on the services provided by Gavin” (Cole 2003, vol. 13, p. 259). This would have been an example of creative accounting; more specifically process 3e., increase or decrease net income at will. Harty further defended the practice by saying “that Comet Training described the invoices in a way that Higgon had requested”, thereby placing blame with Multiplex (Cole 2003, vol. 13, p. 259). This exchange illustrates two interesting cultural norms within the construction industry regarding profit reporting. First, creative accounting appears acceptable, as Harty quickly used it as a defence against wrongdoing. Second, accountants appeared to follow instructions with a defence that it was the other parties’ fault if things emerged as inappropriate. This latter conclusion is based on Harty’s defence that the invoices were simply described as requested. Accountants simply followed instructions.

As this practice continued over the next few years, some people questioned it. The ATO audited Comet Training in 2001, and found that “at no time was the ATO notified that the description on the invoices as ‘training’ did not properly reflect the nature of the service provided by HVG Enterprises to Multiplex NSW” (Cole 2003, vol. 13, p. 260). When Harty was later questioned by Commissioner Cole, he stated that he “did not believe that the ATO was being misled as to whether GST should have been paid” (Cole 2003, vol. 13, p. 260). Commissioner Cole found that Mr Brian Seidler, Executive Director of the MBA of New South Wales and Director of Comet Training Pty Ltd, first became aware of the sponsorship arrangement between Multiplex NSW and Comet Training in late 2001 (Cole 2003, vol. 13, p. 260). It is insightful that a director of one of the companies involved, Comet, did not know about this practice for four years. This
illustrates how inappropriate behaviour could be easily hidden. In response, Seidler worked with Mr Alex Stuart, President of the MBA of New South Wales, also a board member of Comet Training Pty Ltd to organise a letter from Comet to Multiplex formally thanking them for “continuing support of skill development and skill formation in the building and construction industry” (Cole 2003, vol. 13, p. 260). Seidler and Stuart later told Commissioner Cole that they were concerned that “the arrangement between Comet Training and Multiplex NSW should be clearly articulated for what it was” (Cole 2003, vol. 10, p. 349). In other words, they wanted to be honest about the arrangement.

The RC hearings surfaced some of the activities of staff involved in the arrangement between Gavin, Multiplex and Comet. The following extract from the RCR illustrates the role of Multiplex’s senior accountant: the company secretary:

On 12 April 2002 Mr Darrin Smith, Company Secretary of Multiplex Constructions (NSW) Pty Ltd, wrote to Comet Training seeking to have amended tax invoices issued by Comet Training properly describing the work performed, namely ‘safety audits’, and to include the 10 per cent GST component in the invoices. Harty refused to change the description as the invoices had been subjected to an ATO audit. It became apparent to Harty at a meeting with Smith to discuss the invoices that Smith was not aware of the arrangement between Multiplex NSW and Comet Training in respect of the sponsorship (Cole 2003, vol. 13, p. 261).

This is a particularly important passage in the context of this thesis. It provides evidence supporting the proposition that accountants were not involved in unlawful behaviour in the construction industry. In this case at least, the accountant, Smith, appears unaware of the fraudulent activity involved in the sponsorship payments. There were also changes to the practice after the meeting between Smith and Harty. The invoices were described differently and there were now separate invoices for safety audits and sponsorship. The amount of the sponsorship was also decreased. It seems that in this case at least,
accountants sought to correct inappropriate behaviour when they became aware, and to take steps to introduce appropriate behaviour. However, the fact that Smith was a very senior accountant, company secretary of a large construction company such as Multiplex, meant he would have authority and power to impose his will. Accountants working in smaller companies or external accountants depending upon their clients for income, may have had less ability to bring about appropriate behaviour.

The RC found some unusual features in the relationship between the unions and Comet. First, “Comet Training was an initiative of the CFMEU aimed at spreading its influence in the industry by the provision of training services” (Cole 2003, vol. 13, p. 261). Second, Comet Training was a tenant of the CFMEU, and “since October 1996, the CFMEU has received from Comet $1 196 146.53” in rent (Cole 2003, vol. 13, p. 261). Therefore, there were commercial and strategic interests from the unions in Comet’s business success. The RC suggested that this whole practice was a “donation or sponsorship by Multiplex NSW to foster training in the industry, except that Multiplex NSW went to considerable trouble to disguise the fact, if it be the fact, that it was sponsoring training in the industry” (Cole 2003, vol. 13, p. 261). This raises questions about the practice of “sponsoring” unions and other stakeholders in the construction industry. The allocation of money to sponsor is usually associated with an expectation of receiving something in return. Multiplex were, in effect, paying money to the unions disguised as sponsorship.

The RC found that this case study was indicative of falsifying invoices in the construction industry. Whether this was creative accounting or fraud, is a matter of opinion and might be considered a fine line. Commissioner Cole appeared to focus on the fact that “invoices rendered by Comet Training did not truly disclose the service for which the invoice was rendered” (Cole 2003, vol. 13, p. 262). This was misleading.
Whether it was falsifying documents or concealing significant information is a matter of debate. There is, however, good news for accounting practice in this case study. Commissioner Cole found that the parties involved only began to manage this matter appropriately when a senior accountant became aware there was a problem. Commissioner Cole commented “there was never any reference to sponsorship before the Secretary of Multiplex NSW became aware of the arrangement” (Cole 2003, vol. 13, p. 261). When Smith discovered what was happening, he addressed the situation. This provides support for the argument that accountants could play a role in addressing unlawful behaviour and address the societal contract breach.

The RC contained numerous other similar case studies highlighted inappropriate behaviour associated with profit reporting.

**6.2.6 Owners/Managers and Project Managers**

Project managers play an important role in construction companies. They manage all aspects of a building project often as a turnkey task, that is, from design to hand over to the customer. This includes managing operations and costs, as well as subcontractors. The following case described in the RCR illustrates the role of project managers working for a large construction company.

Mr Adrian Powell is a Project Manager employed by Westfield Design & Construction Pty Ltd (a large construction company). As Project Manager, he has overall responsibility for the day to day running of the project he is employed to manage. A number of site-based personnel report to him and, in turn, he reports to a General Manager at Westfield Design & Construction Pty Ltd in Sydney. Powell was responsible for project management at Westfield shopping centres at both Airport West and Fountain Gate. Westfield Design & Construction Pty Ltd and Powell considered $20 000 to be a figure which represented a real and reasonable contribution to a worthy cause, such as the establishment of an occupational health and safety unit. Powell subsequently received approval to make the donation to the CFMEU FEDFA Division occupational health and safety unit by two instalments of $10 000 each plus GST. Powell told Hallet (his boss) about the contribution and indicated that the payment of the second instalment was conditional on the CFMEU FEDFA
Division continuing its good relationship with Westfield Design & Construction Pty Ltd by not adopting an unreasonable stance in relation to future forklift operations at the site. On 1 December 2000 Westfield Design & Construction Pty Ltd received a tax invoice from the CFMEU FEDFA Division for $11 000 in relation to its ‘Health and Safety Campaign’, for ‘Services relating to education, plus preparation, production and distribution of literature for improved health and safety in the building construction industry.’ The payment of this invoice was approved by Powell. The invoice was paid on 19 December 2000 (Cole 2003, vol. 16, p. 273 & p. 279).

This type of transaction was an example of how union officials demanded money from large companies, as well as small companies, in return for industrial peace. While a project manager approved the payment of the invoice, it raises questions about whether accounting staff have queried an invoice from a union about educational services.

6.2.7 Summary Comments

This section looks at whether members of the social network listened to accountants and, if so, whether they adjusted their behaviour accordingly. A fundamental cause of the problems that led to the RC was that the industry’s management were influenced by the demands of different stakeholders, the unions in particular. The RC also found non-industrial relations issues such as tax evasion and unlawful acceptance and reporting of commissions/cash payments. This section examines which stakeholder groups influenced these behaviours and why. A fundamental structural problem within the construction industry was short-term focus. Those stakeholders with long-term interests, that is the unions, were aware that those with a short term focus were vulnerable to project delay and cost. Those stakeholders with a short-term focus such as owners/managers, knew that to cooperate with the unions was a better economic alternative to conflict with the unions. This created an inequality of bargaining power. The following analysis summarises how these socio-political inequities influenced the social relationships between stakeholders.
The main battle for power between stakeholders was between owner/managers and unions. The RC contains considerable evidence that the unions tried to exert power over owners/managers. The first impact of this behaviour was unions threatening to expose employers to regulators. The most common threat was to expose tax evasion. Case studies involving Hackett Laboratory Services, The Civil Management Group Pty Ltd, and Cables at Cammeray site were used to illustrate the aggressive behaviour of unions to achieve their aims. Commissioner Cole found that the unions behaved this way to ensure better working conditions for their members, defined by EBA’s. While this is a legitimate activity, the unions often went about achieving this aim illegitimately.

The unions used various methods to coerce owners/employers to comply with their demands and numerous case study examples are scattered throughout the RCR. A principal tactic of union officials was to use tax evasion as a threat. This involved threatening owners/managers that union officials would contact the ATO with accusations of tax evasion. This implicates construction companies in two of the seven unlawful activities – tax evasion and payroll tax – for two reasons: union officials must have been aware of unlawful activity and the fact that owners/managers complied in response to the threat suggests they did not want the accusation to be made. This suggests there was unlawful behaviour and the owners/managers did not want the authorities to know.

A third of the seven unlawful activities - inappropriate payments – was also found in this section. An example of unions demanding financial contributions was a practice called dual ticketing. This practice begins with coercion to ensure employees are union members. A response from some employers was to purchase casual tickets (that is, memberships) as a means of avoiding industrial disruption is a problem. Westfield Design and Construction Pty Ltd (Westfield) in Victoria provided an interesting case
study to illustrate the practice, because it reveals evidence about accounting practice associated with making and receiving payments. Associated with buying industrial peace, some unions negotiated workplace agreements with contractors which included inappropriate payments in the agreements.

The relationship between owners/managers and staff was different. In this case, owners/managers held power over staff and exploited them for financial gain. Owners/managers had three types of relationships with staff. First, full-time employees were exploited by owners/managers by withholding or refusing to pay employee entitlements. This was the fourth of the seven unlawful activities. Some unscrupulous contractors delayed paying employees wage increases as a way of improving their cash flow. The section showed evidence of underpayment or miscalculation of workers’ wages and entitlements. The second type of relationship was with sub-contractors. Sub-contractors were also exploited by owners/managers by withholding or refusing to make payments. Commissioner Cole found that some unions tried to force contractors to pay members while on strike. This practice, known as strike pay, was considered unlawful. The third relationship between owners/managers and staff was use of illegal workers. Illegal workers were exploited by owners/managers who paid them low wages. Illegal workers are often paid less than legal entitlements; some were not paying tax, either at the correct rate or at all; and some were claiming social security benefits to which they were not entitled.

The construction industry’s complex contracting system created socio-political power inequities between companies at the various levels of the system, head contractors (large companies), contractors (medium sized companies), and sub-contractors (small companies). Power inequities emerged from this complex work relationship between companies and revealed problems in the fifth of the seven unlawful activities: security of
payments. Head contractors called rogue builders, depended upon the financial vulnerability of smaller contractors and delaying tactics.

The sixth of the seven unlawful activities - profit manipulation was done for several purposes and for different audiences. Owners/managers might seek to manipulate profit reporting to falsify the company’s financial position to persuade other companies of financial viability when tendering for work, or to mislead regulators and evade tax, or even to avoid the threshold for payroll tax. It was included in this section on the relationship between owners/managers and the general public because profit manipulation has the potential to affect all members of society; particularly investors or shareholders.

The seventh of the seven unlawful activities – phoenix company activity – was purely self-interest by owners/managers and was not included in this section on social relationships between stakeholders.

6.3 Expectations

6.3.1 Introduction

The third ST construct was expectations. In order to understand the social reality of accounting from a critical theory perspective, PET is used. This theory elucidates that the strategic outcomes of accounting practices favour specific interests in society and disadvantage others (Cooper & Sherer 1984, p. 208). The differing interests of the social actors may explain the social praxis underlying the behaviour leading to the construction industry’s legitimacy gap. In this section, the construction industry’s multiple social contracts are examined. These explain what society expected of the industry. The
analysis highlights stakeholder expectations of one another as well as the construction industry’s legitimacy gap, that is, the difference between society’s desired behaviour and actual behaviour. The analysis will explore whether accounting played a role in this legitimacy gap either by contributing to the undesired behaviours or by improving the behaviours.

The main societal expectations of the construction industry were:

1. Contribute to public funds. This was an expectation that construction companies would meet their corporate citizenship responsibilities and pay taxes. In this way, they would contribute to the funds gathered by government to be shared with all of society through government services. Tax evasion was the main problem in this area.

2. Pay employees their entitlements. This was an expectation that individuals employed by construction companies would receive their salary and non-salary reward for their work. Underpaying employees or avoiding payment altogether through insolvency were the main problems in this area.

3. Pay suppliers their entitlements. This was an expectation that companies and individuals who provide materials and services to construction companies, including sub-contractors, be paid appropriately in return. Delaying or withholding payments was the main problem in this area.

4. Accurate performance reporting. This was an expectation that construction companies would honestly and accurately report on their business activities, including profit reporting. Society includes public and private investors; as well as other stakeholders interested in the financial position of construction companies such as customers, creditors (for example banks), suppliers, and regulators. These stakeholders want to know if they will get a return on their investment, have their
building project completed, and whether they will be paid. Profit manipulation was the main problem in this area. These expectations emerged from the analysis. Based on the findings about the nature of the social contract breach surrounding the seven unlawful activities, these four expectations summarized what society expected the construction industry to do to repair its legitimacy and bridge the social contract gap.

Commissioner Cole was scathing in his criticism of the construction industry’s unlawful behaviour. While he is often highly critical of unions and sympathetic towards employers, he concludes that “every participant bears some responsibility” (Cole 2003, vol. 3, p. 211). His most aggressive criticism of the industry emerges when he describes participants as uncivilised: “civilised standards of the kind which would be expected by ordinary Australians have too often evaded workplace relations in the building and construction industry” (Cole 2003, vol. 3, p. 211). The use of words such as civilised standards by Commissioner Cole, illustrates the industry’s inability to satisfy societal expectations.

**6.3.2 Contribute to Public Funds**

*6.3.2.1 Societal Expectation*

The first expectation of society regarding the construction industry was that it should contribute to public funds. Companies must pay tax on income earned. There are particular accounting rules and conventions related to the recognition of expenses and income which lead to the determination of accounting profit.

Society expects two outcomes from companies in terms of the issues outlined above. First, society expects companies to make a profit. This would reflect that the company is using the resources allocated to it by society wisely. This is reflected in accounting
profit. Investors and other stakeholders are happy if there is accounting profit and it reflects good performance from the company. Second, society also expects the company to pay taxes. Taxes on income are paid by all citizens of society. These taxes help pay for essential government services such as education, health, defence, and infrastructure. It is expected that all members of society, including companies, contribute towards these services by paying taxes. Individuals and organisations who try to avoid making their contribution to these essential government services, by not paying their taxes, are considered outlaws, in the sense that they are not meeting society’s expectations of them. This is reflected in profit gained from tax evasion.

The Federal and State Governments in Australia have also seen payroll tax as a problem area for many years. This perception was created by two factors. First, companies have tried to avoid paying payroll tax. Second, the governments have varied in their treatment of payroll tax. As a result, considerable government revenue has been lost due to non-payment, and governments have found it difficult to respond. Part of the problem was inconsistency in the treatment of payroll tax which created confusion for companies and the regulators. In response the governments have moved towards a consistent approach to payroll tax, called harmonisation. This is described in the following extract:

A Protocol for Payroll Tax Harmonisation between Jurisdictions (Signed 28 July 2010):

On 29 March 2007 State and Territory Treasurers announced a decision to overhaul payroll tax arrangements to achieve greater legislative and administrative harmonisation. Payroll tax harmonisation was endorsed and continued by the Council of Australian Governments as one of 27 projects designed to achieve a National Seamless Economy. Under the National Partnership Agreement to Deliver a National Seamless Economy, the States and Territories were responsible to work together to produce a nationally coordinated approach in relation to payroll tax, and complete the reforms by 1 July 2012. All jurisdictions have taken steps to enact legislation aligning provisions in eight areas agreed to by State and Territory Treasurers. Further, New South Wales, Victoria, Tasmania, Northern Territory and South Australia have enacted identical payroll tax legislation, apart from minor differences identified in schedules to the legislation. Queensland has also passed legislation to establish
harmonisation with those jurisdictions. On 11 July 2008 the Commissioners of all State and Territory Revenue Offices signified their commitment to establishing and maintaining consistency in the administration of payroll tax. In order to implement arrangements for harmonised administration, the Commissioners established the Payroll Tax Harmonisation Committee in December 2008. The role of the Committee is to oversee the design, implementation and maintenance of an administrative framework to support the goal of harmonisation of payroll tax administration, and it has already undertaken significant work to advance harmonised administration. (2012 - The work of this committee is now undertaken by the Tax Law Committee.) By signing this Protocol the Commissioners agree to continue their high level of cooperation and consultation in order to further payroll tax harmonisation (Payroll Tax Australia 2010, paras. 1-6).

Payroll tax is a self-assessed, general purpose state and territory tax assessed on wages paid or payable by an employer to its employees, when the total wage bill of an employer (or group of employers) exceeds a threshold amount (Payroll Tax Australia 2010). The payroll tax rate and threshold amount vary between states and territories. Payroll tax returns are lodged and payment of liability is made at an agreed frequency (monthly, quarterly, or annually) to the respective revenue office in the Australian state and/or territory in which the wage payment is deemed liable (Payroll Tax Australia 2010). The Australian states and territories agreed to harmonise a number of key areas of payroll tax provisions in order to address inconsistencies across the country (Payroll Tax Australia 2010). However, payroll tax administration differs between the states and territories in other areas (Payroll Tax Australia 2010).

6.3.2.2 Societal Contract Breach

The RC found “avoidance and evasion of taxation obligations” (Cole 2003, vol. 1, p. 6). It was clear that the regulator, the Australian Federal Government, was very concerned about taxation misconduct within the construction industry before, during and after the period of the RC. The RC recommendations included the need for the industry to achieve compliance with taxation laws (Cole 2003, vol. 9, p. 90). An investigation
conducted during the same period by the DEWR Report in 2003 announced that the industry reform program included steps to combat tax evasion. The second BIT Report in 2005 also recommended that there was need to combat tax evasion. This trail of regulator intervention reveals that tax misconduct continued after the RC. It seems that the behaviour was embedded within the industry’s culture and was accepted as a normal part of doing business.

Tax evasion within the construction industry occurred as follows:

1. Income tax evasion by persons and entities
2. Payroll tax evasion
3. Phoenix company activity

Commissioner Cole stated that:

The avoidance and evasion of taxation obligations is relevant to the Royal Commission Terms of Reference because it affects the building and construction industry at a number of levels. It affects the public taxation revenue raised from the industry, it puts law abiding contractors in a non-competitive situation, and it can turn legitimate employees into contractors (Cole 2003, vol. 9, p. 51).

The significance of the problem of inappropriate income tax activity within the construction industry at the time of the RC is illustrated in three ways. First, estimates by the ATO. The ATO Submission to the RC (exhibit 0714), questioned “the utility of estimating ‘revenue leakage’, and states only that, with respect to the building and construction industry, this ‘leakage’ is ‘significant’” (Cole 2003, vol. 12, p. 234). It was suggested that “$354 million worth of income tax is evaded or avoided in the industry each year” (Mr Wallace Trohear in Cole 2003, vol. 12, p. 234), but Commissioner Cole qualified this by emphasising this was an estimate, and “there is no empirical data in evidence which might support this figure” (Cole 2003, vol. 12, p. 234). Second, efforts to recoup tax avoided. Since 1998, the “ATO has recovered over $370 million in tax in
Third, the unions used tax evasion as a way to threaten employers (Cole 2003, vol. 12, p. 484; Cole 2003, vol. 13, p. 34). There are specific cases in New South Wales and the Australian Capital Territory where union officials threatened to call the ATO and tell them to conduct audits of contractors and their employees if industrial demands were not met. The fact that unions could make this threat, and contractors backed down in the face of the threat, suggests the reality and widespread practice of tax evasion within the construction industry at that time.

Income tax evasion occurred within the construction industry in several ways. In his submission to the RC, Mr Ian Read, Assistant Commissioner of Taxation in the Small Business Line of the ATO, stated that “the level of non-compliance in this industry is significant, and if left unaddressed would pose a risk to ongoing revenue collections” (Cole 2003, vol. 9, p. 56). He gave evidence describing the ATO’s interpretation of tax evasion activities conducted by the construction industry:

- untaxed cash payments including salary and wages, overtime, rostered days off (RDOs) and bonuses
- ‘bodgie’ or bogus labour hire companies
- phoenix activity
- fraudulent claims for GST Input Tax Credits;
- false claims for Tax Instalment Deduction by directors of phoenix companies (Cole 2003, vol. 9, p. 56).

A major cause of tax evasion behaviour was the industry’s complex contracting system. Much of the evidence presented to the RC regarding tax evasion involved smaller companies, even sole traders. While larger contractors were implicitly involved because they would have cooperated in activities such as cash payments, they may appear to have engaged less in tax evasion compared with smaller companies. However, the Australian Taxation (ATO) submission to the RC provides a different picture. The ATO stated that it “undertakes a structured process in relation to ‘large clients’” and “of the
top 200 such large clients, 17 were from the property and construction industry”, that is 8.5% (Cole 2003, vol. 9, p. 62).

The ATO providing evidence that large construction companies also engaged in tax evasion. In 2015 the problem still existed. Ryan (2015) reported a senate enquiry of Australia’s top 40 companies to examine why these companies pay so little tax. Tax evasion appears to be common practice for large companies as well as small companies across all industry sectors. The ATO has identified that large companies engaged in tax evasion in the following ways:

- tax planning as a strategy used to minimise the tax liabilities of these entities. In this group of taxpayers the ATO uses as a major tool a Client Risk Review, which examines the economic performance of the corporate group as a whole and includes financial analysis and qualitative profiling. The ATO has conducted such reviews on the top 200 large clients. The ATO submission states that recent projects covering large clients have involved examination of major construction and infrastructure projects and loss utilisation (Cole 2003, vol. 9, p. 62).
- The ATO states that the particular risk issues involving large clients relate to:
  - Division 10D write back
  - Capital and revenue losses

The ATO concluded that “the tax planning and other behaviours of the 17 entities in the property and construction industry are consistent with those entities in other industries” (Cole 2003, vol. 9, p. 62). In other words, large companies in the construction industry may have engaged in tax evasion in ways similar to large companies in other industries.

One of the peculiarities of the contracting system with particular relevance to tax evasion was the widespread use of subcontractors. In the construction industry, skilled workers often “do not want to work as employees and want to run their own businesses, seeing subcontracting as rewarding effort and providing better financial incentive” (Cole 2003, vol. 3, p. 207). Employers (large contractors) argue that subcontracting is a benefit to all parties: “it rewards productivity, innovation and quality [and] … makes individuals
responsible for their own well-being” (Cole 2003, vol. 3, p. 207). Unions, on the other hand, argue that “many workers become subcontractors to avoid paying tax or because they are required to by employers trying to avoid paying them their proper entitlements” (Cole 2003, vol. 3, p. 207). In either case, the use of subcontractors encourages activity such as tax evasion.

Evidence provided to the RC argued that there were two types of “illegitimate contractors”:

1. those that want to operate that way and flaunt, in general terms, the tax and industrial systems for greater in hand returns
2. those that are told to be subcontractors to minimise the labour-related overheads of their employers (Cole 2003, vol. 12, p. 445).

The PC recommended banning pyramid subcontracting on commercial building sites following concerns about “artificial labour only contractor arrangements which were designed to avoid legal responsibility for employee entitlements and tax payments, and the poor occupational health and safety practices associated with some of these contractors” (Cole 2003, vol. 4, p. 104). The PC proposed “that the extent of pyramid subcontracting should be at the discretion of the head contractor” because sometimes it was economically beneficial, so long as unlawful behaviour was not involved (Cole 2003, vol. 4, p. 105).

The RC provided case studies of pyramid contracting; including:

- The No.1 The Esplanade, Glenelg case study involving Rapid Building Services (SA) Pty Ltd

There was also evidence in the RCR that some major contractors (large companies) enforced the pyramid subcontracting prohibition (Cole 2003, vol. 12, p. 253), which essentially demanded subcontractors and their workers to become employees against
their will (Cole 2003, vol. 12, p. 253). This was illustrated by a case study on Timbercraft Pty Ltd.

The unions were particularly concerned about a practice they called “sham contracting”. They argued this had a significant effect on taxation revenue and the proliferation of incorporation and the use of ABN’s. Senior union official John Sutton’s evidence to the RC included the following: “by far the biggest problem in the building industry [is] the misclassification of workers as so-called independent contractors and there’s massive amount[s] [of] tax being lost to the Australian Government” (Cole 2003, vol. 9, p. 63). On behalf of his union, the CFMEU, Sutton argued “unless we can do something about the massive tax fraud epidemic, we can’t seriously address the question of wages and conditions … because about half of all blue collar workers are … being classified as non-employees” (Cole 2003, vol. 9, p. 63). This statement explains why the unions were so interested in exposing tax evasion in the construction industry. Sutton’s testimony indicates the union’s view of the illegality of tax evasion behaviour, and the use of the word “massive” illustrates the extent of this unlawful behaviour, it was widespread.

Mr Richard Williams, Secretary of the Electrical Trades Union of Australia, Queensland Branch and Secretary of the Queensland Branch Electrical Division of the Communications, Electrical, Electronic, Energy, Information, Postal, Plumbing and Allied Services Union of Australia, gave evidence to the RC indicating widespread use of working arrangements to evade or avoid taxation (Cole 2003, vol. 9, p. 63). He exposed that “on some sites, contractors from the housing industry may pay cash in hand and the workers be treated as contractors while they were working alongside workers being paid under enterprise bargaining agreements as employees” (Cole 2003, vol. 9, p. 63). This statement illustrates again how the unions’ interest in tax evasion was because
it effected their members who they felt were treated unfairly because they were not engaging in tax evasion.

Bill Shorten of the Australian Workers Union (AWU), the Federal Opposition Leader at the time of writing, highlighted the use of bogus subcontracting as a major contributor to the avoidance of taxation within the industry (Cole 2003, vol. 9, p. 64). He referred to the 1999 Review of Business Taxation (the Ralph Report 1999) which recommended “that many subcontractors who were in fact really employees should be taxed as such as the economic reality of earning their income is unchanged, their income should be taxed on the same basis as other PAYE income” (Cole 2003, vol. 9, p. 64). Shorten is explaining that employees, for example union members, were being exploited by employers in order to gain tax evasion benefits and this was unfair.

The RC cited a report by Dr John Buchanan, Deputy Director (Research), Australian Centre for Industrial Relations Research and Training, University of Sydney and Cameron Allan entitled ‘The Growth of Contractors in the Construction Industry: Implications for Tax Revenue’ (Cole 2003, vol. 9, p. 67). This study cited research that, “on average, contractors in construction paid $6,217 a year less tax than their PAYE equivalent” (Cole 2003, vol. 9, p. 67). The study looked at those workers who were sole traders, own account workers without incorporated status and without employees (Cole 2003, vol. 9, p. 67). In evidence to the RC, Buchanan pointed out the significance of lost revenue, noting “that if their conclusions were only 25 per cent right, the amount of revenue lost was still about $500 million” (Cole 2003, vol. 9, p. 67). The main building unions told the RC “that there is an ‘epidemic’ of tax fraud within the industry” (Cole 2003, vol. 9, p. 53). A senior union official, Ferguson, alleged that “there’s $1 billion worth of tax evasion taking place in the building industry; and about 30 per cent of the companies don’t pay workers’ compensation and I would say a very substantial
percentage, 30 per cent perhaps, don’t pay payroll tax” (Cole 2003, vol. 9, p. 53). Commissioner Cole stated that when interrogated by the RC hearings, union officials and others making these claims, provided little actual evidence, in terms of documents or other facts. However, the willingness of many companies to “succumb” to union pressure in response to threats to tell the ATO about their tax evasion; is sufficient implicit evidence.

In its submission to the RC, the ATO explained that it had completed investigations into “209 cases involving bogus labour hire schemes, or ‘bodgies’, including a number of cases which have resulted in successful prosecutions, resulting in $26 million in tax and penalties being raised in New South Wales” (Cole 2003, vol. 9, p. 57). Scheme promoters retained a commission and returned the balance in cash of fake invoices paid by cheque by employers (Cole 2003. vol. 9, p. 57). “A further $94 million in revenue was raised as a result of the indirect compliance effect of ATO audit activities” (Cole 2003, vol. 9, p. 57). Four identified scheme promoters have been jailed (Cole 2003, vol. 9, p. 57), which highlights the illegal nature of this activity.

The RC identified non-compliance with payroll tax as one of the construction industry’s unlawful behaviours. Commissioner Cole stated “there is substantial evidence of evasion of payroll tax obligations in the building and construction industry, particularly by persons engaged in phoenix company activity” (Cole 2003, vol. 1, p. 106).

The significance of the problem of inappropriate payroll tax activity within the construction industry at the time of the RC was limited by the proportion of companies involved in payroll tax evasion. This occurred because most construction companies are small employers (see chapter 3) and are below the payroll tax threshold. As Commissioner Cole pointed out “the high threshold means that the number of registered
employers is considerably less than the number of employers who hold a workers compensation policy” (Cole 2003, vol. 8, p. 95). For example, the RC reported that “in New South Wales as at 30 June 2001, there were a total of 25 873 registered employers liable for payroll tax and approximately 357 000 holders of workers compensation policies” (Cole 2003, vol. 8, p. 95). However, while the proportion of companies involved in payroll tax evasion was relatively smaller than those engaged in other unlawful behaviour, for example income tax evasion, Commissioner Cole stated that “evasion of obligations is still prevalent” (Cole 2003, vol. 8, p. 93).

The RC provided specific evidence of the prevalence of payroll tax evasion. In New South Wales, for example, audit work in the construction industry indicated a high risk of non-compliance regarding payroll tax. The RC found that “this has been an ongoing focus for the New South Wales Office of State Revenue (NSW OSR), which is charged with the administration of payroll tax” (Cole 2003, vol. 8, p. 97). “In 2000–01, a total of 1947 full payroll tax audits were completed [by the NSW OSR], including 180 audits associated with the construction industry (9.2 per cent)” (Cole 2003, vol. 8, p. 97). “Underpaid payroll tax liabilities were identified in approximately 80 per cent of construction audited cases” (Cole 2003, vol. 8, p. 97). However, this does not mean that 80% of construction companies are non-compliant with payroll tax. “The majority of audit cases were either specifically targeted or selected according to likely revenue risk” (Cole 2003, vol. 8, p. 97).

In 2002 the WorkCover Authority of New South Wales (WorkCover NSW) and the NSW OSR commissioned a report entitled “Review of employer compliance with workers compensation premiums and payroll tax in New South Wales” (Le Couteur & Warren 2002). The final report of the Review was delivered in September 2002 and stated in its Executive Summary:
Australia has a long history of reviews and recommendations for improvement in employers’ compliance with workers compensation premiums and pay-roll tax. It is a common belief that significant premium and tax revenues are being lost, although it is impossible to quantify the extent of the problem (cited in Cole 2003, vol. 8, p. 97, is a citation by Cole of the NSW Workcover Review).

However, there is some data available. A NSW OSR Building and Construction Audit Task Force raised “additional assessments totalling $16.5 million during the period November 1999 till December 2000” (Cole 2003, vol. 8, p. 101). An audit project, targeting known phoenix operators, “issued assessments totalling $4.8 million” at the time of the RC; and a second project, “based on data matching with other agencies, had issued assessments totalling $7 million” (Cole 2003, vol. 8, p. 101). These figures illustrate that despite the relatively small proportion of construction companies required to pay payroll tax, a significant amount of money are recoveries from construction companies avoiding payroll tax, which provides evidence of the scale of payroll tax evasion in the industry.

The 2002 WorkCover Authority of New South Wales (WorkCover NSW) of employer compliance with workers compensation premiums and the NSW OSR Review of payroll tax found challenges in addressing non-compliance. The challenges for the OSR in respect of pay-roll tax were:

1. complex legislation in relation to ‘relevant contracts’;
2. the ability of employers to avoid reaching the threshold by splitting activities (despite grouping rules); and
3. non-registration (which may be undetected as a result of the self-assessment system used to administer the tax) (cited in Cole 2003, vol. 8, p. 98, is a citation by Cole of the NSW Workcover Review).

In Victoria, Mr Grant Dunlop, Project Leader, Pay-roll Tax Investigations, State Revenue Office Victoria (SRO), informed the RC that:
The principal pay-roll tax compliance issues dealt with by the SRO are failure to lodge returns, late lodgement of returns, failure to be registered as an employer, incorrect application of the grouping provisions and failure correctly to declare taxable wages (in particular by incorrect application of exemptions and failure correctly to declare taxable components) (Cole 2003, vol. 8, p. 101).

Using employees as sub-contractors to avoid paying tax and other financial commitments, such as employee entitlements was a widespread practice in the construction industry. The widespread nature of this practice was shown by data provided by WorkCover where the NSW OSR was “able to identify many employers who had not registered for pay-roll tax but had been paying a workers compensation premium” (Cole 2003, vol. 8, p. 98). Consequently the Review found that “employers are more likely to take out workers compensation insurance because any worker who is injured will then be covered by the benefits of the insurance” (Cole 2003, vol. 8, p. 98).

The main building unions generally expressed to the RC the view “that there was an ‘epidemic’ of tax fraud within the industry” (Cole 2003, vol. 9, p. 53). The unions were very vocal about the use of employees as sub-contractors to avoid paying tax. This practice, which the unions called ‘sham contracting’, was widespread. In his testimony to the RC, Mr Wallace Trohear, State Secretary of the Construction, Forestry, Mining & Energy, Industrial Union of Employees, Queensland and Branch Secretary of the Construction and General Division of the CFMEU “estimated that up to 65% of the building and construction industry is on sham subcontracting arrangements and is only paying tax on the amount received as award or Enterprise Bargaining Agreement (EBA) rates” (Cole 2003, vol. 9, p. 53). In New South Wales, Mr Andrew Ferguson, the Branch Secretary of the CFMEU, Construction and General Division, New South Wales Divisional Branch (CFMEU New South Wales Divisional Branch) alleged that “there had been the misuse of tens of thousands of Australian Business Numbers (ABNs), which had been issued to individuals who were really employees, and the incorrect
receipt of and misuse of goods and services tax refunds” (Cole 2003, vol. 9, p. 53). While it is difficult to agree on quantified data on payroll tax noncompliance, it is clear that the unions felt the problem was significant, widespread, and a serious breach of the construction industry’s societal contract.

The 2002 WorkCover Authority of New South Wales (WorkCover NSW) and the NSW OSR Review of payroll tax stated:

Changes to the labour market brought about by growing use of contractors have fundamentally changed the nature of the employer/employee relationship. They have impacted on union membership, workplace relations, personal income tax, pay-roll tax, workers compensation premiums and OH&S (Cole 2003, vol. 8, p. 99, is a citation by Cole of the NSW Workcover Review).

Unscrupulous individuals exploited these industry structures to disguise the employer/employee relationship to avoid paying payroll tax. The Review recommended that “the principal contractor be liable for amounts of payroll tax and workers compensation premiums evaded by contractors unless the principal has a written statement from the contractor advising that appropriate payroll tax and workers compensation premiums have been paid” (Cole 2003, vol. 8, p. 99). This recommendation aimed to address the problem by placing responsibility with the contractor. In this way, the contractor was responsible for payroll tax of those employed on their projects, whether they were employed as staff or as sub-contractors. However, this measure still did not address the problem of avoiding the payroll tax threshold by using employees as sub-contractors. If the contractor could split up his/her staff into smaller companies each of which did not reach the threshold figure, a practice known as grouping, then he/she would avoid payroll tax and also avoid any responsibility for these subcontractors paying payroll tax. The RC concluded that “in effect, there is currently no
real disincentive for a principal to engage a contractor who is non-compliant with the pay-roll tax legislation” (Cole 2003, vol. 8, p. 99).

The unions’ main concern in terms of payroll tax evasion was what some witnesses at the RC called “illegitimate use of contracting” (Cole 2003, vol. 8, p. 103). Mr John Sutton, National Secretary of the CFMEU, Construction and General Division, gave the following evidence:

MR GINNANE: Can I ask you about payroll tax. Do you agree that payroll tax is not a major feature of most building enterprises because of the payroll threshold that exists in various states? We were told this morning in Victoria it’s about $500,000 payroll before you have got to pay any payroll tax. There [are] thresholds around the states. Most building businesses, we are told, employ five or less people. Do you agree that payroll tax is not really much of a compliance issue in the building industry?

MR SUTTON: It’s still an important issue because… There’s many legitimate contracting firms that do employ significant numbers of men in this industry. When we say 95 per cent of firms employ less than five, there’s a certain fiction in that, because that includes all these workers. On my figures, that includes about 150,000 workers who are called businesses, when they are in fact employees. You put them under the microscope, they are really employees. So it’s not really 95 per cent, if you discounted for all that. But in any event, I do accept that there is a large number of small contractors.

MR GINNANE: The overwhelming majority of businesses in the building industry are small businesses?

MR SUTTON: Yes, indeed. But there is a substantial number of medium sized contractors on all the commercial building sites around the country that do employ anywhere from 10 workers to 200 workers and many of those, of course, don’t pay their payroll tax or again understate it. So compliance with payroll tax laws is another – or non-compliance, I should say – is another very serious problem in the building industry (Cole 2003, vol. 8, pp. 103-104).

This extract presents two opposing views. Mr Ginnane is trying to establish that payroll tax evasion is not a significant problem due to the complex nature of contracting in the construction industry. Most companies are so small that they do not meet the threshold figures, in terms of total wages bill, and therefore do not have to pay payroll tax. Mr John Sutton, on the other hand, is arguing that payroll tax noncompliance is a significant
issue. He is blaming the problem on mid-sized companies, with 10 to 200 employees, who would certainly reach the threshold and have to pay payroll tax. In this testimony, Mr Sutton is suggesting that these mid-sized companies are creating the problem of noncompliance because they are trying to avoid paying payroll tax by declaring their employees as sub-contractors. It seems that Mr Sutton is basing his argument on an assertion that the employee figures of 10-200 are the “real figures” but that these companies try to report much lower figures in the hope of avoiding their payroll tax obligations. They do this by “pretending” staff are subcontractors. The RC accepted evidence submitted by the CFMEU that it had notified the New South Wales OSR of its concerns regarding payroll tax, “but it was not apparent what response had been received” (Cole 2003, vol. 8, p. 104). This provides support for the point that the unions were not creating payroll tax noncompliance as an issue for its own political means, thereby confirming that the unions felt they had legitimate concerns about the matter and had raised it with relevant authorities prior to the RC.

This raises questions about where this practice of “hiding” employee numbers to avoid payroll tax fits within the payroll tax process and whether accountants would be involved. This activity would probably not involve accountants. Decisions about employment status would be made by management, perhaps with the advice of human resource management.

A strategy which construction companies used to avoid reaching the payroll tax thresholds was to split activities to avoid having employees included in a “group” of companies that would aggregate the wages bill. The 2002 WorkCover Authority of New South Wales (WorkCover NSW) and the NSW OSR Review of payroll tax found that data matching with Workcover was encouraging but limited due to a number of conceptual differences. The Review found:
differences in the definition of wages, the concept of ‘employee’ for pay-roll tax and ‘worker’ for workers compensation and the differing rules regarding grouping, currently relevant for pay-roll tax purposes only, versus the concept of ‘related activities’ for workers compensation purposes (Cole 2003, vol. 8, p. 98, is a citation by Cole of the NSW Workcover Review).

Opportunities for payroll tax recovery, particularly in the case of phoenix company activity, were improved with legislative amendments in New South Wales. “Section 31C of the Pay-Roll Tax Act 1971 (NSW) enabled the service of a notice of liability to payroll tax on a director, or former director, once an assessment of their company becomes overdue” (Cole 2003, vol. 8, p. 101). In its submission to the RC, the NSW OSR stated:

Whilst section 31C was partially successful, phoenix company operators tended to ensure that none of their companies that paid wages held any worthwhile assets, which protected those assets from any legal action by OSR. To overcome this problem section 16LA was introduced. This section makes all members of a group jointly and severally liable for the debts of other group members, regardless of whether or not the group member pays wages. This provision had a commencement date of 1 January 2001. The current OSR compliance project regarding the building and construction industry has used s16LA to settle the debts of twenty-four (24) companies (controlled by known phoenix operators) which had a total liability of $2.8 million were prior to the introduction of this legislation, responsible for debts totalling $2.4 million considered to be irrecoverable (Cole 2003, vol. 8, p. 101).

A further strategy used by construction companies to avoid tax was not registering as being eligible for payroll tax. The NSW OSR, using data provided by WorkCover, was able to identify many employers who had not registered for pay-roll tax but had been paying a workers compensation premium (Cole 2003, vol. 8, p. 98). The 2002 WorkCover Authority of New South Wales (WorkCover NSW) and the NSW OSR Review of payroll tax found that “employers were more likely to take out workers compensation insurance because any worker who is injured will then be covered by the benefits of the insurance” (Cole 2003, vol. 8, p. 98). Therefore, the number of employers paying workers compensation premiums was a more accurate measure of employers
with employees, rather than sub-contractors, because employers could see consequences in not paying workers compensation insurance, like being sued for workers compensation, as opposed to avoiding payroll tax where they felt they could avoid detection.

The State Revenue Office Victoria (SROV) identified the construction industry as “the single largest industry group in which non-compliance to register for payroll tax occurred, representing 18% of failures to register” (Cole 2003, vol. 8, p. 102). The SRO reported to the RC that the “main cause of that non-compliance was found to be ignorance of the legislation” (Cole 2003, vol. 8, p. 102). This suggests that these non-compliant companies were failing in process 1a. recognise the payroll tax liability, which is a process involving accountants. Accountants should have been aware of payroll tax legislation. Revenue South Australia (RSA) told the RC that:

During the period 1 July 1995 to 30 November 1997, 39 audits and investigations (7.3%) had been conducted on the construction industry from a total of 534 assignments across 15 industry sectors. Pay-roll tax revenue of $685,778 (9.8%) was identified within the construction industry by these programs from the total revenue of $7M. The largest pay-roll tax revenue ($523,934 or 74.6%) in the construction industry has been as a result of non-registration. 25.4% of the noncompliance revenue has resulted from errors and omissions from returning incorrect taxable wages (Cole 2003, vol. 8, p. 102).

More recent data (2001/02) showed that RSA had identified 24 employers not registered; which led to recovery of “$2,163,310 in pay-roll tax including penalty tax, additional tax and interest” (Cole 2003, vol. 8, p. 103). The Queensland OSR’s investigation program reported to the RC that “in 2000–01, $8.1 million was collected following 521 investigations” (Cole 2003, vol. 8, p. 102). However, the revenue obtained from the construction industry could not be separated from this total. “Queensland identified labour hire as a high risk area” (Cole 2003, vol. 8, p. 102). Given labourers represent part of the construction industry’s workforce, this could represent a problem. However,
the data from Queensland was broader than for the other Australian states and not helpful in identifying the precise nature of payroll tax evasion in the Queensland construction industry. Similarly, “Tasmania does not collect data to allow it to compare non-compliance in payroll tax in the construction industry with other industries” (Cole 2003, vol. 8, p. 103). Australia’s two territory governments found limited payroll tax noncompliance. The Department of Treasury Australian Capital Territory informed the RC that:

The significant cause of non-compliance with payroll tax obligations is due to a failure to declare a liability or the full extent of the payroll tax liability. In addition, payroll tax legislation requires the employer to determine which contractors and payments are included in the salary base for payroll tax purposes. Determining the payroll tax liability of employers in the building and construction industry is often difficult because of the widespread use of contractors and cash payments in the industry (Cole 2003, vol. 8, p. 103).

This statement defends employers by suggesting that the construction industry is complex due to its contracting structure and it is difficult for companies to monitor their obligations because the threshold may rely upon information from others. The Department provided this further information to the RC:

The ACT’s data indicate that the level of compliance in the building and construction industry improved in the period 1998-99 to 2000-01:

From July 1998 to June 2001, 17 inspections on companies in the building and construction industry were undertaken. This represents 6% of the overall number of inspections undertaken and is in line with industry representation… In 1998-99, a significant amount of unpaid payroll tax was detected in the building and construction industry. This was mainly due to three companies who were identified because of a failure to lodge a return or register for payroll tax. Over 80% of the unpaid revenue detected had been incorrectly paid to another jurisdiction. Similar investigations undertaken in subsequent years did not uncover the same level of unpaid payroll tax (Cole 2003, vol. 8, p. 103).

This indicates that payroll tax is not a significant problem in the Australian Capital Territory. The fact that non-compliant companies appeared to pay monies elsewhere
suggests that non-compliance was an honest mistake rather than deliberate action to avoid paying tax. The Department’s testimony is forgiving of construction companies in terms of payroll tax evasion. However, it does highlight failure to declare payroll tax liability as a problem. This suggests that these non-compliant companies were failing to recognise the payroll tax liability, which is a process involving accountants.

The Northern Territory, payroll tax noncompliance was much more prevalent, as shown by this extract from the RC:

…in 2001-02, 32 investigations were conducted on businesses in the construction industry of which 18 (or 56%) resulted in the issue of a pay-roll tax assessment. In comparison, 208 pay-roll tax investigations were conducted on businesses in other industries of which 102 (or 49%) resulted in the issue of a pay-roll tax assessment in the same period. Of note is that this reflects only 25% of the taxable employers in the construction industry and 17% of taxable employers in all other industries (Cole 2003, vol. 8, p. 103).

This indicates that while payroll tax noncompliance within the construction industry was high, it was high in other industries within the Northern Territory as well; perhaps suggesting a culture on unlawful behaviour common across the territory’s industry. Despite this widespread culture, construction industry was still worse than other industries in the Northern Territory, suggest payroll tax non-compliance was a significant problem.

Construction companies were also guilty of failing to lodge returns, late lodgement of returns, and incorrect lodgement of returns. The submission by Mr Dunlop of the SROV provides insight into the type of activities associated with payroll tax evasion. The SROV engaged in audit activities of companies investigated for payroll tax evasion. The audit activities undertaken by the SROV indicate how companies may have been avoiding payroll tax. This is helpful in determining whether accountants were involved in these activities. The audit activities conducted by the SROV included:
• evaluations based on employer profiles
• measures directed at coverage of the tax base and identified risk areas
• Audit activities are undertaken via a mixture of desk and field audits of particular taxpayers (Cole 2003, vol. 8, p. 102).

Incorrect lodgement of returns involves failure to correctly declare taxable wages; in particular by incorrect application of exemptions and failure to correctly declare taxable components. “The main areas of non-compliance were non-inclusions of superannuation, understatement of remuneration and non-inclusion of directors’ superannuation and directors’ fees” (Cole 2003, vol. 12, p. 257).

The RC found “significant incidence of fraudulent phoenix company activity in the construction industry” (Cole 2003, vol. 1, p. 108). It is important to highlight the word ‘fraudulent’ used here by Commissioner Cole. Phoenix companies were created by the construction industry to avoid paying tax and this activity was considered illegal. A 2009 Australian Government Treasury report estimated cost of phoenix activity to the ATO to be $600 million per year (Treasury 2009). This is the direct cost to the regulator. Indirect costs to other creditors were also considered significant. The RC found that a major reason for establishing phoenix companies was to evade payroll tax obligations (Cole 2003, vol. 1, p. 106). Commissioner Cole described this as fraudulent conduct. He also found that businesses and individuals who engage in phoenix company activity are often trying to evade other revenue obligations, including the proper payment of employee entitlements (Cole 2003, vol. 1, p. 106). This suggests that phoenix companies were often established for fraudulent purposes and were associated with other unlawful activity. A major reason for this activity was the lack of accountability and information sharing between regulators. Some people knew that the activity was poorly policed and so they took the risk of getting away with it. Commissioner Cole stated “since 1998 the Australian Taxation Office has raised at least $110 million in taxes and penalties from
the detection of fraudulent phoenix company activity in the construction industry” (Cole 2003, vol. 1, p. 108). That means that more than $20 million in taxes per year were being avoided by companies engaging in phoenix activity. Commissioner Cole added “for every $1 spent by the Australian Taxation Office on the detection of phoenix company activity in the period 1 July 2001 to 30 June 2002 $8 in revenue was raised” (Cole 2003, vol. 1, p. 108).

While Cowan described phoenix company activity as “mischief” (Cowan 2012, p. 19), it is clear that Australian society viewed it much more seriously, and saw it as unlawful and a significant breach of the societal contract. In 2009, a report from the Federal Government Treasury Department showed that losses caused by phoenix activity had been mounting in Australia (Treasury 2009). The regulator’s attention on phoenix activity heightened when it realised that losses to taxation authorities were estimated to run into the hundreds of millions of dollars (Commonwealth, Parliamentary Debates, cited in Anderson 2012, p. 412). A press release in 2011, accompanying draft legislation to penalise the non-remittance of superannuation contributions, estimated that there were 6000 phoenix companies in Australia (Shorten 2011). This highlighted the widespread nature of the activity.

The significance of the breach of societal contract by phoenix company activity is not limited to avoiding taxation. What makes phoenix activity so objectionable to the public is its widespread impact on so many parts of society. Those who suffered from phoenix activity included “unsecured trade creditors, employees and revenue authorities” (Anderson 2012, p. 412). The impact on employees included losing their “accrued annual and long service leave entitlements, in addition to wages, redundancy and pay in lieu of notice” (Anderson 2012, p. 412). There is also impact on state and federal taxation authorities because they “lose payroll tax revenue, and pay-as-you-go (PAYG)
instalments and superannuation amounts, deducted from employees’ wages, are not remitted” (Anderson 2012, p. 412). In each case, there are negative flow-on effects. For example, trade creditors may experience their own financial difficulties as a result (Anderson 2012). This is particularly true in the construction industry where so many small companies struggle to survive. Overall, the greatest burden is borne by the Federal Government who suffers “loss from tax avoidance, and indirectly the taxpayer, who represents all of the rest of society, and who is further burdened where properly levied taxation liabilities are unable to be recovered” (Anderson 2012, p. 412).

The significance of the problem of phoenix company activity was further highlighted in a recent article in The Australian newspaper which cited a study that found that “dishonest and debt-laden directors who set up phoenix companies to avoid tax, superannuation and other creditors are costing the country up to $3 billion a year” (Owen 2012, p1). A regulator, the FWO, released a report it commissioned by consultants PricewaterhouseCoopers, to reveal the scope of phoenixing. The report estimated the cost of phoenixing at between $1.78bn and $3.19bn (Owen 2012). Analysis of the cost breakdown showed company directors engaging in phoenix activity were avoiding paying up to $655m in unpaid wages and other worker entitlements (Owen 2012). They also avoided up to $1.93bn in unpaid debts, and goods and services paid for but not provided (Owen 2012). The federal government was estimated to lose up to $610m in revenue, mainly in unpaid taxes, but also from the avoidance of payments to employees under the GEERS (Owen 2012).

The RC found evidence that “persons associated with fraudulent phoenix company activity in the building and construction industry [were] being appointed as directors of other construction companies” (Cole 2003, vol. 1, p. 109). As these people were declared bankrupt they were disqualified to act as directors. Commissioner Cole was
critical of regulatory authorities for allowing these individuals to avoid detection. Commissioner Cole’s recommendation to change the law to allow the disqualification of directors after being associated with one failed company was not adopted, but “the period of potential disqualification for directors was doubled in 2004” (Anderson 2012, p. 414).

The RC found evidence that tax evasion occurred by directors setting up a group of companies within the same industry offering the same services, that is construction. While not unlawful, it provided opportunity for individuals to avoid liabilities, such as paying tax, by transferring assets to one company and liquidating one of the companies. By declaring insolvency in one of the group’s companies, the directors could avoid paying its debts, such as tax, but carried on doing the same business as directors in one of the other group’s companies.

The RC found that some “offenders deliberately structure their operations to engage in phoenix activity and to avoid detection” (Cole 2003, vol. 3, p. 208). Commissioner Cole was clear that this behaviour was intentional. These individuals “fail to pay their debts, act in a manner that intentionally denies unsecured creditors equal access to the entity’s assets to later re-emerge as a similar business controlled by parties related to either the management or directors” (Cole 2003, vol. 3, p. 208). While a primary aim of phoenix company activity was to avoid paying tax, Commissioner Cole reveals that the activity had a spill-over effect on other businesses. Failing to pay debts to other companies can cause recurrent losses to other businesses. The RC found that company directors intentionally “designed and planned their businesses to profit at the expense of their creditors” (Cole 2003, vol. 3, p. 208, p. 18). Phoenix company activity also involved deliberate intent to avoid paying other companies, for example subcontractors, wages and other entitlements legally deserving.
Commissioner Cole recommended that the way to stop this practice was that directors “should be jointly and severally liable for the taxation debts of the other group members” (Cole 2003, vol. 19, p. 92). This would deter declaring insolvency and also make directors accountable for taxation debt.

Commissioner Cole’s recommendation to include “corporate group liability in relation to certain tax debts of other group members” was not adopted (Anderson 2012, p. 414). Therefore, there is no specific evidence that accountants involved with the construction industry changed their practices associated with phoenix company activity as a result of the RC finding a societal contract breach in this area. It may be inferred, however, that if there were any changes to accounting practice, it had little impact on phoenix company activity. The evidence is that phoenix company activity continued after the RC and that it remained a significant societal contract breach almost 10 years afterwards. Therefore, it may be concluded, that if it is accepted that accountants must have played some role in phoenix activity (see above), that they did not succeed in bringing a sense of order to some individuals in the construction industry. Indeed, this analysis provides support that accounting has a subjective role and that some accountants would have bent the rules, that is, the accounting standards, in their work with company directors involved in phoenix activity.

A further clue on how difficult it may have been for accountants to change phoenix company activity is provided by how difficult the regulators found it to police unlawful behaviour. Anderson (2012) explains how frustrated the Federal Government was with continued phoenix activity six years after the RC:

The Joint Committee of Public Accounts and Audit in 2008 noted an increase in the numbers of individuals promoting the benefits of fraudulent phoenix activity, and at its hearings, ATO Deputy Commissioner Mark Konza expressed his frustration that the fight against phoenix activity was being thwarted by light
penalties and a lack of prosecutions. The 2009 Phoenix Proposals Paper acknowledged that ‘[i]t is clear that ... existing mechanisms do not provide a sufficient disincentive to prevent fraudulent phoenix activity.’ This is undoubtedly true (Anderson 2012, pp. 422-423).

Commissioner Cole states that phoenix company activity was associated with tax evasion and Anderson (2012) calls it fraudulent. Therefore, phoenix company activity for the purposes of tax evasion represents non-compliance with accounting standards. If the ATO felt powerless to enforce the law regarding phoenix activity, how could accountants employed by the construction industry have felt any differently? This evidence suggests that accounting practice regarding phoenix activity had not changed based on two assumptions. First, phoenix activity was actually increasing in the period after the RC. Second, accountants were unlikely to have the authority or disincentives to prevent fraudulent phoenix activity. Therefore, it may be concluded that there were no observable changes to accounting practice regarding phoenix activity in the period after the RC. Accounting may be considered a subjective practice in regards to phoenix company activity. It was unable to stand above this activity and to enforce accounting standards to prevent fraudulent phoenix activity. Accountants employed by the construction industry were most likely applying subjective judgements in their work associated with phoenix activity depending upon the amount of pressure exerted on them by others, for example company directors.

6.3.3 Pay Employees Their Entitlements

6.3.3.1 Societal Expectation

The second expectation of society regarding the construction industry was that it would pay employees their entitlements. Employee entitlements includes: wages, superannuation, workers compensation, annual leave and long service leave, and
redundancy payments (s596AA(2) Part 5.8A of the Corporations Act 2001 (C’wth)). However, researchers tend to exclude wages, and classify employee entitlements as non-salary items that employers provide for employees (Symes 2003). These items are expenses which should be recorded in the entity’s IS. As an expense, they have an impact on the entity’s profitability. Manipulation of employee entitlements, that is underpayment, would decrease expenses and increase profitability.

Australian insolvency law has protected employee wages since at least 1825, that is colonial times (Symes 2003, p. 134). From the 1930s, “the various States Companies Acts gave employees' wages a statutory priority upon insolvency” (Symes 2003, p. 134). Originally, this involved “only wages but was extended to other entitlements”, as part of employment awards (Symes 2003, p. 134). In 1984, the Termination, Change and Redundancy case changed industrial laws and “employees enjoyed rights to accumulate entitlements, not just wages” (Symes 2003, p. 134). These changes had an important impact on employee entitlements and industrial relations. The 1984 case provided legal precedent for employees and their unions to demand non-wages benefits, such as sick leave and superannuation. It also provided a change in the socio-political relationships in industries such as construction, where unions felt they had legal support for arguing for employee entitlements.

From a theoretical perspective, employee entitlements is grounded in organisational science; more specifically the disciplines of human resource management and industrial relations. From an organisational science perspective, employee entitlements is based on social reciprocity theory (Blau 1964), and psychological contract (for example, see Massingham & Diment 2009). Strong psychological contract means the employee is happy with their employer and this will generate positive work attitudes and behaviours such as increased motivation and productivity (Massingham & Diment 2009). Employee
entitlement is fundamental to understanding employees' expectations and, in particular, the nature of exchange between each individual and the employing organisation (Naumann, Minsky & Sturman 2002). From an industrial relations perspective, research has generally focused on the philosophical debate regarding the specification of what is entitled (for example, Nozick 1974). Related disciplines have different assumptions about entitlement. Law, for example, treats entitlement as a measure of one's right, which cannot be taken away without due process (Black 1990). Industrial relations grounds employee entitlements within debate over the merits of socialism versus capitalism. This debate contrasts human resource management’s focus on distributive justice with industrial relation’s focus on procedural justice. Distributive justice aims to distribute pay equitably within the organisation (Phillips & O’Connell 2003). If employees feel that the organisation has a fair distribution of pay, the employees’ psychological contract will be higher than those who feel pay is unfairly distributed (Phillips & O’Connell 2003). Industrial relations focus is on procedural justice and employees need to understand the process through which pay is administered. Employees need to be able to address organisational procedures if problems occur with the administration and delivery of pay (Phillips & O’Connell 2003). This debate explains employees’ perception about pay inequality and the extent to which employees understand how performance affects salary (Phillips & O’Connell 2003). Procedural justice occurs when employees have the right to appeal unfair pay practices and is the focus of the unions’ attention in the construction industry.

The various disciplines involved in employee entitlements research agree that entitlement is related to what a person perceives he/she deserves from their employer in return for their services. Where the disciplines tend to disagree is why entitlement is deserved. Research influenced by socialism and trade unionism, for example industrial relations,
suggests that an employee's level of entitlement is predetermined. This research argues that employees are not required to reciprocate in return for a certain entitlement, for example food, legal rights, democracy, and that employers are obliged to provide these societal benefits for members of society (for example, see Naumann, Minsky & Sturman 2002). More recently, Fisk (2010) proposed a concept called “excessive entitlement”, which she defined as a trait reflecting unjustified beliefs of deservingness. Fisk (2010) proposed a model to predict counterproductive work behaviours by examining where this trait interacts with specific HRM practices related to staffing and performance. While this research suggests a personality defect at the individual level, meaning the person has unrealistic expectations of their entitlement from their employer, this may be projected onto groups of individuals (for example, union members) or organised groups (for example, unions) who may exhibit these types of attitudinal traits, that is, unrealistic expectations. This is particularly interesting for the construction industry where profit margins are so small and employers could reasonably argue that union expectations of entitlements are unrealistic. In contrast, research influenced by business strategy, for example human resource management, implies that the individual is only entitled to as much as his/her benefit to the overall good. If the individual can demonstrate how their work benefits society, they are then entitled to receive the full amount of that benefit (Naumann, Minsky & Sturman 2002). In other words, the individual must earn their level of entitlement.

The second difference amongst the employee entitlements research disciplines, concerns the level of reciprocity inherent in the employee-organisation exchange relationship (Naumann, Minsky & Sturman 2002). The difference is about whether employees should be rewarded for loyalty or their performance. This discussion is grounded in psychological contract theory, which argues that if the organisation rewards individuals
with high employee entitlements, the individual’s emotional relationship with their employer will be strengthened resulting in positive work attitudes and behaviours (for example, see Massingham & Massingham 2014). Researchers have identified two types of employee-organisation relationships: job focused and organisation focused (Tsui, Pearce, Porter & Hite 1995). This framework offers a spectrum of psychological contract and a way to measure levels of reciprocity. At the lowest level, job focused relationships are more transactional in that the employer is primarily interested in obtaining high levels of task performance from employees, without expecting organisational commitment in return (Tsui et al. 1995). At the highest level, employees working in organisation focused relationships have broadly defined jobs, a high degree of organisational involvement, and a willingness to perform tasks outside of their job descriptions (Tsui et al. 1995). In return for this loyalty, employers are expected to offer a wide range of benefits including: investing in the employees' careers, providing job security, and offering extended benefits (Tsui et al. 1995).

The solution to the differences in levels of employee entitlements and reciprocity is to align employee expectations with employee entitlements. Some employees will have low reciprocity which means they will have low expectations of their employer in terms of employee entitlements. These individuals will have a job focused relationship with their organisation. They are likely to accept lower levels of entitlements than individuals with high reciprocity. These latter employees will have high expectations of their employer in terms of employee entitlements. These individuals will have an organisational focus relationship with their employer; are not likely to accept low levels of entitlements and would expect to be rewarded for their loyalty. Naumann, Minsky and Sturman (2002) suggest that employee alignment with employee entitlements expectations is contextual in the sense that some industries tend to have strong political ideologies supporting
workers’ rights. These industries are characterised by strong trade unionism which encourage employees to see employee entitlements as a right rather than something to be earned. The construction industry had these characteristics. The aim of employers should be to align employee entitlements with employee expectations which in the case of the construction industry the employers did not do. The levels of reciprocity help us understand why this happened. Construction industry employees would have a job focus rather than an organisation focus. There was high employee turnover and employees moved from project to project. According to this previous research, these employees should have low reciprocity and expect lower employee entitlements, however, the unions wanted high employee entitlements which created tension within the stakeholder system, and misalignment in employee entitlements expectations.

6.3.3.2 Societal Contract Breach

The RC found unlawful behaviour in the way the construction industry paid employee entitlements. In an industry with intense competition and small profit margins (see chapter 3), owners or investors and management would have been under pressure to reduce expenses and improve profitability. Given entitlements are an expense in the IS, it is easy to see how underpayment of employee entitlements would have occurred in these operating conditions.

The consequences of non-compliance and underpayment of employee entitlements is that society suffers, through the financial impact for employees who do not receive their full entitlements. The significance of this problem is highlighted when the financial amount of employee entitlements is considered. Employers’ liabilities for employees’ accrued annual and long service leave entitlements alone probably exceed $50 billion (Davis & Burrows 2003). To illustrate how much this figure actually means, it is an
amount approximately equal to total lending by all finance companies (Davis & Burrows 2003). Considering employees are, in essence, providing these funds to their employers until they seek them, that is take the leave or exit the company, the situation takes a different context. Employee entitlements represent a very significant amount of funds in Australia, equal to all of the funds made available as debt by the country’s financial sector, and these are in essence loaned by employees to their employers. It is a remarkable measure of the reciprocity involved in employee entitlements. Employees allow their employers to use funds, which employees essentially own, for other purposes. It seems only fair that employers provide these entitlements when employees want them.

Underpayment of employee entitlements was allowed to evolve as a widespread practice in the construction industry because of a loophole created by industry structure. As shown in chapter 3, the construction industry was characterised by its fragmented structure and by the very high proportion of small firms known as subcontractors. This changed the employee relationship in ways that encouraged and even allowed underpayment of employee entitlements.

The first change in the employee relationship was employees who pretend to be contractors. During the RC hearings, Mr Dean Mighell and Mr Bill Shorten highlighted the problem of workers, who had all the fundamental characteristics of an employee, but who operated as contractors. These were workers who essentially supply labour only services. Mighell stated that this was done to “avoid taxation and payment of correct employee entitlements” (Cole 2003, vol. 12, p. 141). The Construction and General Division of the CFMEU Queensland gave evidence to the RC that employers avoided payment of Workcover premiums by classifying workers as subcontractors. The Queensland State Government also acknowledged that the “attraction of not having to
pay workers’ compensation premiums was one significant inducement for employers to engage their workers through subcontracting arrangements” (Cole 2003, vol. 12, p. 208).

A second change in the employee relationship was through the use of cash payments. While the primary objective here was to avoid paying income tax it was also used as an incentive to persuade employees to work as subcontractors and avoid paying them entitlements.

A third change in the employee relationship was through the use of pyramid subcontracting. This was the practice of sub-contractors employing other sub-contractors. The RC found that pyramid contracting was “an artificial labour only contractor arrangement which was designed to avoid legal responsibility for employee entitlements and tax payments” (Cole 2003, vol. 4, pp. 104-105).

Insolvency can occur lawfully and unlawfully. The analysis of phoenix company activity above provides further details. Some company directors used insolvency as a way to avoid paying employee entitlements.

6.3.4 Pay Suppliers Their Entitlements

6.3.4.1 Societal Expectation

The third expectation of society regarding the construction industry was that it would pay suppliers their entitlements. This involved two activities: inappropriate payments and security of payments. The payable and receivable of payments involves the accounts payable and receivable functions. These are considered the most labour intensive of all accounting functions (Bragg 2007, p. 18). The basic accounts payable process in most companies is to receive three types of information from three sources: an invoice from
the supplier, a purchase order from the purchasing department, and a proof of receipt from the receiving department. This information ensures that the payment is appropriate.

The RC identified inadequate security of payment for subcontractors as one of the construction industry’s unlawful behaviours. Indeed, Commissioner Cole stated that “security of payment in the construction industry throughout Australia remains one of the most significant and controversial issues impacting the success or failure of any party working in the construction industry” (Cole 2003, vol. 8, p. 227). Commissioner Cole concluded that “in general, security of payment practices in this industry throughout Australia remain barbaric and definitely unfair” (Cole 2003, vol. 8, p. 229). This strong language suggests the problem of inadequate security of payment is cruel to its victims, which are small business owners who suffer enormously as a result. Commissioner Cole felt passionately about this problem and argued that it was one the most important unlawful behaviours in the construction industry. He described it as a topic of national concern (Cole 2003, vol. 8, p. 229).

6.3.4.2 Societal Contract Breach

There appears to be two types of payment issues associated with the unlawful behaviour within the construction industry identified by the RC. First, delaying or withholding payments in the normal course of completing a construction project (see Tran & Carmichael 2012). Second, delaying or withholding payments as the result of business failure, that is, liquidation (see Ramachandra & Rotimi 2012). However, there are also unlawful payments disguised by incorrectly recording the expense, but this is a recording issue rather than a payment issue. Commissioner Cole focused mainly on the third behaviour, incorrect recording of expenses, because it allowed the opportunity for illegal payments such as bribes.
In terms of the first and second unlawful behaviours, delaying or withholding payments, Tran and Carmichael (2012) identify four scenarios employed by the construction industry:

- **Scenario 1** (best scenario): the contractor always pays its subcontractor punctually and in full regardless of payment from the owner.

- **Scenario 2**: the contractor delays and/or withholds part of the owner payment, responding to every subcontractor claim with exactly the same treatment, in terms of delay and partial payment, that it gets from the owner (a "pay when paid" situation applies). For example, if the owner pays a claim one week late then the contractor would also pay its subcontractor one week late. When the owner pays the contractor, the contractor also pays its subcontractor. In this case, payment from the contractor to subcontractor reflects exactly the owner payment characteristics in both timing and quantum. If the owner pays the contractor, then the subcontractor also gets paid.

- **Scenario 3** (worst scenario): The contractor tries to delay and withhold payments to the subcontractor even if the owner has made its payment on time and in full, in order to improve its own cash flow to the detriment of the subcontractor. Payment to the subcontractor is completely independent of the payment from the owner to the contractor. In this case, the two issues are independent since they reflect the owner's and the contractor's separate payment behaviour. The issue is created by the contractor payment behaviour.

- **Scenario 4**: A contractor's response to each subcontractor claim may not be consistent. The contractor may not always act as in any of the scenarios above, but rather may exhibit behaviour which is a combination of the above scenarios. For some claims, the contractor pays its subcontractor when the owner pays; for other claims, the contractor does not pay even if the owner has paid.
In terms of the unlawful behaviour, incorrect recording of expenses, examples include cash bribes, purchasing goods and services at inflated prices, or where the payment is for a service that cannot be recorded, for example a financial incentive to win a contract or deter industrial action.

Small companies are sometimes not paid due to legitimate business failure, as opposed to the other inappropriate behaviours listed above. In this case, problems can arise because the company is in financial difficulty and does not have the cash flow to pay subcontractors; or the company has become insolvent and cannot pay the full amounts owing to their creditors, including subcontractors (Cole 2003, vol. 8, p. 231). In these circumstances, the small company suffers as it would if the contractor was behaving inappropriately. The difference is this behaviour is legitimate, the contractor cannot pay even though they would like to do the right thing, while the others are illegitimate, unscrupulous individuals deliberately intend not to pay. This raises the question whether security of payment may be improved to anticipate contractors likely to get into financial difficulty. This could signal the risks for subcontractors even though the company might be in satisfactory financial health at the time of signing the contract.

The RC found unlawful behaviour in the way the construction industry treated security of payments. Security of payments was raised at the RC during the public hearings, in meetings Commissioner Cole held with interested parties, in interviews conducted by Commission investigators, and in submissions to the RC (Cole 2003, vol. 1, p. 115). Commissioner Cole stated that it “became apparent that it is an issue that critically affects the ability of participants in the industry to make a living, and to be rewarded for work that they have performed” (Cole 2003, vol. 1: p. 115). Commission investigators were “repeatedly told of the suffering and hardship caused to subcontractors by builders who are unable or unwilling to pay for work from which they have benefited” (Cole
Commissioner Cole was very sympathetic towards those companies who suffered from inadequate security of payment arrangements in the construction industry. He stated “the subcontractors who experience payment problems are often small companies or partnerships”, and “frequently they do not have the expertise or resources to enforce their legal rights, because enforcement would require protracted litigation against much better resourced and more sophisticated companies” (Cole 2003, vol. 1, p. 115). The language used by Commissioner Cole portrays these small companies as powerless victims. He presents the problem of security of payments as a significant societal contract breach by the construction industry. Commissioner Cole concluded that “subcontractors that have operated profitably and well for many years can be forced into liquidation through no fault of their own, often with devastating consequences for the owners of these businesses, their families, their employees and their creditors” (Cole 2003, vol. 1 p. 115). The use of the phrase “devastating consequences”, creates sympathy for the victims of inadequate security of payments. Commissioner Cole clearly feels strongly about this problem. He is arguing that society has a responsibility to fix this problem due to the serious negative impact it has on members of society, that is, small business owners who are suffering through no fault of their own.

The unions also felt very strongly about the problem of security of payment. The RC reported that “on 27 July 2001 the CFMEU New South Wales Divisional Branch organised a march on the Sydney office of the PM to protest that ‘100 building workers became the latest victims of the Government’s paltry security of payment laws’” (Cole 2003, vol. 8, p. 180). The CFMEU claimed that “‘the men were abandoned by their employer – Emerson Formwork – without warning and [that they had] not been paid for two weeks and [were] owed some $500 000 in wages, redundancy, holiday pay and
super”” (Cole 2003, vol. 8, p. 180). The union is arguing here that if the regulator, the government, had better security of payment legislation and methods to police compliance then companies like Emerson would not have been awarded this contract and the workers would not have suffered from its business failure.

6.3.5 Accurate Performance Reporting

6.3.5.1 Societal Expectation

The fourth expectation of society regarding the construction industry was that it accurately report on performance. Profit or loss is calculated by subtracting the expenses of an organisation from its income (Deegan 2012, p. 560). The aim of profit reporting is to explain the organisation’s profitability. Profitability is defined as the organisation’s ability to generate profits from the available resources (Birt et al. 2010, p. 304). Profitability is an effective measure of past performance that may be used by shareholders to predict future performance. Financial statements depict historical information and profit reporting will influence perceptions of future profitability. Profit or losses generated by an entity will also have a direct impact on the equity of an organisation; with a consequential impact on assets and/or liabilities (Deegan 2012, p. 560).

6.3.5.2 Societal Contract Breach

The RC identified profit manipulation as one of the construction industry’s unlawful behaviours. Profit manipulation involves the alteration of accounting information associated with profit and loss to convey a particular image; normally aimed at creating a more favourable view of a company’s performance than is warranted (Beattie & Jones 2002). The small profit margins in the construction industry created opportunities for
creative accounting. This was particularly true in the case of managing costs. The RC found two types of contracts used in the construction industry: “payment based on a fixed price, and payment of the costs incurred by the contractor plus a fee for services” (Cole 2003, vol. 4, p. 72). Commissioner Cole noted that “while cost–plus contracts placed the risk on the principal, they offered greater flexibility for the project manager” (Cole 2003, vol. 4, p. 72). However, fixed price contracts had become more common in the industry (Cole 2003, vol. 4, p. 72). The RC identified a number of problems with fixed price contracts (Cole 2003, vol. 4, p. 72). First, tenderers commonly built “risk into the cost of their tender” (Cole 2003, vol. 4, p. 72). Second, “the costs of terminating a deficient fixed price contract” might be more than the costs of continuing with it (Cole 2003, vol. 4, p. 72). Third, a contractor may “seek to enhance his profit by cutting costs, either through lower quality building or litigious behaviour” (Cole 2003, vol. 4, p. 72). In contrast, those in favour of fixed price contracts proposed that “the risks were assigned to the person in the best position to manage it, that is, the project manager” (Cole 2003, vol. 4, p. 72). This type of contract had a direct impact on management of costs. Fixed term contracts placed more pressure on cost management because any cost increases had to be absorbed by the contractor, who was often already under considerable pressure to make a profit. This led to creative accounting solutions, involving the use of accrual accounting, which when abused or illegal, could mislead users of the profit statements about the real financial performance of the company.

The RC found evidence of profit manipulation in the construction industry. However, Commissioner Cole places the blame onto unions for exerting industrial pressure on struggling companies. He frequently refers to small profit margins in the construction industry and how union pressure eroded these small margins for many companies. He also refers to intense competition and tax evasion as reasons for engaging in profit
manipulation. Altogether, Commissioner Cole is almost forgiving of construction companies for engaging in profit manipulation. This raises the important question of whether profit manipulation was inappropriate behaviour or unlawful behaviour. Given the nature of activities involved in profit reporting, accountants must have been involved in profit manipulation. It is an excellent opportunity to explore the level of subjectivity, or creative accounting, within the construction industry. This section will explore just how creative accountants were, and whether some may have stepped over the boundary into fraudulent activity or inappropriate application of the accounting standards.

The consequence of profit manipulation is that the financial position and the results of operations do not fall into fair presentation of financial results. This means that the profit reported will not represent the long-term capacity of the firm to generate earnings. However, profit manipulation may be a matter of different interpretation rather than fraud. Accountants engaged in profit manipulation might be making honest mistakes, or behaving inappropriately if it is intentional, or illegally if fraudulent activities. Profit manipulation, therefore, offers possibilities of a range of accounting behaviour. It is certainly evidence that accounting is a subjective rather than an objective process.

The measurement of corporate profits is a critical method used by society to evaluate an industry or firm’s legitimacy. PIT explains that society confers resources, such as capital and labour, in expectation that these resources will be used wisely and for the benefit of society (Deegan 2013). Profit reporting is central to the process of capital allocation within an economy (Desai 2005, p. 172). The relationship between capital allocation and profit reporting is as follows. Investors infer a firm’s prospects and value from reported profits (Desai 2005, p.172). Suppliers and banks assess profits reported in terms of the firm’s financial health and ability to repay debt. Economists and policy analysts “employ corporate profits to assess the nature of economic fluctuations, to project tax revenues,
and to assess the desirability of a variety of policies aimed at fostering capital formation”
(Desai 2005, p. 173). This discussion illustrates the importance of accurate profit
reporting, and how it represents how society measures the social contract. Society
allocates capital to the construction industry and in return expects that companies will
report honestly and accurately on how they used this capital to benefit society. Profit
manipulation, this context, is a breach of the social contract because the construction
companies are misleading society about how they used the capital allocated to them.

6.4 Conclusions

The purpose of this chapter was to complete the reconstruction the social reality of how
accountants work within the construction industry which began in chapter 5. The chapter
examined the second and third of three constructs adopted from ST, impact and
expectations to explore the social practice of accounting in the construction industry.

The chapter provides three groups of findings: first, understanding the use of power and
level of influence of each stakeholder group; second, discussing further whether social
practice in the construction industry was ethical or managerial; and third, drawing
conclusions about accountants’ differing social contracts which leads to chapter 7 and
further exploration of how to address social contract breach.

The first findings relate to use of power by stakeholders within the construction industry.
Power may be defined at several levels. ST looks at it in terms of influence and
management’s willingness to listen to various stakeholder groups and adjust their
behaviour accordingly. For example, whether people making decisions about tax evasion
were willing to listen to accountants and adjust their behaviour accordingly. Power may
be defined in terms of self-interest. This was measured in terms of short-term versus long-term interests. Short-term interest was a sense of survival, for organisations and individuals. Construction companies operated under tight profit margins and were often under financial pressure to be profitable and solvent. Individuals, including owners/managers and accountants would also have felt job insecurity in an industry where companies regularly went out of business. On the other hand, trade unions had long-term interests to improve the working conditions for their members. Long-term suggests less immediacy and pressure compared with short-term. The trade unions’ survival did not depend upon the success or failure of an individual construction company or individual. Therefore, they were willing to place their long term interests before the short term interests of other stakeholders. They were also able to use political behaviour to exploit the short term interests of others.

Power was also defined in terms of the cause of power. The study makes a further important contribution to SNA theory by using causes of power to explain political behaviour contributing to our understanding of the construct, impact. The analysis produced these findings. The first battle for power between stakeholders was owner/managers and unions. In this battle, the trade unions used coercive power by threatening to expose employers to regulators. The most common threat was to expose tax evasion. There was evidence of the level of threat posed by the trade unions by the use of language such “go down the tube”. The trade unions leveraged the short-term focus of owners/managers by reminding them of the consequences if they did not comply with union demands, that is, business closure, which re-enforced the threat. The results showed that union officials used threatening language and intimidating behaviour to achieve their goals. Commissioner Cole’s description that people “instinctively succumb to the exercise of industrial muscle in the interests of commercial expediency
and survival” (Cole 2003, vol. 3, p. 211) illustrates the success of the trade unions’ political behaviour. The unions did not use this power to direct owners/managers to conduct unlawful financial activities. The construction companies did engage in unlawful behaviours in response to union pressure. However, these activities were decisions taken by the companies themselves. The unions would argue they were only exerting pressure to ensure their members, employees of the construction companies and sub-contractors, were paid what they were entitled to.

The trade unions also used a form of reward power. They would reward owners/managers for compliance with industrial peace. This was important to construction companies because industrial action, such as strikes, would delay projects having negative impact on project management, schedules, and cost. In an industry with tight profit margins, these delays could influence profitability and also business survival. The trade unions knew the impact of these delays. Associated with buying industrial peace, some unions negotiated workplace agreements with contractors which included inappropriate payments in the agreements. In this way, the unions used reward power, in the guise of industrial peace, to negotiate improved working conditions for members and inappropriate payments, sometimes called union sponsorship.

The next battle was between owners/managers and staff. Owners/managers had three types of relationships with staff. First, full-time employees were exploited by owners/managers by withholding or refusing to pay employee entitlements. In this relationship, owners/managers used reward power. They had power to pay staff and also to determine what they paid staff. This made full-time employees vulnerable because they depended upon owners/managers for their income and also their level of income. Some unscrupulous individuals abused this power. The RC also found “substantial” evidence of underpayment or miscalculation of workers’ wages and entitlements. This
occurred for two reasons: to improve their cash flow and to lower costs and improve profitability. The second relationship was with sub-contractors. Owners/managers would exploit the construction industry’s contracting system to pretend full-time staff were sub-contractors to avoid paying employee entitlements and payroll tax.

The trade unions became involved in this relationship and used their coercive power to address inequities in the owners/managers reward power over staff. The RC found three examples of the outcomes of this coercive power: first, increased wages and salaries for employees as a result of union pressure was over award payments; second, some unions tried to force contractors to pay members while on strike, a practice, known as strike pay, which was considered unlawful; and third, demands by the unions related to inappropriate payments or enforced donations either to unions funds or charities. This raises questions about how these payments were classified and recorded. How would an accountant respond if asked by their boss, the owners/managers, to treat a cash donation to a union official as something else?

The third relationship between owners/managers and staff was use of illegal workers. Illegal workers were people who lived in Australia illegally, that is, they did not have a valid visa, and therefore, they may work for low wages on the basis of receiving cash, which enables to avoid paying income tax (Cole 2003, vol. 8, p. 11). Illegal workers were exploited by owners/managers who paid them low wages. This was another example of reward power. Unscrupulous individuals did this to lower costs and, therefore, compete unfairly with law abiding businesses, as well as avoiding paying tax.

The third battle was between owners/managers and suppliers. This complex relationship was shaped by the construction industry’s contracting system. Owners/managers had reward power over sub-contractors. Smaller companies depended upon larger
companies, that is head contractors, for work. The head contractors were aware of this and some exploited the situation and, therefore abused their reward power. They did this in several ways. First, they ignored or did not monitor EBA’s, which were workplace agreements designed to ensure adequate working conditions, including employee entitlements were paid. Commissioner Cole argued that head contractors had a responsibility to ensure sub-contractors had appropriate EBA’s. Second, they did not monitor the financial health of sub-contractors. This meant that head contractors might be doing business with companies which were technically insolvent which is illegal. Third, they delayed or withheld progress payments to sub-contractors, including project variations, for example additional work from the original contract. These latter two activities affected security of payments and illustrates the domino affect caused by the contracting system.

The issues were illustrated by the case of Multiplex, a very large company, who could afford to pay its sub-contractors but it chose not to. Five subcontractors may have been required to demonstrate security of payment to win respective contracts to work with Multiplex. They would, therefore, have been able to demonstrate their ability to pay their staff and any subcontractors they used on the project. However, they were not able to meet their financial commitments during the project. This case shows how the subcontractors’ security of payment situation changed over the life of the project due to the behaviour of the head contractor. Multiplex explained that it chose to engage in non-payment or late payment because it was not being paid by the client. The nature of the reward power abused by head contractors is realised when the options available to sub-contractors is considered. The cost for a small contractor to pursue a head contractor for non-payment/slow payment to them was so high that unless the payment dispute was of a very significant nature, in many instances the small contractor made a commercial
decision not to take the matter further. This explains sub-contractors’ lack of power and perhaps why this abuse of reward power was tolerated by the industry; people felt they had to comply.

The next battle was between owners/managers and general public. The construction industry’s unlawful behaviours affected the broader community, particularly in terms of profit manipulation and tax evasion. The public expects companies to provide honest and accurate financial reports. Investors make decisions on these reports and they expect the truth. The public also expects companies to pay tax in order to meet their corporate social responsibilities. Owners/managers have information power over the general public. They have the power to share information about their company, manipulate this information, and disguise the truth. They also have the power to choose what information to disclose to taxation authorities. The public does not have access to this information and would find it difficult to discover the truth; particularly with smaller companies who do not have to issue annual reports.

What was the role of accountants in this political behaviour? Accountants had expert power based on their financial management capability. This provided them with opportunities to be advisors and even decision makers within construction companies regarding the seven activities listed as unlawful by the RC. However, this expert power had differing influence on other stakeholders. Chapter 5 showed that accountants were often shown respect and tolerance (homogeneity), as well as being allowed to participate in decisions (democracy). However, they were also excluded as outsiders or enemies (heterogeneity) and their opinions were challenged or ignored. Therefore, while they had expert power, this was not always enough to over-ride the reward power of owners/managers who had the fundamental short term power of hiring and firing.
The findings indicate that two types of power dominated relationships between stakeholders in the construction industry: reward power and coercive power. The main problem was the need for reward. In an industry with tight profit margins and the constant threat of business closure, owners/managers and employees were always focusing on the short-term and survival. The trade unions, on the other hand, were aware of the vulnerability of owners/managers and used coercive power to try to address their long-term goal to improve working conditions in the industry. A way forward would be to decrease the reward power of owners/managers. This would reduce employees’ the need for reward and the need for trade unions to exercise coercive power. This might be achieved by getting all stakeholders to adopt a long term perspective which embraces the viability of the industry as a whole rather than competing at the expense of one another. While this is aspirational, it enables the framing of a set of societal expectations which would help repair the construction industry’s legitimacy and restore the social contract.

The main societal expectations of the construction industry were:

First, contribute to public funds. This was an expectation that construction companies would meet their corporate citizenship responsibilities and pay taxes. In this way, they would contribute to the funds gathered by government to be shared with all of society through government services. Tax evasion was the main problem in this area.

A major cause of tax evasion behaviour was the industry’s complex contracting system. It is reasonable to assume that smaller companies were the main problem due to the widespread use of sub-contractors, use of cash payments, and the lack of financial reporting required of these companies. Given smaller companies usually did not employ an internal accountant; it tends to excuse accountants
from their social contract in terms of tax evasion. Yet these companies still had to use an external accountant, that is a tax agent, to do their annual tax returns. These external accountants were breaching their social contract. Further, the findings showed that larger companies also engaged in tax evasion. The ATO concluded that “the tax planning and other behaviours of the 17 entities in the property and construction industry are consistent with those entities in other industries” (Cole 2003, vol. 9, p. 62). In other words, the large companies in the construction industry engaged in tax planning in ways similar to large companies in other industries. This means that some internal accountants in large companies would have breached their social contract in terms of tax evasion.

The RC also found significant incidence of fraudulent phoenix company activity in the construction industry (Cole 2003, vol. 1, p. 122). It is important to highlight the word ‘fraudulent’ used here by Commissioner Cole. Phoenix companies were created by the construction industry to avoid paying tax and this activity was considered illegal. The significance of the societal contract breach by phoenix company activity is not limited to avoiding taxation. What makes phoenix activity so objectionable to the public is its widespread impact on so many parts of society. Those hurt by phoenix activity include unsecured trade creditors, employees and revenue authorities (Anderson 2012, p. 412). In addition to losing their wages, redundancy and pay in lieu of notice, employees may also lose their accrued annual and long service leave entitlements in the case of phoenix activity (Anderson 2012, p. 412).

Accountants must have played some role in phoenix activity (see chapter 5), and breached their social contract whilst bending the rules, that is, accounting standards, in their work with company directors involved in phoenix activity.
However, accountants’ social contract may have been unreasonable in this case. Evidence on how difficult it may have been for accountants to change phoenix company activity is provided by how difficult the regulators found it to police unlawful behaviour. Anderson (2012) explains how frustrated the Federal Government was with continued phoenix activity six years after the RC. If the ATO felt powerless to enforce the law regarding phoenix activity, how could accountants employed by the construction industry have felt any differently? This evidence suggests that accounting practice regarding phoenix activity had not changed. First, phoenix activity was actually increasing in the period after the RC. Second, accountants were unlikely to have the authority or disincentives to prevent fraudulent phoenix activity. Therefore, it is conclude that there were no observable changes to accounting practice regarding phoenix activity in the period after the RC. Accounting may be considered a subjective practice in regards to phoenix company activity. Accountants employed by the construction industry were applying subjective judgements in their work associated with phoenix activity depending upon the amount of pressure exerted on them by others, such as company directors.

Second, pay employees their entitlements. This was an expectation that individuals employed by construction companies would receive their salary and non-salary reward for their work. Underpaying employees or avoiding payment altogether through insolvency were the main problems in this area. In an industry with intense competition and small profit margins (see chapter 3), owners or investors and management would have been under pressure to reduce expenses and improve profitability. It is easy to see how underpayment of employee
entitlements would have occurred in these operating conditions, given entitlements are an expense in the IS.

The social contract breach affected relationship between owners/managers and staff in three ways. First, employees pretended to be contractors. Second, was the use of cash payments. Third, was the use of pyramid subcontracting. These issues illustrated the systemic structural and cultural problems in the construction industry. This is a significant social contract breach. Society expects organisations to pay staff what they are entitled to. Australian culture has a legacy of ‘getting a fair day’s pay for a fair day’s work’, which was discussed in chapter in the history of the trade union movement. The consequences of non-compliance and underpayment of employee entitlements, is that society suffers, through the financial impact for employees who do not receive their full entitlements. Yet, it was not just about underpaying staff. The industry developed systemic ways of avoiding its social contract with a deliberate intent to breach this contract and avoid its moral and ethical obligations to pay people what they are entitled to. Given the high involvement of accountants in employee entitlements (see chapter 5), they must accept responsibility for participating in this systemic breach of social contract.

Third, pay suppliers their entitlements. This was an expectation that companies and individuals who provide materials and services to construction companies, including sub-contractors, be paid appropriately in return. There were two types of payment issues associated with the unlawful behaviour within the construction industry identified by the RC. First, delaying or withholding payments in the normal course of completing a construction project. Second, delaying or withholding payments as the result of business failure, that is, liquidation. There
was also incorrectly recording the expense to disguise unlawful behaviour. While all three behaviours are serious, Commissioner Cole focused mainly on the third behaviour, incorrect recording of expenses, because it allowed the opportunity for illegal and corrupt behaviour such as bribes. It also had a significant impact on security of payments. Given the involvement of accountants in inappropriate payments (see chapter 5), they must accept some responsibility for participating in this breach of social contract.

Fourth, provide accurate performance reporting. This was an expectation that construction companies would honestly and accurately report on their business activities, including profit reporting. Society includes public and private investors; as well as other stakeholders interested in the financial position of construction companies such as customers, creditors (for example banks), suppliers, and regulators. These stakeholders want to know if they will get a return on their investment, have their building project completed, and whether they will be paid. Profit manipulation was the main problem in this area.

The consequence of profit manipulation is significant because the financial position and the results of operations do not fall into fair presentation of financial results. This means that the profit reported will not represent the long-term capacity of the firm to generate earnings. It is misleading the public. However, profit manipulation is not considered to be fraud. It is a matter of interpretation. This indicates that accountants engaged in profit manipulation are perhaps behaving inappropriately, particularly if their interpretation does not involve honest mistakes, that is, it is intentional; but it is not illegal, unless they engage in fraudulent activities. There is a grey area between creative accounting and deliberately misleading the public by providing false information. Accountants
involved in profit manipulation in the construction industry would argue they were simply trying to serve the best interests of their company with creative accounting. Chapter 5 also found that this activity typically excluded accountants wherever possible, that is the relationship with stakeholders was hostile because they were seen as the enemy. Therefore, profit manipulation is the area where accountants would be seen as having the least contribution to the social contract breach. It would also be argued it was an area where they were placed under the most pressure by owners/managers using reward power to coerce them. It is certainly evidence that accounting is a subjective rather than an objective process.

Commissioner Cole was scathing in his criticism of the construction industry’s unlawful behaviour. While he is often highly critical of unions and sympathetic towards employers, he concludes that “every participant bears some responsibility” (Cole 2003, vol. 3, p. 211). Accountants played a role in the social contract breaches found in this chapter. Chapter 7 will discuss the research findings and suggest ways that accounting may be used to address these social contract breaches and legitimise the construction industry.
CHAPTER 7: ACCOUNTING AS A LEGIMIZATION PROCESS - A CONCEPTUAL MODEL

7.1 Introduction

This chapter develops a preliminary conceptual model on the role of accounting as a legitimisation process, based on the findings presented in this study. As discussed in chapter 2, LT asserts that “organisations continually seek to ensure that they are perceived as operating within the bounds and norms of their respective societies, that is, they attempt to ensure that their activities are perceived by outside parties as being ‘legitimate’” (Deegan 2009, p. 323). LT is part of the broader PET (Gray, Owens & Adams 1996). PET explains how capitalism, as a social system, is shaped by economic and political interests (Gaffikin 2008, p. 82). In a capitalist society, such as Australia, there are many social inequalities amongst social classes brought about by their inequitable access to the use of resources. Economic forces serve to protect the interests of those with access to resources. Regulation is the political forces used to find more balance in the allocation of these resources.

LT fits within PET because it explains how organisations obtain access to resources in return for acting within the broader public interests. In essence, responsible corporate citizenship is rewarded with approval by society and wealth. The measure of legitimacy expectations is the social contract. Historically, social contracts were measured by profit. Traditionally, accounting theory has been situated within the goal of profit maximization as the optimal measure of corporate performance (Patten 1991). Under this notion, a firm’s profits were viewed as an all-inclusive measure of organisational legitimacy.
(Ramanathan 1976) because this increased societal wealth. However, an increase in corporate disasters, for example Enron, and unethical behaviour has led to a shift in focus. Social contracts now expect organisations to react and “attend to the human, environmental, and other social consequences” of their activities (Heard & Bolce 1981, p. 247).

Legitimacy, therefore, is the measure of societal perceptions of the adequacy of corporate behaviour (Suchman 1995). Legitimacy is a theoretical concept in the sense that there is usually no clear statement from society about what it expects of an organisation. It is unlikely that an organisation can find a copy of their social contract and ‘negotiate’ that with society (Deegan 2009, p. 326). However, this study has identified that the construction industry had a very clear social contract. The RCR defined societal expectations of the industry and its social contract breach. The legitimacy gap, as defined by this study, was the seven unlawful activities identified by the RC, for example tax evasion. If the industry wanted to regain legitimacy and restore public confidence, it needed to address the unlawful behaviours associated with these seven activities.

The main societal expectations of the construction industry were listed at the conclusion to chapter 6, for example contribute to public funds. Construction companies and other industry stakeholders were able, therefore, to find a copy of their social contract. The RC findings told the industry stakeholders what society expected of them (see section 6.3.1 for explanation).
7.2 The Role of Accounting

7.2.1 Critical Accounting

Critical accounting can identify theories for changing the way accounting is practiced in industry and ultimately lead to reforms in how business and society operate (Deegan 2009, p.530). CAT aims to identify the prevailing social arrangements within a community, such as an industry, within the broader context of the society in which it exists (Roslender 2006, p. 250). CAT aims to promote self-awareness of both “what is” and “what might be”, and how the former might be transformed to install the latter (Roslender 2006, p. 250). It is concerned with the promotion of a better society, and understanding the change processes necessary to achieve this goal. Therefore, it lends itself to examining the role of accounting in legitimising the construction industry.

Chapter 6 showed that the accounting process was manipulated by stakeholders within the construction industry. This manipulation occurred in the seven unlawful activities identified by the RC. Chapter 5 used SNA theory to extend critical accounting’s ST. This allowed development of analytical frameworks to examine the interaction between construction industry stakeholders (relationships), how stakeholders influenced each other (impact), and how this produced different social contracts for each stakeholder (expectations). The analysis showed that accountants would have been involved in each of the seven unlawful activities. Further, accountants were involved because many of the processes associated with the unlawful activities were the work of accountants. Finally, accountants would have been under considerable pressure to engage in creative accounting in conducting work associated with these unlawful processes. Accountants were either internal or external to the firm, in the case of small firms.
From a CAT perspective, chapters 5 and 6 established the social practice of accounting, that is, the ‘what is’. Chapter 7 proposes a way to learn from the events surrounding the construction industry at the time of the RC and to develop a role for accounting that might address the unlawful activities. In this sense, chapter 7 will propose a ‘what might be’ with the aim of using accounting to change the processes associated with this unlawful behaviour and help the construction industry address its legitimacy gap.

7.2.2 Legitimation of the Construction Industry

Legitimation is the process that leads to legitimacy (Deegan 2005; Lindblom 1994). Legitimation tactics might differ depending upon whether the entity is trying to gain, maintain, or repair legitimacy (Deegan 2009, p. 331). Deegan (2009) argues that theoretical development in this area remains weak. Given the historical context of the study, this represents an area where a significant theoretical contribution can be made. Chapter 7 proposes strategies to repair legitimacy. The only real difference between gaining and repairing legitimacy is that gaining is a proactive approach and repairing is a reactive approach. Repairing involves responding to a crisis. The RC definitely created a crisis.

In Lindblom’s (1994) recommendations for repairing legitimacy, the first two are possible in the case of the construction industry, while the latter two are not possible:

1. Communicate to the public the organisation’s performance and activities which align with society’s expectations
2. Change perception of the public via disclosure of positive or desirable activities, without falsifying
3. Manipulate perception by deflecting attention from problem areas onto positive or desirable activities
4. Change social expectations, perhaps by arguing they are unreasonable.

The first two strategies involve correcting undesirable behaviour and communicating this to the public. The latter two strategies involve manipulation and changing society’s expectations, neither of which would be accepted by the public. There are, therefore, two steps to repairing the construction industry’s legitimacy: fix the unlawful behaviours and communicate this to the public. Deegan suggests that the actual conduct of the organisation is somewhat irrelevant and rather it is what society collectively knows or perceives that shapes legitimacy (Deegan 2009, p. 324). However, given the construction industry’s history of unlawfulness and the high level of public scrutiny, it is unlikely that the public would be satisfied in just being told that the industry was behaving. This creates an opportunity for accounting to help fix the unlawful behaviour and then to communicate that information.

LT emphasizes that the organisation must appear to consider the rights of the public at large, not just shareholders or investors (Deegan 2009, p. 325). It explores questions about the type of information that needs to be disclosed, and how organisations can persuade society that they are behaving legitimately. The construction industry has many challenges if it is to repair its legitimacy and address the social contract breach.

The first challenge is to persuade the public that the construction industry is willing to contribute to public funds. Australia is under fiscal pressure. The Federal Government is spending more than it earns which has resulted in a large budget deficit. The public expects organisations and individuals to help address this problem by paying taxes. The construction industry’s reputation for tax evasion has created a very negative perception amongst the Australian public. The industry needs to restore public confidence by showing it is willing to meet its corporate responsibility to pay tax.
The second challenge is to persuade the public that the construction industry is willing to pay employees their entitlements. Australian culture is based on values of fairness, equity, and comradery, that is, mateship. In a work context, these values translate to the idea of a fair day’s pay for a fair day’s work. Australia’s history of trade unionism has been built upon these values (see chapter 5). The public expects construction companies to uphold these values in their treatment of employees, particularly ensuring employees receive expected salary and non-salary reward for their work. The industry needs to restore public confidence by showing it is willing to pay employees what is expected, and to also stop illegitimate insolvency aimed at avoiding payment altogether.

The third challenge is to persuade the public that the construction industry is willing to pay suppliers their entitlements. This was an expectation that companies and individuals who provide materials and services to construction companies, including subcontractors, be paid appropriately in return. This problem is similar to employee entitlements, except this often involves small business owners, usually companies employing one-to-five staff. The public expects that these small business owners and their staff also be treated with fairness and equity. The industry needs to restore public confidence by showing it is willing to pay suppliers what is expected, and to also stop delaying or withholding payments.

The fourth challenge is to persuade the public that the construction industry is willing to accurately report on its performance, particularly its financial reporting. This was an expectation that construction companies would honestly and accurately report on their business activities, including profit reporting. Society includes public and private investors, as well as other stakeholders interested in the financial position of construction companies such as customers, creditors such as banks, suppliers, and regulators. These stakeholders want to know if they will get a return on their investment,
have their building project completed, and whether they will be paid. The industry needs to restore public confidence by showing it is willing to stop profit manipulation.

In summary, the construction industry can repair its legitimacy by addressing the business processes associated with these broad activities and communicate that to the public:

1. Meet its corporate responsibility to pay tax
2. Pay employees what is expected
3. Stop illegitimate insolvency
4. Pay suppliers what is expected
5. Stop making and receipting inappropriate payments
6. Stop profit manipulation

7.2.3 What Can Accountants Do?

Chapters 5 and 6 found that accountants would have been involved in all seven unlawful activities identified by the RC. Therefore, accountants could help repair legitimacy in the construction industry by changing their behaviour to improve the way these activities are performed in the construction industry and help eliminate unlawful behaviour.

To understand what accountants can do to help the construction industry repair legitimacy, it is necessary to examine three issues:

1. Why do accountants act subjectively rather than objectively when doing their work?
   By subjectively, it is meant that accountants have scope to act independently of the accounting standards; that is, to use their own judgment, intuition, experience, or organisational context to adapt the standards. By objectively, it is meant that accountants always follow the standards. This study has shown that accountants in
the construction industry acted subjectively. They did this because accounting allows scope for what is called creative accounting.

2. Why did accountants in the construction industry become involved in activities they should have known were unlawful? This was explained in chapter 6 by the pressure placed on accountants by other stakeholders (see the section on Impact). Despite this, accountants still have free will and choice about how they behave. To understand this behaviour, accountants’ motivation will be explored.

3. Did accountants have different social contracts? Society’s expectation of accountants varies depending upon the stakeholder. The public expects accountants to be guardians of good financial management within organisations. Accounting bodies expect accountants to uphold good accounting practice and follow the standards. Industry stakeholders, particularly owners/managers, expect accountants to help them achieve their business goals. There are conflicting goals amongst these three groups. If accountants are to change their behaviour to satisfy the public, and help restore confidence in the construction industry, this may make their employer unhappy. At a fundamental level, the accountant needs to be employed to satisfy the need for income for them and their family. Employers, that is, owners/managers, have the power to hire and fire. Employers, not the public, provide accountants with the income they need. These conflicting demands on accountants can be explored through the six legitimation behaviours expected of the industry outlined at the conclusion of section 7.2.2.

In exploring the first issue, why do accountants act subjectively rather than objectively when doing their work, creative accounting is used. Creative accounting is “the transformation of accounting figures from what they actually are to what perpetrators desire by taking advantage of the existing rules and/or ignoring some or all of them”
The difference between creative accounting and fraud is that creative accounting is working within the regulatory environment but fraud involves breaking the law or violating the regulatory framework (Jones 2011). In Australia, the regulatory environment for accountants has two dimensions: ASIC enforces compliance with the accounting standards and the accounting bodies have the power to sanction or discipline members only for errant behaviour, and the social contract enforced by the government on behalf of society.

Generally, fraud involves “deliberate distortion of accounting records, falsification of transactions, or misapplication of accounting principles” (Salem 2012, p. 1). Irrespective of how the fraud is manifested, it is “typically difficult for auditors to discover since the perpetrators take steps to deliberately conceal the resulting irregularities” (Salem 2012, p. 1). Furthermore, most accounting practitioners realize that “auditors are often not positioned to detect the occurrence of fraud” (Salem 2012, p. 3). Auditors are deprived of the “continuous presence necessary for the establishment and implementation of fraud prevention and deterrence programs” (Salem 2012, p. 3). This means that auditors are not present all of the time and, therefore, inappropriate practices, which might even be routinely done at an organisation, may be hidden from auditors during the short period when they are physically present at the organisation doing their audit.

Creative accounting is allowed by law in some countries, such as Greece (Baralexis 2004), while in some other countries it is considered illegal (Healy & Wahlen 1999). Similarly, some researchers argue that creative accounting is legitimate and ethical, while others consider it illegitimate and unethical (Healy & Wahlen 1999). Creative accounting is very important to the discussion of the role of accounting as a legitimising process. Creative accounting suggests accounting is a subjective process, where individuals have scope to make judgments regarding whether they follow the rules, that
is accounting standards, or not, and the type of information included in accounting disclosures. On the other hand, if accounting is an objective process, accountants would not engage in creative accounting. The social reconstruction of accounting in the construction industry, therefore, aims to establish the degree of creative accounting.

One of the main forms of creative accounting is “creative disclosure” (Matis, Vlalu, & Cuzdriorean 2012, p. 73). Creative disclosure is located in step three in the accounting process (Deegan 2013, p. 630), and evidence is found in annual reports under forms of distortion of financial information, often found in numerical and graph manipulation (Matis, Vlalu & Cuzdriorean 2012, p. 73). “Creative accounting presented under all its forms of manifestation can directly affect the profit and loss account and also the balance sheet and it is also related to measurement or disclosure, the latter referring to the extent of to the method of presentation” (Matis, Vlalu & Cuzdriorean 2012, p. 73).

Matis, Vlalu and Cuzdriorean (2012, p. 75) states that “creative presentation must be regarded as a complex mechanism that comprises: motives for engaging in manipulation of accounts, types of information disclosed, and types of manipulations strictly connected to presentation of information”. The types of information presented comprise of two categories: verbal information and numerical information (Matis, Vlalu & Cuzdriorean 2012, p. 75). The following strategies are summarized in regards to the types of manipulations connected to presentation of financial information:

- Using a creative manner to make the text difficult to read;
- Using persuasive language that comprises only positive words and emphasizes positive financial performance;
- Using creative visual manipulation in the way information is presented with the scope of attracting the attention from others items that are important but in the same time are not flattering for the financial performance presented;
- Using performance comparisons that involve choosing the benchmarks that portray current financial performance in the best possible light (Matis, Vlalu & Cuzdriorean 2012, p. 75).
Each one of these strategies is not part of an objective disclosure choice. Furthermore, these strategies are based on subjectivity and bias (Matis, Vladu & Cuzdriorean 2012, p. 75), which provides evidence for how accounting as a subjective process occurs.

Creative accounting, such as creative disclosure, is apparently widespread. Firms have been manipulating accounts for a long time, and this practice has been given various names in the literature including: earnings management, income smoothing, big bath accounting, creative accounting, and window dressing (Stlowy & Breton 2004). Stlowy and Breton (2004) provide a comprehensive literature of the topic, which they summarise as accounts manipulation. While creative accounting is a theme throughout the accounting practices presented in this chapter, accounts manipulation is particularly relevant in section 7.3.1.3 inappropriate payments and section 7.3.1.6 profit manipulation. The motivation for accounts manipulation stems from the desire to influence wealth transfer between the various stakeholders (Stlowy & Breton 2004). The use of the word manipulation suggests that accounts are prepared in a way that differs from normal accounting practice; and here Stlowy and Breton (2004) are suggesting this happens because a stakeholder wants to profit at the expense of others. Stlowy and Breton (2004) identify the potential targets of manipulation in the financial statements as earnings per share (EPS) and the debt-equity ratio. “Earnings per share can be modified in two ways: firstly, by adding or removing some revenues or expenses (modification of net income), and secondly, by presenting an item before or after the profit used to calculate the earnings per share (classificatory manipulations)” (Stlowy & Breton 2004, p. 7). In certain countries where full dilution is not mandatory, the denominator can also be manipulated by applying unrealistic assumptions that are very difficult to challenge (Stlowy & Breton 2004).
Who then is involved in creative accounting? In their analysis of several corporate accounting scandals Yallapragada, Roe & Toma (2012) found that corporate fraud, white-collar crime, and identity theft were costing the United States hundreds of billions of dollars every year. Accounting fraud is defined as “knowingly falsifying accounting records in order to boost sales revenue and net income and is perpetrated by corporations by means of presenting false information, using funds for illegal purposes, overstating revenues, understating expenses, overstating the value of corporate assets, and understating liabilities” (Yallapragada, Roe & Toma 2012, p. 1). Yallapragada, Roe & Toma (2012, p. 4) were scathing in their criticism of Enron and WorldCom, describing their accounting fraud as “the result of unbridled greed of corporate executives, utter lack of ethical standards, unscrupulous and cooperating auditors, lawyers, and bankers, lack of regulations, political favours, and useless and ineffective board of directors”.

A final word on creative accounting is provided by Dickinson (1913) who described the role of accountants in these terms. The accountant’s responsibility is “largely moral, and only to a small extent legal” (Dickinson 1913, p. 240). This suggests that accountants have an ethical responsibility, but are not necessarily legally obligated to do so. The reason for this point is found in Dickinson’s discussion of the facts, where he argues that ascertaining facts is the “simplest and frequently the smallest and least important part of the work” of an accountant (Dickinson 1913, p. 240). At this point, Dickinson shows that he sees accounting as a subjective process, although he does not use those words. He argues that accountants use their judgment, or their “trained mind”, to “approximate the facts as is practicable” (Dickinson 1913, p. 240). This description of accounting practice as an approximation, based on the accountant’s interpretation, provides evidence from this work that accounting is subjective. In reconstructing the reality of accounting in the construction industry, this study aims to suggest what was
“practicable” for accountants employed by the industry in the period under review. Dickinson suggests that the only legal responsibility for accountants is limited to “gross errors of omission or commission” (Dickinson 1913, p. 240), which suggests major mistakes which would be obvious to any other accountant. However, he provides an escape clause by suggesting this legal responsibility “would not extend to errors of judgment” (Dickinson 1913, p. 240), in other words accountants are allowed to make mistakes if their interpretation is within a tolerable range. From a creative accounting perspective, this discussion appears to allow accountants scope to use their professional judgment to find their approximate view of the facts, so long as it does not vary too far from what others would also find, that is, it is not a “gross error”. While accounting is far more complex today than it was in 1913 when Dickinson wrote these comments, it is useful historical context and enables consideration of accounting values in a simpler time. The issues of judgment and honesty still apply today.

In exploring the second issue, why did accountants in the construction industry become involved in activities they should have known were unlawful, accountants’ motivation is used. As was discussed in chapters 5 and 6, when accountants became involved in business processes associated with unlawful activities they were either acting alone or on the direction of another stakeholder, often owners/managers. In examining the motives of accountants in the construction industry, it is necessary to distinguish between self-motivation, that is acting alone, and motivation created by others, that is pressure exerted by other stakeholders. In following the theme consistent throughout this study, the analysis does not seek to find the truth about accountants’ motives, as only they could tell us what was inside their heads at the time which would be very difficult to discover. Rather, the aim is to reconstruct the social practice of the industry at that time by inferring motive.
Behavioural finance (Shefrin 2000) has identified three principal themes that cover many types of inappropriate behaviour, such as accounting manipulation; including heuristic-driven bias, frame dependency and inefficient markets. These themes involved cognitive constraints, bias and frame dependency, and imperfect access to information, inefficient markets. In the case of accountants employed by the construction industry at the time of the RC, this translates in terms of whether they made mistakes or errors in judgment or whether they operated in an imperfect world. Dechow and Skinner’s (2000) research on accounts manipulation is based on motivations linked to market expectations. This defines what information stakeholders not only expect from financial reports but also whether they should expect perfect information.

Stlowy and Breton (2004) define accounts manipulation as “the use of management’s discretion to make accounting choices or to design transactions so as to affect the possibilities of wealth transfer between the company and society (political costs), funds providers (cost of capital) or managers (compensation plans)” (Stlowy & Breton 2004, p. 6). In the first two cases, the firm benefits from the wealth transfer. In the third, managers are acting against the firm. The firm benefits from the wealth transfer. Figure 7.1 summarizes the principles of accounts manipulation. The distinction between political costs, cost of capital and compensation plans is taken from Watts and Zimmerman (1978).
Firms in the construction industry are economic entities in the sense that their main purpose is to create wealth. Wealth is created for owners and investors, but also for management and staff, including accountants, in terms of employment. Wealth is provided for material and service providers to construction firms; which includes banks, suppliers, and professional firms such as external auditors and accountants, in the form of payment from the firm to the supplier. The role of external auditors and accountants is particularly important for this study because the majority of construction firms are small and would not employ internal audit, tax or accounting staff. Wealth is important to the unions in terms of the welfare of members, that is, construction industry employees, and the union leaders. Wealth is also created for society in terms of the direct and indirect economic benefit of the construction industry (see chapter 3).
The fundamental driver in the motivation of accounting manipulation is wealth creation. In the development of a conceptual model explaining why accounting manipulation occurred in the construction industry, this chapter examines the tensions amongst stakeholders in the distribution of wealth. This conceptualization is supported by earlier research. Stlowy and Bretton (2004) found that accounts manipulation mainly emanates from the desire to influence the likelihood of wealth transfer between the various stakeholders. This chapter will show that the main stakeholder in the battle for wealth distribution in the construction industry was owners/managers, who worked both for and against the firm in negotiating stakeholder share of wealth.

Wealth is, therefore, the key driver of the unlawful behaviour within the construction industry. Owner/managers were under significant pressure to cut costs to ensure profitability and survival in an industry characterised by fierce competition and small profit margins. Accountants may have been influenced by self-interest to protect and sustain their job. If their company survives, they get to keep their job. That must have been a powerful motivator in an industry where companies regularly declared insolvency and went out of business. This establishes justification for creative accounting. However, accountants would still be faced with a choice about how creative they were willing to be. Is there a line which may be drawn, where accountants say they cannot cross?

To answer this question, the difference between manipulation and fraud must be established. Manipulation that is outside the law and standards constitutes fraud (Stlowy & Bretton 2004, p. 9). The activities covered by the terms “earnings management” (income smoothing, big bath accounting) or generally “creative accounting” normally remain within the law (Stlowy & Bretton 2004, p. 9). In this study’s examination of accounting manipulation in the construction industry, it is necessary to classify the types of activities discussed in chapters 5 and 6 in terms of whether they were creative
accounting or fraud. The difference appears to involve intent, that is, did the accountant intend to provide misleading information, or was it an error either due to incompetence, resulting in a mistake, or an error in judgment due to misinterpretation.

Fraud occurs when somebody commits an illegal act (Stlowy & Bretton 2004, p. 11). In the case of financial statements, fabricating false invoices to boost sales figures is fraud, while interpreting consignment sales as ordinary sales is an error (Stlowy & Bretton 2004, p. 11). The difference, however, does not appear clear to everyone. The American commission created to investigate fraudulent financial reporting defines fraud as “any act resulting in ‘materially misleading financial statements’” (National Commission on Fraudulent Financial Reporting [NCFFR] 1987, cited by Belkaoui 1989b, p. 62). In his classification of fraudulent behaviour, Merchant (1987, cited by Belkaoui 1989a, p. 67), defines what is considered to be real fraud, that is, falsifying or altering documents, deleting transactions from records, recording forged transactions or concealing significant information. Brown (1999) analyses the difference between earnings management and reporting fraud and points out that the distinction between the two is often very narrow.

At this point it is important to examine the motives behind fraud and creative accounting. Fraud seems to involve a deliberate intent to falsify financial reports and provide misleading information, whereas creative accounting appears to involve interpretation of accounting standards in a way that benefits the firm. This is where the lines between fraud and creative accounting become blurred. If an accountant deletes a transaction from the firm’s accounting records or fails to include significant information, can they defend themselves against allegations of fraud by arguing they made a mistake or that they did it based on their interpretation of the accounting standards? If so, the accountant can say that they were doing creative accounting and not engaging in
criminal activity. In this chapter, the conclusion is drawn that the distinction between fraud and creative accounting may be found in terms of the level of stakeholder involvement. If management, or another stakeholder, tells the accountant to deliberately falsify financial reports, for example, then this is fraud, as defined by Merchant (1987), and the accountant is involved in illegal activity, even if it is under duress. If the accountant engages in this activity without being told to do so by management or another stakeholder, then it may be concluded that it is based on their interpretation of accounting standards, and it is creative accounting and not illegal. The issue then comes down to intent and whether the accountant performs account manipulation under the direction by others, against their own judgment, or on their own, based on their judgment. The latter absolves them from fraud so long as they are attempting to follow accounting standards.

Support for this argument is found in Merchant’s (1987) discussion that accounts manipulation is related mainly to interpreting accounting standards. In most countries, GAAP allow for a certain degree of interpretation (Stlowy & Bretton 2004, p. 11). “To be legal, interpretations may be in keeping with the spirit of the standard or, at the other extreme, clearly stretch that spirit while remaining within the letter of the law” (Stlowy & Bretton 2004, p. 11). They may be erroneous, but never fraudulent (Dechow & Skinner 2000). Therefore, accountants are allowed to make mistakes or errors in judgment. This tolerance is even quantified by researchers as a “fair presentation zone” (Stlowy & Bretton 2004, p. 11), which is the degree of error tolerated in financial reporting before moving into the area of fraud. In this way, Stlowy and Bretton (2004, p. 11) conclude that accounting manipulation is not fraud; it is just a matter of interpretation.
In summary, if accountants in the construction industry were engaging in accounting manipulation rather than fraud, it may be argued that they were simply being creative and were not actually doing anything illegal. While this behaviour supports this study’s central theme that accounting is a subjective rather than an objective process, it does not help find a way forward. If accountants can avoid punishment or responsibility for their behaviour in the construction industry, they will most likely continue to behave in the same way. Accountants will continue to be creative in the processes identified in chapter six because they are motivated by self-interest to do so, that is, to maintain employment.

It seems the only way forward, if accountants are to help repair the construction industry’s legitimacy, is to make them accountable for the unlawful processes identified in chapter 6. This may be done by exploring the third issue outlined at the start of this section.

In exploring the third issue, did accountants have different social contracts with industry stakeholders, the results from chapters 5 and 6 are used to reconcile stakeholder conflicting demands and make accountants accountable. In simple terms, if accountants had worked alone then these unlawful processes might be described as mistakes, errors in judgment or creative accounting. However, if accountants worked under the direction of other stakeholders, it may be described as fraud. For example, the conceptual framework presented in figure 5.3 (see chapter 5), showed that the role of accountants in inappropriate payments was isolation. This proposes that accountants might have processed an invoice marked as “sponsorship” for a trade union social event as a legitimate activity, whereas the funds might have been a cash payment to a union official for industrial peace. The accountant was involved in the activity but might be excused because they did not know the truth and this could be described as an honest mistake. On the other hand, tax evasion was an area where accountants must have been actively
involved with unscrupulous individuals. While accountants might argue their role is to help minimise tax, that is, use creative accounting, some of the tax evasion activities were illegal. If accountants participated in this type of activity they cannot defend themselves by saying the boss put pressure on them. It is still an illegal activity irrespective of the pressure exerted.

Figure 5.3 explained how the seven unlawful activities identified by the RC involved different social practice, defined by the three stakeholder constructs used in chapter 5: relationships (interaction) and chapter 6 impact (harmony), and expectation (cohesion). The summary map plots the location of the seven activities in terms of their dominating characteristics. The percentage under each label indicates the proportion of processes associated with this activity which have these characteristics (see table 6.2 in chapter 6).

The figure illustrates how accountants are heavily involved with the broad range of stakeholders in making decisions in the seven areas outlined. However, at this point there is a need to differentiate between social interaction and information usage. ST explains that varying social contracts will be negotiated with different stakeholder groups. In reconstructing the social reality of accounting within the construction industry, this study seeks to infer the nature of the various social contracts accountants had with the other stakeholder groups. This will provide an understanding of society’s expectation of accountants through the lens of those they interacted with.

Accountants’ interaction with construction industry stakeholders was personal and impersonal. It was personal in the sense that accountants interacted socially with others in doing their work and in helping others find meaning and interpretation in their work outputs, that is, their reports. Accountants employed by the construction industry would interact closely with internal users of their reports in meetings and other work
interaction. Interaction was impersonal in the sense that the work produced by accountants have been read and interpreted by others without any personal contact with the accounting staff that produced the report. For example, an investor might read the financial statements of an entity produced by an accountant whom the investor has never met nor ever interacted with. Similarly, an official from the ATO might review taxation returns prepared by an accountant whom they have never had personal contact with. The distinction between personal and impersonal interaction highlights that accountants had different interaction with the construction industry’s various stakeholders. This different interaction is explained by the type of work output, internal versus external, and the type of decision. Accountants were much more likely to have personal interaction with internal users, and impersonal interaction with external users. This then raises the question of what was accountants’ social contract with internal versus external users.

The social contract with external users was most likely objective in the sense that accountants were expected to follow standards and behaviours expected from accountants in any industry. Owners/investors, for example, would expect to see common accounting treatment of expenses and income, so that they could compare one entity against another and make appropriate investment decisions. Similarly, regulators including the ATO, accounting bodies, and auditors, would also expect accountants to follow accounting standards and taxation legislation. Banks and suppliers would expect not to be misled and that accountants would provide them with honest and accurate information on the entity’s financial position, particularly its capacity to repay debt. Society would expect accountants to represent it in accurately portraying how well the entity is managing its resources. This discussion highlights that accountants probably played an objective role in interaction with external users of work outputs, that is, financial reports. Owners/investors or regulators, for example, would have been unlikely
to interact personally with accountants and to try to influence them to behave in any way other than what society would expect of an accountant in any industry. This situation may, of course, have been different in the case of small firms or privately owned businesses, such as subcontractors, where the owner or investor was often the manager. The only other exception was the unions.

The social interaction with internal users, including the unions, was more likely to be personal and to result in accountants playing a subjective role. By a subjective role, it is meant that accountants had different social contracts with the various internal users. The different contract resulted from internal stakeholders having different expectations of accountants.

In understanding the nature of accountants’ different social contracts with industry stakeholders, it is necessary to consider the four steps in the accounting process (Deegan 2013). While external users are most interested in the work outputs of accountants, that is, step four financial reports; internal users interact with accountants at all four steps.

Step one is identifying business transactions. As outlined above, this step involves accountants identifying events that will have an impact on the financial performance of the entity. Figure 7.2 identified these as cash withdrawals, payment of wages and salaries, earning of fees revenue, and payment of tax. In reconstructing accountants’ social contract with stakeholders here, there is a need to identify who was involved and what they expected.

Cash withdrawals would involve owners/investors and management. Accountants would not necessarily be informed of cash withdrawals. Cash outflows are movements of cash out of the entity resulting from transactions with an external party. However, it is often not practical to record every transaction separately in the cash flow statement (CFS).
Therefore, to ensure the CFS is not too lengthy, cash inflows and outflows are grouped into activities: operating activities, investing activities, and financing activities. It is reasonable to assume that owners/investors or management could have withdrawn funds from a firm’s bank account, used those funds to hand over to union officials for the various activities identified by the RC, itemised it as a business expense, and not told the firm’s accountant(s). This cash withdrawal might then be lost in the system as an operating activity and recorded anonymously in the cash outflows. Accountants are supposed to be able to track events which would impact the entity’s cash position. It might be argued that good accountants would find the cash withdrawal and require an explanation. The owners/investors or managers involved would probably then expect the accountant(s) to cooperate and ignore the transaction. The social contract for accountants in the cash withdrawal process is that accountants are expected not to find irregular cash withdrawals or, if they do, to cooperate and not to query the reasons for the cash withdrawal. This suggests accounting as a subjective process.

Payment of wages and salaries would involve managers, human resources, and the unions. Accountants would not usually be involved in negotiating employee compensation and benefits. This activity would be led by human resources staff. Wages are typically grouped as an expense in the IS. Other employee benefit matters such as superannuation, workers compensation, annual leave, and redundancy payments would typically be handled by human resources. In the case of the construction industry, employee compensation and benefits was a major area of inappropriate behaviour. However, the negotiations would have involved management and human resources. It is unlikely that accountants would have been involved. The only involvement would have been recording the outcomes of negotiations as an increase or decrease on the IS, under the broad expense category of wages. The social contract for accountants in the wages
and salaries process is that accountants are expected to be excluded from negotiations with unions or staff and to record the outcomes on the IS without query. Given accountants would not normally be part of this process, other than recording business transactions on the IS, this suggests accounting as an objective process. Accountants would have been involved in considering FBT implications of certain benefits to employees especially managers.

Earning of fees revenue involves management, project managers, and accountants. Earning of fees revenues describes the way the entity reports its revenues. This falls under the accounting activity called earnings management. Earnings management is the managers’ use of accounting discretion via accounting policy choices, that is which standard to follow and how this is interpreted, and/or estimated to report a desired level of earnings (Birt et al. 2010, p. 206). Earnings management is an area where accounting can become very subjective. Revenues are a critical part of profitability. Managers may be motivated to report the entity’s profitability in terms of economic reality, that is, the truth. However, they may also be motivated by self-interest, perhaps to help persuade the banks to provide additional loans, or to maintain share price, or to maximise performance bonuses (Birt et al. 2010, p. 206).

As outlined in chapter 3, the construction industry is characterised by intense competition and small profit margins. As a result, managers are often under pressure to report good news in financial statements, rather than bad news. This satisfies owners/investors, as well as the banks, and suppliers. The nature of construction projects means that revenues are usually split over many months, and sometimes years. Revenues fluctuate on each project, based on the percentage of completion, and this presents an opportunity to manipulate revenues to help management report good news. For example, if the entity has less than expected revenue next month, management might hold some of
this month’s revenue and carry it over to the next month. This is an example of earnings management. It improves the quality of earnings (Birt et al. 2010, p. 206) by spreading the earnings over a period of time. In the construction industry, if the project is completed within one financial year, the monthly fluctuations do not really matter, but if the project runs over more than one year, it can affect the results in each financial year. In this activity, management can manipulate the revenue, and therefore the profit result, presented in the IS. The social contract for accountants in the earnings management process is that accountants are expected to cooperate and not to query the reasons for revenue manipulation. This suggests accounting as a subjective process.

Furthermore, costs can be deferred to the BS as work in progress (WIP) to later match with like revenue for work completed. WIP is also open to manipulation by transferring costs to the BS rather than expensing them is another way to manage earnings. Expenses are lowered, profits increased and assets increased on the BS.

Payment of tax involves owners/investors, management and accountants. Taxation is an expense of a company, because it has an obligation to pay tax on business activities. The process of paying tax involves taxation rules and accounting rules. The tax that should be paid is based on the company’s taxable income as calculated by applying taxation rules. As an expense, tax can be a significant expense for a company and subsequently has a strong influence on profitability. Profit performance measures can be referred to as pre and post-tax basis. In contrast to taxation, where taxation rules must be applied, profit reported in the IS is measured by applying accounting rules, that is, accounting standards. The difference between taxation rules and accounting rules is explained by the fact that the tax expense of a company will not be simply the pre-tax accounting profit multiplied by the applicable tax rate. Accountants are placed under pressure by owners/investors and management to minimise the tax expense, so that the post-tax
profit increases. This is called tax avoidance. Taxation and accounting rules can diverge due to income not being assessable for taxation purpose, and expenses not being deductible for taxation purposes. The social contract for accountants in the taxation process is that accountants are expected to minimise the tax expense. This suggests accounting as a subjective process.

Step two, of the accounting process, is measuring business transactions. As outlined above, this step involves accountants identifying how business transactions will affect the entity’s position, and groups together similar items, such as expenses and income. Figure 7.2 identified these as analysis, recording, and classifying. In reconstructing accountants’ social contract with stakeholders here, there is a need to identify who was involved and what they expected.

The measurement of business transactions mainly involves accountants working on their own. In most cases, other stakeholders would probably defer to the accountants’ professional judgment in this area and leave them alone. For the purposes of this study, this step is somewhat “murky” in the sense that it is impossible to reconstruct the social reality of what accountants did on a day-to-day basis in analysing, recording and classifying business transactions. Perhaps the only way to discover this truth would be to examine audit reports, but these would be inaccessible. All that can be done is to infer that step two is where creative accounting would most likely have occurred. In this sense, accountants would have adopted creative ways of analysing, recording, and classifying business transactions under pressure from owners/investors or management to achieve other outcomes, tax evasion for example. The social reconstruction of step two is that accountants would probably have conducted these activities based on their own professional experience and judgment, but probably had the outcomes expected by owners/investors or management in the back of the mind while carrying out these tasks.
The social contract for accountants in the measurement of business transactions process is that accountants are expected to follow accounting rules but to employ creative accounting, wherever possible, to meet outcomes specified by owners/investors or management. This suggests accounting as a subjective process.

Step three, of the accounting process, is communicating via reporting. As outlined above, this step involves accountants identifying events that will have an impact on the financial performance of the entity. Figure 7.2 identified these as IS’s, BS’s, and CFS’s. In reconstructing accountants’ social contract with stakeholders here, there is a need to identify who was involved and what they expected.

IS’s, BS’s, and CFS’s all involve owners/investors, managers and accountants. They may also involve regulators and auditors. The IS reflects the accounting return for the entity for a specified time period, and includes income and expenses, to calculate profit. IS’s are important because they measure profitability and, in doing so, they allow evaluation of the entity’s performance; more specifically reviewing past decisions, future growth, and enable future decisions. Large companies are subject to statutory reporting requirements and are required to prepare an IS at least every 12 months. The BS details the entity’s assets, liabilities, and equity at a particular point in time. BS’s are important because they represent the financial position of an entity at a particular time. For this reason, suppliers and banks, as well as employees may be interested in the BS. CFS’s measure liquidity, which is important to paying bills or debts on time and maintaining business confidence. Cash flow explain whether the entity has enough cash to meet its financial obligations such as paying wages, taxes, and other bills as they are due. For this reason, suppliers and banks, as well as regulators such as the ATO, are also interested in CFS’s.
Accountants follow accounting rules, that is accounting standards, in preparing ISs, BS’s, and CFS’s. While the analysis above showed that a wide range of stakeholders are interested in these financial reports, in most cases they would not try to influence accountants in the preparation of these reports. The socio-political power inequities amongst stakeholders emerge in step one and step two of the accounting process and only affect step three in the sense of being inputs into the information portrayed in step three’s financial reports. The social contract for accountants in the communicating for reporting process, is that accountants are expected to follow accounting rules. Deviation from this expectation would be picked up by auditors. This suggests accounting as an objective process.

Step four, of the accounting process, is decision making. As outlined above, this step involves accountants providing information that users can employ to make strategic decisions about the business. Figure 7.2 identified these as investment, product or service range, and pay debts. In reconstructing accountants’ social contract with stakeholders here, there is a need to identify who was involved and what they expected.

Accountants play an important role here in anticipating the type of financial information that is relevant and useful for a wide range of users. Financial analysis helps users evaluate the entity’s performance and future financial health. It helps guide owners and investors, both current and prospective, regarding decisions about investing funds into the business or withdrawing funds. Regulators such as the ASIC protect the public interest by ensuring investors receive accurate information. Accountants would feel under pressure to produce truthful financial information for investors. Owners/investors and management may use financial information about which markets to compete in, and which products and services to offer. These decisions will have a significant impact on the entity’s competitiveness and, therefore, its profitability. Accountants would feel
under pressure to provide accurate information for owners or investors and management. Suppliers and banks will want to know if the entity can pay for their services before trading with the entity. However, here a conflict emerges in the construction industry’s socio-political power inequities. Owners or investors and managers may not wish to fully disclose financial information to suppliers or banks, particularly if it faces a difficult financial period, cash flow problems for example, and needs material and capital to continue operating. Under these circumstances, accountants would have been under pressure to adjust financial information for certain external users. The social contract for accountants in the decision making process is that accountants are expected to follow accounting rules. Deviation from this expectation would be picked up by auditors and regulators. This suggests accounting as an objective process. However, this may have been different in providing information regarding debt repayment.

The following figure updates the accounting process with social contracts summarised.
The figure highlights areas where accountants employed in the construction industry may have been under pressure to act in ways that did not always follow accounting rules, that is, accounting standards.

7.3 Regulatory Outcomes

7.3.1 The Regulators

This study’s findings present an opportunity for regulators of the construction industry to take action to address the industry’s unlawful behaviour. While the seven unlawful activities were identified by the RC more than a decade ago, there is evidence that the construction industry continues to misbehave. The Royal Commission into Trade Union Governance and Corruption (Heydon 2015b), completed by The Honourable John Dyson Heydon AC QC, confirmed lawlessness in the construction industry as an ongoing problem more than a decade after the RC. Heydon found evidence of unlawful or unprofessional conduct by the trade union movement (2015b p. 49).

This study provides regulators with information about the social practice of accounting which might be used to improve regulation of the industry. This could be done by empowering accountants to act as internal regulators. Given that much of the industry’s unlawful behaviour occurs due to poor or inappropriate financial management, improved accounting practice in the industry could help restore public confidence and repair legitimation.

Policy improvements could be led by the lead regulator within each unlawful activity. For tax evasion, this is the ATO. The ATO could work with accounting bodies and accountants to empower them to regulate tax evasion and payroll tax activities. The aim is to identify who is the lead regulator, and then look at their website, and research their
TOR and role, and perhaps identify how they could give accountants the authority and protection to be internal regulators. One of the areas needs to be the FWO to provide accountants income protection and ensure unfair dismissal laws are very rigid in the construction industry, otherwise there will be no whistle blowers. Perhaps, also anonymity or confidentiality in giving testimony, for example, hidden screens in court rooms.

The lead regulator for each of the seven unlawful activities identified by the RC is as follows:

- For payroll tax, the lead regulator is the Australian State and Territory Revenue Offices.
- For employee entitlements, the lead regulator is the Fair Work Commission (FWC) and the FWO.
- For inappropriate payments, the lead regulator is Australian Industrial Relations Commission (AIRC).
- For security of payments, the lead regulator is the *Building and Construction Industry Security of Payment Act 1999* (BCISP Act 1999) in all States and Territories, apart from Western Australia and the Northern Territory, where regulation is by the *Construction Contracts Act 2004* (CC Act 2004) and is administered by various bodies in each State and Territory, for example, the Office of Fair Trading in NSW.
- For phoenix company activities, the lead regulator is the ASIC.
- For profit manipulation, the lead regulator is ASIC.
- For tax evasion, the lead regulator is the ATO.
Each of the seven activities identified by the RC is now examined in terms of the current regulation of the construction industry, areas for improvement, and the role accountants could play.

7.3.1.1 Payroll tax

Payroll Tax Australia permits employers to self-register and self-assess payroll tax. In Australia, payroll taxes are paid to the State or Territory governments via the revenue collection offices. Each State or Territory has different payroll tax rates and general deduction thresholds. Payroll tax is a percentage of a business’s wages and salaries that exceed the threshold amount annually. Consequently, payroll tax is an employment on-cost associated with large employers. “Most building and construction businesses are small employers and are below the payroll tax threshold” (Cole 2003, vol. 8, para. 8, p. 95).

In 2003 the RC found “that there is significant non-registration and underpayment of payroll tax in the building and construction industry, particularly in New South Wales” (Cole 2003, vol.8, p. 105). Apart from the reduction in revenue collection by the states, the findings had implications for the financial performance of a business. “Evasion of payroll tax disadvantages businesses which comply with their statutory obligations. Some contractors avoid the payment of their statutory obligations so that they can quote for work at lower rates” (Cole 2003, vol. 8, p. 93).

Payroll tax is predominantly avoided in one of two ways. The first method to avoid payroll tax is via sham contracting arrangements whereby employees are treated as “contractors” and “some union witnesses stated that there is significant avoidance of payroll tax flowing from the illegitimate use of contracting” (Cole 2003, vol. 8, p. 103). The second method of avoiding payroll tax was through the use of phoenix companies;
and “significant numbers of companies in the building and construction industry, particularly phoenix operations, do not pay or underpay payroll tax” (Cole 2003, vol. 8, p. 105). These two mechanisms are covered in other unlawful activities that follow. In light of this, the RC made three recommendations in relation to non-compliance with payroll tax obligations in the building and construction industry. These recommendations were Recommendation 101, Recommendation 102 and Recommendation 103. It appears that only the last two recommendations have been adopted and considerable time after the RC.

Recommendation 101 proposed that the “Commonwealth encourage the States and Territories to consider the adoption of the provisions contained in s. 16LA of the Pay-Roll Tax Act 1971 (NSW) (PRT Act 1971) to address phoenix company activities in the building and construction industry” (Cole 2003, vol. 8, p. 106). Adoption of the provisions would have made “all members of a group jointly liable for the payroll tax debts of other group members” (Cole 2003, vol. 8, p. 106). However, at the time the Government did not consider the changes as necessary because “it in effect imposes liability on related parties and therefore implies a significant change to current corporate law and insolvency law policy” (Australian Government 2003, p. 89). According to Anderson (2012, p. 3), “this recommendation was not adopted”.

Recommendation 102 advocated that the “Commonwealth discuss with the States and Territories appropriate methods of permitting their revenue authorities to share information relevant to the detection of payroll tax evasion in the building and construction industry where this does not already occur” (Cole 2003, vol. 8, p. 106). This recommendation was adopted. The OSR in NSW stated:

We regularly exchange information with the ATO in accordance with the Memorandum of Understanding signed by the ATO and all state revenue offices.
Our shared use of information and data includes using Business Activity Statement (BAS) data to identify those businesses which should be registered for payroll tax and matching business wages, salaries data, and fringe benefits tax data from the ATO to identify variances for payroll tax…(2015a, p.2)

Recommendation 103 suggested the “Commonwealth encourage the States and Territories to continue efforts to harmonise between jurisdictions the key definitions of the payroll tax system, particularly the definition of wages” (Cole 2003, vol. 8, p. 107). This last recommendation has been adopted: “although each jurisdiction continues to have different payroll tax rates and general deduction thresholds, the payroll tax legislation is virtually identical due to the harmonisation of payroll tax legislation in July 2010” (OSR NSW 2015b).

Non-compliance with payroll tax obligations continues to be an ongoing issue in the building and construction industry in many states of Australia. In June 2013, the Queensland OSR examined payroll tax compliance in the construction industry, by focussing on employers in the industry who were attempting to avoid paying payroll tax (FWBC 2013). The OSR NSW (2015a, p. 6) payroll tax compliance program in 2015-2016 is targeting non-complying employers in various industries, including construction. During 2015-16, the Western Australia revenue collection office payroll tax compliance program will be concentrating on a number of industries, particularly the construction industry (Department of Finance WA 2015).

7.3.1.2 Employee Entitlements

The minimum employee entitlements are defined in the National Employee Standards, which are set out in the FW Act 2009 (FWO 2015). The practical application of the FW Act 2009 in workplaces is overseen by the FWC and the FWO. The Fair Work System is a national system that provides a safety net of minimum employee entitlements.
The payment of employee entitlements is dependent upon a company having adequate cash reserves (Deegan 2012, p. 429). Employees in the building and construction industry are particularly vulnerable to non-payment of employee entitlements (Cole 2003, vol. 9, p. 290). The non-payment of employee entitlements is often the result either insolvency or phoenix activity. “There are high levels of business insolvency in the building and construction industry particularly among small employers, whose businesses collapse financially and whose workers remain unpaid” (Cole 2003, vol. 9, p. 290). Some insolvency is deliberate and is the planned outcome of phoenix activity whereby “operators are serial offenders who use deliberate and fraudulent methods to avoid obligations” (Cole 2003, vol. 8, p. 119). According to the FWO’s commissioned report on phoenix activity, prepared by PwC in 2012 (p. iii, Table 1) the cost to employees, in lost employee entitlements, due to phoenixing activity was estimated to be between $191,253,476 and $655,202,019 in 2009/10.

The RC made several recommendations regarding employee entitlements (Cole 2003, vol. 9, pp. 338-342). Recommendations 154 to 165 were primarily centred on the Commonwealth and states providing a service for the recovery of unpaid entitlements, adopting a greater role in the enforcement of employee entitlements, and provide advice and where appropriate representation for all employees for claims of unpaid entitlements in the building and construction industry (Cole 2003, vol. 9, pp. 338-342). At the time, most of these recommendations were considered or accepted by the Government (Australian Government 2003, pp. 97-98).

However, the Government focused on the recovery of unpaid entitlements rather than on the enforcement of employee entitlements. Consequently taxpayer government funded schemes, such as the EESS and the GEERS arose to compensate employees who had not been paid their employee entitlements. “However, much of the employee entitlements
paid by GEERS are not subsequently recovered from the insolvent employer” (Anderson 2011, p. 150).

Whilst GEERS provided a recovery mechanism for employees who had not been paid their entitlements due to insolvency by their employer, not all losses were recoverable due to the annual maximum wage limit cap, and certain “workers” were not covered by the scheme (Anderson 2011, p. 150). The major limitation of GEERS was that there was no legislative basis for the scheme; “the scheme is also not established by statute, but is rather a decision of executive government, which can be withdrawn at any time” (Anderson 2011, p. 150).

The Fair Entitlements Guarantee scheme that commenced on 5 December 2012 replaced the GEERS. It establishes a legislative basis, through enactment of the *Fair Entitlements Guarantee Act 2012* (C’wth), for the recovery of certain unpaid entitlements owed to employees due to the insolvency of their employer (Department of Employment 2015). If employees have lost their job and believe they are owed outstanding employee entitlements, but their employer is not in liquidation or bankrupt, then they can seek further information from the FWO, ASIC, or from the insolvency practitioner looking after the business affairs of their former employer (Department of Employment 2015). If the employer is still operating a business, the FWO may be able to provide information about the employer’s obligations to meet unpaid employee entitlements (Department of Employment 2015). Employees who are owed employee entitlements by abandoned companies can submit a request to ASIC to wind up the company (Department of Employment 2015).

The role of accountants and other professional advisors must be examined in relation to the non-payment of employee entitlements. Anderson and Haller (2014) question:
whether the FWO ought to be seeking monetary penalties from the company’s other accessory — in other words, the advisor who recommended to the director, acting as the directing mind and will of the company, that they liquidate the company and move the business elsewhere as a means of avoiding payment of liabilities (p. 473).

In considering the role and responsibility of advisors, Anderson and Haller (2014) state:

Where a legal or insolvency practitioner advises a company director to phoenix their company as a means of the company avoiding payment of employee entitlements, the advisor is linked in purpose and thus an accessory to that company’s breach of the Act in the same way ......(p. 489).

Anderson and Haller (2014) conclude:

In relation to employee entitlements lost as a result of phoenix activity, the FWO can play a significant role in the deterrence of this behaviour. While the FWO should be given credit for routinely bringing actions against directors as accessories to their company’s breaches of the *Fair Work Act*, they have not gone further to seek a penalty against the advisors who might be behind the decision to phoenix the offending company (p. 497).

7.3.1.3 Inappropriate payments

Inappropriate payments, typically in the form of “donations”, are regulated by the Industrial Registrar, which is part of the AIRC, and the ABCC. The BCII Act 2005 requires registered organisations to lodge a statement with the Industrial Registrar of donations exceeding $500 received by the organisation and clients, head contractors and subcontractors to notify the ABCC of any request or demand for a donation exceeding $500 be made to a registered organisation. Subsequently, the BCII Act 2005 was superseded by the *Fair Work (Building Industry) Act 2012* (FWBI Act 2012). Consequently, the ABCC was replaced with FWBC. The Wilcox Report 2009 recommended the structure and power of FWBC, which were considerable less under the FWBI Act 2012.
The RC made a number of recommendations in response to inappropriate payments identified in the building and construction industry. These were specifically stated in recommendation 145, recommendation 147 and recommendation 149 of the RC, Volume 1, Summary of Findings and Recommendations. In recommendation 145 (Cole 2003, vol. 1):

The Building and Construction Industry Improvement Act require registered organisations, as soon as practicable after the end of each financial year, to lodge with the Industrial Registrar a statement showing the following particulars in relation to each donation exceeding $500 received by the organisation during that financial year:
(a) the amount of the donation;
(b) the purpose for which the donation was made; and
(c) the name and address of the person who made the donation (p. 132).

In recommendation 147 (Cole 2003, vol. 1):

The Building and Construction Industry Improvement Act require clients, head contractors and subcontractors to notify promptly the Australian Building and Construction Commission of any request or demand that a donation exceeding $500 be made to, or at the direction of, a registered organisation or an official, employee, delegate or member of a registered organization (p. 133).

In recommendation 149 (Cole 2003, vol. 1):

The maximum penalty for non-compliance with the following obligations in the Building and Construction Industry Improvement Act be set at $100 000 for a body corporate and $20 000 in other cases:
(a) failure by an employer to notify the Australian Building and Construction Commission of any demand or claim for payment to an employee in relation to a period during which the employee engaged or engages in industrial action, within 24 hours of receiving that demand or claim;
(b) failure by a registered organisation to include all donations exceeding $500 received by the organisation in a statement lodged with the Industrial Registrar and the Australian Building and Construction Commission as soon as practicable after the end of each financial year; and
(c) failure by a client, head contractor or subcontractor to notify the Australian Building and Construction Commission of any request or demand that a donation
exceeding $500 be made to, or at the direction of, a registered organisation or an official, employee, delegate or member of a registered organization (p. 133).

However, inappropriate payments continue to be an issue in the building and construction industry. There is evidence of this in the report by Heydon (2015b). Heydon (2015b) had “uncovered and examined a wide range of corrupt or inappropriate conduct on the part of some union officials across a range of unions...(including for example): a former lead organiser for the (union name) conceded during hearings in Canberra that he had personally received $100,000 in secret payments from employers” (p. 25).

A recent example of inappropriate payments is in a submission prepared by the CFMEU in 2014, whereby it was revealed that:

In October 2013, reports emerged of an Australian Federal Police investigation into allegations of multi-million dollar ‘consultancy fees’ paid by Leighton Holdings to a UAE businessman in return for securing lucrative Iraqi government construction projects (CFMEU 2014, p2, para 1.7).

This story was further corroborated by a number of newspaper articles, one of which, for example claimed:

Damning evidence has emerged in a court case linking construction firm Leighton Holdings to allegedly corrupt payments of ‘not less than $25 million in marketing fees’ to a Monaco firm to help win Iraq government projects, even though the projects required no marketing (McKenzie & Baker 2013, para. 1).

The problem of inappropriate payments in the building and construction industry remains an issue over a decade after the RC. The Royal Commission into Trade Unions, which commenced in 2014, acknowledges that the “giving and taking of such benefits is not a new phenomenon” (p. 94, clause 315). However, this raises the question as to why inappropriate payments are an ongoing issue in the building and construction industry. Reasons as to why inappropriate payments are an ongoing issue in the building and
construction industry are that existing laws and regulatory bodies have been ineffective at curbing inappropriate payments. Inappropriate payments are symptomatic of the lawless culture of the building and construction industry by being “antithetical to the rule of law” (Heydon 2015a, p. 94).

Heydon (2015a, p. 98) believes, in addition to disclosure requirements, the introduction of specific legislation, prohibiting the making or receiving of inappropriate payments, with significant penalties may address the issue of corrupting benefits. If found to be in breach of the law, an individual could be imprisoned for ten years or fined up to $1.7 million and a corporation could be fined up to $17 million (Heydon 2015a, p. 98).

However, it is questionable whether additional laws and significant penalties would eliminate corrupting benefits, given that inappropriate payments have continued for well over a decade since the RC. The root cause of such behaviour appears to be cultural. Clearly, the cultural change recommended by the RC has not yet occurred in the industry to induce compliance with the law regarding inappropriate payments. After all, the building and construction industry lacks a “culture of legality” (Zimmermann 2007, p. 11). Unless there is cultural change, the law alone will not be able to change this behaviour.

7.3.1.4 Security of Payments

The entitlement of subcontractors to receive payment due for work performed is regulated by the Building and Construction Security of Payment Acts in all states and territories, apart from Western Australia and the Northern Territory, where regulation is by the CC Acts 2004. Consequently there are two security of payment legislative models operating in Australia, referred to as the ‘East Coast’ and ‘West Coast’ Models (Coggins, Fenwick & Bell 2010). The two security of payment legislative models that
operate in Australia indicate an inconsistent approach to the regulation of security of payments in Australia. Security of payments legislation varies between the states and territories with the earliest enactment in New South Wales in 1999 and the latest in South Australia, Tasmania and the Australian Capital Territory in 2009. The Acts are administered by various bodies in each of these states and territories, ranging from the Office of Fair Trading in NSW, the building commissions in Queensland, Victoria and Western Australia, to Land and Planning Authorities in the Northern and Australian Capital Territories.


Reforms, considered by the RC, to the payment of subcontractors in the building and construction industry were on opposite ends of the continuum. The first approach concentrated on “the financial performance of businesses in the industry, in order to reduce the risk of financial problems that lead to the failure to pay subcontractors” (Cole 2003, vol. 8, p. 245) and considered strategies such as prequalification guidelines and licensing conditions. The second approach focused on “schemes to improve the mechanisms that assist subcontractors in recovering payments that are owed to them, or
to provide some protection against the insolvency of parties higher up the contractual chain” (Cole 2003, vol. 8, p. 245).

The draft Building and Construction Industry Security of Payments Bill 2003, to reform security payments, recommended national legislation focused on rapid adjudication in line with the second approach focusing on mechanisms to recover payments due to subcontractors. Other mechanisms to improve payment, in particular trust funds, which were strongly opposed by industry, were not the focus of the Bill. “The Commission has therefore chosen to focus upon reform recommendations to improve security of payment that have better prospects of being accepted and implemented” (Cole 2003, vol. 8, p. 250). The draft Building and Construction Industry Security of Payments Bill 2003 has not become Commonwealth law.

In the years following the RC, ‘Nothing has changed’ (Collins 2012, p. 12), in relation to security of payment, particularly in New South Wales. Whilst security of payment problems can be the result of many factors, “security of payment problems can result from builders… that become insolvent” (Cole 2003, vol. 8, p. 231). In 2011/12, the construction industry accounted for 22.1 percent of insolvencies in all industries while “one in every two insolvency events occurs in NSW’ (Collins 2012, p. 50). Due to this increase in the number of insolvencies in NSW, the NSW Government commissioned an investigation which produced the following report: The New South Wales Government’s Independent Inquiry into Construction Industry Insolvency in 2012 found that:

The Inquiry has absolutely no reason to think that the detailed examination of the problem conducted by the Cole Royal Commission does not continue to accurately describe the situation at present. The Inquiry has every reason for thinking, on the basis of credible evidence given to it that the position revealed by the Royal Commission investigators and summarised by the Royal
Commissioner in the above quoted passage [on security of payment] is an accurate representation of the present position (p. 13).

Subsequent to the Collins Inquiry into Insolvency in the NSW Construction Industry, which considered payment practices affecting subcontractors, the Building and Construction Industry Security of Payment Amendment Bill 2013 was introduced in New South Wales, and commenced from 21 April 2014. The Amendment Bill 2013 was introduced to amend the BCISP Act 1999 for changes to improve payment claims procedures as well as to shorten periods for progress payments. The purpose of the bill, as explained by the second reading of the Bill in Parliament, “is to introduce reforms that will provide greater protection for subcontractors and promote cash flow and transparency in the contracting chain” (Building and Construction Industry Security of Payment Amendment Bill 2013, p. 1).

The application of the East Coast model is further fragmented with these and other recent changes to security of payment legislation by individual states. This creates discrepancies in terms of how security of payment is regulated and administered between states and territories within Australia. Given that all states and territories have the common objective of facilitating cash flow within the construction contractual chain, there have been calls for harmonisation of the security of payment legislation (Coggins, Fenwick, & Bell, 2010). As stated by Coggins et al. (2010):

Few in the industry would seriously advocate that the present, disjointed situation ought to continue; rather, there have been increasing calls – echoing those of the Cole Royal Commission (Cole 2003) nearly a decade ago – to forge a uniform national approach to security of payment regulation (p. 20).

In recent years, during 2014-2015, many of the states (NSW, Qld, SA and WA) have announced or commenced reviews of their security of payments legislation with some of the states adopting strategies or schemes previously recommended in the RC in 2003.
For example, NSW Fair Trading announced in December 2014 and made effective from May 2015, a retention trust scheme established for projects valued at $20 million or more to protect subcontractors’ retention money if a head contractor becomes insolvent (Fair Trading 2015). The Queensland Building and Construction Commission (QBCC) has implemented, effective from October 2015, a Minimum Financial Requirements Policy as a condition of licensing to “minimise the incidence of financial failure in the building industry” (2015, p. 4).

The Queensland [licensing] model presents the only solution to the problem of preventing insolvency in the first place. The construction trust is important because it operates in a remedial manner after insolvency has begun to cause its problems, yet the best defence to the ills, ailments and undesirable consequences which gave rise to the establishment of this Inquiry [on insolvency], must be the Queensland model. (Collins, 2012, p. 4).

The inclusion of financial criteria as a condition of licensing is a preventive measure and reduces the risk of financial problems arising that are associated with cashflow and insolvency, whereas, the adoption of trust funds is a remedial measure and offers mechanisms to recover money owed to a subcontractor when a head contractor becomes insolvent. Both measures rely on the involvement of accounting to succeed. The role of accounting in these strategies and schemes comes into play with reporting and auditing requirements. The NSW retention trust scheme imposes, on head contractors, record keeping, reporting requirements and annual auditing of trust accounts (Fair Trading 2015). The Minimum Financial Requirements Policy in Queensland requires reports to “be prepared by an Accepted Independent Accountant” (QBCC 2015, p. 16) with the statements “prepared with all of the recognition and measurement standards of the Australian Accounting and Auditing Standards applied (irrespective of the Company’s adopted Accounting Standards)” (QBCC 2015, p. 33). It is important to note that the financial statements must be prepared in accordance with Accounting Standards
irrespective of the Accounting standards adopted by the company. The QBCC has issued a stern warning to accountants to ensure the information provided to the Commission is not false or misleading or face a maximum penalty of two years imprisonment (2015, pp. 16-17).

7.3.1.5 Phoenix Companies

The Federal Treasury issued a report in 2009 (sect 1.1, p.1) which defines phoenix activity as “the evasion of tax and other liabilities such as employee entitlements through the deliberate, systematic and sometimes cyclic liquidation of related corporate trading entities”. Anderson and Haller (2014) explain fraudulent phoenix activity can take two forms:

The first is through successor companies. One company, Oldco, becomes insolvent and a new company, Newco, is incorporated to take over the business of its failed predecessor. Second, phoenixing can occur within corporate groups, where Newco is an existing company within the group, and it takes over the business of Oldco, which is an insolvent related company. Treasury’s 2009 Phoenix Proposals Paper called these ‘basic’ and ‘sophisticated’ phoenix activity respectively. In both cases, the aim is to quarantine Oldco’s debts or legal obligations, which are unenforceable against Newco or its owners. Both Oldco and Newco will have directors, and both companies can employ lawyers and accountants who advise on and carry out the necessary transactions (p.474).

In the case of phoenix companies the primary regulator is ASIC. However, since “phoenix activity involves the avoidance of taxes, employee entitlements and other debts, there are three primary agencies that can detect and act on suspected phoenix activity, the ATO, ASIC and FWO” (PwC 2012, p. 34). Although, it is ASIC who can order the wind up a company if it believes the order is in the public interest under Part 5.4C of the Corporations Act 2001, this was introduced by the Phoenixing Act 2012, which was an act to amend the Corporations Act 2001.
The RC made a number of recommendations in relation to phoenix companies. The “recommendations in this area seek to strengthen government actions to detect and eliminate fraudulent phoenix company activity” (Cole 2003, vol. 8, p. 162). These recommendations range from recommendation 104 to recommendation 109 (Cole 2003, vol. 8, pp. 164-166). Four out of six recommendations were implemented. The recommendations that were implemented formalised the relationship between agencies, amended relevant legislation to permit the exchange of information between relevant agencies, commenced a program to identify persons disqualified from managing a company, and amended the Corporations Act 2001 for maximum disqualification periods of persons from managing corporations for insolvency and non-payment of debts. (PwC 2012, pp. 31-32).

Almost a decade after the RC in 2003, the Phoenix Activity Report requested by the FWO found “Feedback from stakeholders indicated that phoenix activity remains a significant problem in the building and construction industry” (2012, p. 17). According to FWO’s commissioned report on phoenix activity, prepared by PwC in 2012 (p. iii) the total impact of phoenixing activity, on employees, businesses and government revenue, was estimated to be between $1,784,338,743 to $3,191,142,300 for 2009/10.

Consequently, a Senate inquiry into insolvency in the construction industry commenced on 4 December 2014. The report prepared by the Economics References Committee was titled ‘I just Want to Be Paid: Insolvency in the Australian construction industry’, and was issued in December 2015 (Australian Parliament House 2015). The TOR of the inquiry were to examine the scale, incidences, causes and effects, and impacts of insolvency in the construction industry. The TOR were also examining whether the current law and regulatory framework is adequate to reduce the level of insolvency in the construction industry. The TOR of the Senate also examined the incidence of
Phoenix companies in the construction industry, aimed at curbing the practice of phoenixing (Australian Parliament House 2015).

Given that most insolvency practitioners have an accountancy background and insolvency is the result of poor financial record keeping, it is startling that there are no submissions to the Senate inquiry from either the Insolvency Practitioners Association, now known as Australian Restructuring Insolvency and Turnaround Association (ARITA), or any of the three professional accounting bodies; the Institute of Public Accountants (IPA), CPA Australia (CPA) and the Institute of Chartered Accountants in Australia (ICAA). There may be a range of reasons for no submissions from ARITA, IPA, CPA, ICAA, and it would be too simplistic to assume they were not interested in phoenixing activity.


It’s important to note that almost all cases of illegal phoenix activity occur in the SME sector. Perpetrators who engage in this activity have a distinct commercial advantage over competitors that operate lawfully. With less or no debt, they’re then in a position to ‘undercut’ their competitors by offering goods or services at lower prices (ASIC 2015, p. 7).

Anderson and Haller (2014, p. 474) claim accountants “advise on and carry out the necessary transactions” in phoenixing companies. Anderson and Haller (2014) argue in relation to phoenixing companies:

Could the directors devise and implement these illicit transactions without the help of their legal, insolvency or accounting advisors? This is not to suggest that all, or even most, corporate rescues are fraudulent or that the advice behind them is improper. But it must be conceded that undoubtedly some are (p.472).
It appears the role of accounting in phoenix activity is one of an accessory or accomplice. In order to deter phoenix activity, advisors needs to be held responsible for their involvement. Anderson and Haller (2014) contemplate:

whether the more frequent imposition of liability on the advisor as an accessory to the directors' breach of duty is needed to educate and deter other advisors from becoming involved in the creation of these arrangements that cause such harm to the economy (p.472).

7.3.1.6 Profit Manipulation

Profit manipulation is regulated by the ASIC under the Corporations Act 2001. The Corporations Act 2001 governs reporting and other corporate governance matters under Chapter 2M--Financial reports and audit. Section 286 states:

1) A company, registered scheme or disclosing entity must keep written financial records that:
   (a) correctly record and explain its transactions and financial position and performance; and
   (b) would enable true and fair financial statements to be prepared and audited.

In particular, section 296 states that the financial report “must comply with the accounting standards” and “any further requirements in the regulations” (Corporation Act 2001). Furthermore, section 297(a) states “the financial statements and notes for a financial year must give a true and fair view of the financial position and performance of the company, registered scheme or disclosing entity”. However, under section 292 (1) only disclosing entities, public companies, large proprietary companies and registered schemes are required to prepare a financial report and a directors’ report (Corporation Act 2001). Under section 292 (2) of the Corporations Act 2001, small proprietary companies are only required to prepare the reports if directed to do so by shareholders/members or ASIC, as stated below:
A small proprietary company has to prepare the financial report and directors’ report only if:
(a) it is directed to do so under section 293 or 294; or
(b) it was controlled by a foreign company for all or part of the year and it is not consolidated for that period in financial statements for that year lodged with ASIC by:
   (i) a registered foreign company; or
   (ii) a company, registered scheme or disclosing entity.
The rest of this Part does not apply to any other small proprietary company.

Small companies limited by guarantee

(3) Despite subsection (1), a small company limited by guarantee has to prepare the financial report and directors’ report only if it is directed to do so under section 294A or 294B.

Profit manipulation still exists in the construction industry. A recent example of profit manipulation is in a submission prepared by the CFMEU in 2014. The CFMEU submission was part of a union campaign against the need for a specialist regulator for the construction industry. The CFMEU explained that “the principle that the industry required industry specific regulation was first promoted by Justice Cole in his report of the Royal Commission into the Building and Construction Industry” (CFMEU 2014, p. 52, para. 5.5). The CFMEU blamed the RCR for what they felt was unfair government intervention in the construction industry. They disagreed with the RCR’s view that the industry was different to others and, therefore, deserved special attention from the government. The CFMEU stated that there were “insufficient grounds for treating the industry as unique” (CFMEU 2014, p. 56, para. 5.6). The main reason for the CFMEU’s objection to industry regulation was concern about the “suggestion by the Prime Minister and other ministers, that the ABCC can address criminality in the construction industry…the ABCC does not have any powers to deal with criminal activity” (CFMEU 2014, p. 58, para. 5.12). The CFMEU, therefore, was worried about the focus on criminal activity. It tried to show that its concern was for construction companies by revealing the impact of investigations on share prices:
In late 2012 there was extensive media coverage of a significant misreporting of profits and losses on two major AbiGroup Ltd projects, the D2G project in Queensland and the Peninsula Link Project in Melbourne. This misreporting came to light shortly after an audit of the company’s operations and resulted in intervention and ‘internal review’ by the parent company Lend Lease. Several Abigroup executives were stood aside. There was an immediate drop in the company’s share price and a number of other reports suggested that there might be broader compliance and corporate governance issues within the corporate group. (CFMEU 2014, p. 2, para. 1.8)

This story was further corroborated by a newspaper article which claimed:

Lend Lease management has seized control of Abigroup and has been forced to launch an internal investigation and call in its auditors to examine irregularities in the financial reporting relating to more than $1.5 billion of projects (Carter 2012, para. 1).

In the article, two of four executives suspended during the internal investigation, were identified as holding the senior financial accounting role of chief financial officer (Carter 2012):

The company did not name the executives, but they are…the managing director of Lend Lease's Australian construction business, … the chief financial officer of Lend Lease's infrastructure business, …, Abigroup's managing director, and …, Abigroup's chief financial officer (p.1)

The empirical findings of a recent US study suggest “that CFO’s are likely to become involved in material accounting manipulations because they succumb to CEO pressure, rather than because they seek immediate financial benefit” (Feng, Ge, Luo & Shevlin 2011, p. 35).

However, large construction companies, such as the Abigroup, only account for a very small proportion of construction companies. In 2011-2012, “large construction businesses (employment range of 200 or more) accounted for 0.1% (or 186) of all construction businesses and generated just over a quarter of total construction income (27.3% or $83.5b)” (ABS 2013). Whereas, “small construction businesses (employment
range 0-19) accounted for 97.7% (or 204,949) of all construction businesses and the largest share of total income with 49.0% (or $149.8b)” (ABS 2013). Accordingly, efforts to regulate the industry should be focussed on small construction businesses. Currently, many of these small businesses are able to escape the reporting requirements under the Corporations Act 2001. For example, under section 45A, a proprietary company is considered small if it can satisfy at least two of the following criteria; if the company has less than $25 million in consolidated revenue, less than $12.5 million in consolidated gross assets and less than 50 employees (Corporations Act 2001). Many proprietary companies in the construction industry are able to satisfy these criteria by holding very little in assets and employing less than 50 people whilst still being able to earn significant revenue. This is possible through the industry’s ability to subcontract work.

7.3.1.7 Tax Evasion

The ATO is the regulator of compliance with tax legislation. The ATO also has the “responsibility to implement the Australian Business Number and Australian Business Reporting initiatives” (ANAO 2002, para. 4, p. 12). The ATO operates under the Public Governance, Performance and Accountability Act 2013 to ensure the use and management of public resources.

The RC made several recommendations in relation to tax evasion. These recommendations include: increased funding for compliance activities in the building and construction industry (recommendation 124); additional resources to audit, monitor and review compliance with the Alienation of Personal Services Income legislation (recommendation 125 and 126) The alienation of personal services income rules are located in Part 2-42 of the Income Tax Assessment Act 1997(C’wth) and in Division 13
in Schedule 1 to the *Taxation Administration Act 1953* (C’wth) (TA Act 1953), and took effect from 1 July 2000 (Board of Taxation 2009 p.11).

Further recommendations were: implement an auditing process of ABN’s issued to persons participating in the building and construction industry (recommendation 127); consider amendment to the ITA Act 1936 in the form of s16LA of the PRT Act 1971 making all the members of a group jointly and severally liable for the taxation debts of other group members (recommendation 130); consider amendment to s222AOB of the ITA Act 1936 to remove the right of a director of a phoenix company involved in fraudulent activity to avoid the consequences of a Director’s Penalty Notice by placing the company into voluntary administration or into liquidation (recommendation 131) (Cole 2003, vol. 9, pp. 90-92).

The tax evasion identified by the RC was sham contracting, untaxed cash payments to workers, and non-remitting PAYG withholding tax, and all of these activities “affects the public taxation revenue raised from the industry” (Cole 2003, vol. 9, p. 51); furthermore, “evasion has a direct impact upon public revenue and therefore the community as a whole” (Cole 2003, vol. 9, p. 67).

Personal Services Income “is most typically earned by contractors, consultants and sole practitioners and in 2010–11 the majority (59 per cent) of these worked in administrative and support services; professional, scientific and technical services; and the construction industries” (ANAO 2013, p. 13, para. 2).

The Board of Taxation conducted a post-implementation review into the alienation of personal services income rules to determine compliance. The Board’s findings (2009) were:
There is evidence of a low level of compliance. An unintended consequence of the ATO not being seen to be widely monitoring and auditing compliance with the alienation of personal services income rules is that it may have contributed to complacency among some taxpayers and advisors.

The Board accepts that monitoring of compliance activity on personal services income is made difficult by the absence of information from other sources on the taxpayers who should be reporting that they have personal services income (p.7).

Consequently, the taxable payments reporting system was introduced in 2012 to “improve compliance with tax obligations by … contractors” (ATO 2013, p. 15). Mandatory annual reporting requirements for certain businesses that make taxable payments to contractors in the building and construction industry took effect on 1 July 2012 (ANAO 2013, para. 10, p. 13). The new taxable payments reporting is aimed at:

improving compliance with tax obligations by contractors in the building and construction industry, creating a level playing field for businesses and improving tax fairness within the industry. Specifically, the system is aimed at addressing identified compliance problems in this industry that include: non-lodgement of tax returns, omission of contract income by contractors in their tax returns, non-compliance with GST obligations. The system is expected to promote voluntary compliance. Contractors who know their income is being reported are more likely to include the income in their tax returns (ATO 2013, p. 15).

However, the “ATO has … yet to determine whether its compliance activities are effectively mitigating the ongoing alienation of PSI risk” (ANAO 2013, para. 16, p. 18).

Based on recommendation 127 of the RC, the Australian National Audit Office (ANAO) conducted an audit of the performance of the ATO in relation to the administration of ABN registrations in 2002 and a follow up audit into the administration of ABN registrations in 2007. Although these audits have examined the ATO’s efficiency in administering ABN’s, the audits have not specifically looked at the building and construction industry.
The “issue of sham contracting was claimed to be exacerbated by the ease with which such workers are able to obtain ABNs” (ABCC 2011a, p. 19). Sham contracting is defined as an arrangement “where an employer attempts to disguise an employment relationship as an independent contracting arrangement” (FWO 2015, p. 2). In relation to the government and regulators, sham contracting affects the collection of payroll tax from the employer and income tax from the employee. In relation to employers, sham contracting is usually undertaken with the aim of avoiding responsibility for employee entitlements. In relation to competitors within the economy, sham contracting is undertaken to gain a competitive business advantage (ABCC 2011b, p. 12). The ABCC’s Inquiry into Sham Contracting Report 2011, revealed sham contracting still exists in the construction industry:

However, the issue of labour hire arrangements was canvassed by the Cole Royal Commission. While Royal Commissioner Cole made a recommendation in this regard (to develop a ‘code of conduct’ for labour hire in the building and construction industry), the issues that gave rise to his concerns continue to exist today (p. 20, para. 1.58)

Recommendation 130, regarding making all the members of a group jointly and severally liable for the taxation debts of other group members, was not implemented. The recommendation, to insert section 16LA type provisions into the ITA Act 1936, was considered to create “insurmountable difficulties in the administration of the taxation system” and consequently not warranted (Australian Government 2003, pp. 93-94).

Non-remittance of PAYG withholding tax is often the outcome of phoenix activity. In 2009, in its proposal paper entitled ‘Action against Fraudulent Phoenix Activity’, Federal Treasury recommended the director penalty regime “be amended to overcome its limitations with respect to the avoidance of PAYG(W) obligations by fraudulent phoenix operators” (S4.2.1, p. 12). The Tax Laws Amendment (2012 Measures No. 2)
Act 2012 (C’wth) amended the TA Act 1953 by extending “the director penalty regime so that directors are personally responsible for their company’s unpaid superannuation guarantee amounts”; making “directors and their associates liable to pay-as-you-go (PAYG) withholding non-compliance tax in certain circumstances”; and ensuring that “directors cannot discharge their director penalties by placing their company into administration or liquidation when PAYG withholding or superannuation guarantee remains unpaid and unreported three months after the due date” (Treasury 2010-12, p. 7)

Tax compliance activities in the construction industry as at June 2015 revealed:

- 23% of businesses within the industry are rated as higher risk of not correctly meeting their tax obligations, which may be subjecting honest businesses to unacceptable levels of unfair competition
- On average, 23.75% of businesses within the industry fail to lodge their activity statements on-time
- Based on community referrals, this industry has the highest level of community concern reports about potential tax evasion (ATO 2015, para. 2).

The role of accountants is conflicting in relation to tax. Clients expect advice from accountants on how to avoid or evade tax, yet the role of accountant’s is primarily that of “tax enforcer/compliance” (Marshall, Smith & Armstrong 2010, p. 197). “An industry exists amongst accountants, tax agents and lawyers dedicated to the promotion of this [sham contracting] activity” (Cole 2003, vol. 9, p. 68).

Although a decade later, the same problem is evident with calls for advisors, such as accountants to be targeted for their complicity. Anderson and Haller (2014) state:

More must be done to target advisors, both from the legal and accounting professions...As Jooine demonstrates, the decision in Somerville certainly did not discourage the employment lawyers who concocted the sham contracting arrangements for their clients. Fraudulent phoenix activity costs the Australian economy hundreds of millions of dollars annually and it is fair to say that professional advice facilitates a portion of this. How sizeable this is cannot be ascertained. Yet any deliberate efforts to circumvent the proper distribution of
assets to creditors when a company becomes insolvent must be deterred, and it is particularly of concern when those deliberate efforts come from professionals who are subject to codes of practice that stress honesty, duty and propriety (p. 500).

7.3.2 An Action Plan

As discussed in section 7.2.2, there are two steps to repairing the construction industry’s legitimacy: fix the unlawful behaviours and communicate this to the public. This study recommends that the construction industry’s regulators should develop policy to enable accountants to help address the unlawful behaviours and communicate this to the public. This would help restore public confidence in the industry as well as improve the social practice of accounting in the industry. Given much of the unlawful behaviours involved financial management, this would help address the industry’s social contract breach.

At the conclusion of section 7.2.2, it was argued that the construction industry can repair its legitimacy by communicating to the public six behaviours, for example willingness to meet its corporate responsibility to pay tax.

Section 7.3.1 examined how the lead regulators in each of the seven unlawful behaviours could enable accountants to act as internal regulators. The study recommends that the key to successful implementation of new policy is authority for the regulators to empower accountants in the specific unlawful processes involving accountants. In chapter 5, table 5.2 listed these unlawful processes. An action plan for regulators in developing new policy should target these specific processes. In terms of priorities, the study recommends that new policy be developed in this order of urgency:

1. Tax evasion
2. Employee entitlements
3. Phoenix company activity
4. Security of payments
5. Profit reporting
6. Inappropriate payments
7. Payroll tax

Priorities 1 and 2 fall into quadrant 1 (top right hand corner) of figure 5.3. These two activities, tax evasion and employee entitlements, are of highest concern because they fall into the social practice most considered normal in the role of accountants. This is where the accounting role may be described as objective in the sense that accountants are supposed to follow the rules, that is the standards, without adjustment. This is of highest concern because unlawful behaviour may, therefore, be hidden. Individuals participating in unlawful behaviour associated with tax evasion and failing to pay employees their entitlements can feel protected by their accountant. In other words, they can blame their accountant if their unlawful behaviour is discovered. This provides a natural defence for unlawful behaviour. This is further emphasised by the legislation surrounding company directors where directors can avoid punishment by arguing they accepted advice or information from a third party qualified to give such advice or information. In other words, they can feign ignorance. In this case, the third party is the accountant. It is also concerning that the processes associated with unlawful behaviour in these two activities are core accounting work. This presents an opportunity to review the practice of accounting which is covered next in section 7.4.

Priority 3 falls into quadrant 2 (bottom right hand corner) of figure 5.3. This activity, phoenix company activity, is where the accountant is trying to follow accounting standards but is being excluded from the social practice of the activity. In other words, the accountant will try to stop the unlawful behaviour if they become aware or involved. If this happens, the individuals involved will usually follow the accountant’s advice. The
problem with phoenix company activity is that unscrupulous individuals are aware what they are doing is wrong and they try to hide it from accountants. There is an opportunity to introduce policy which would ensure accountants are involved in this activity. It is the next priority because it would deter a major source of illegitimate behaviour within the industry.

Priorities 4 and 5 fall into quadrant 3 (bottom left hand corner) of figure 5.3. These two activities, security of payments and profit manipulation, is where the accountant is seen as the enemy. In security of payments, the accountant may be seeking or hiding financial information from others to establish the company’s financial position. Policy which provides accountants with power to obtain this information and penalties for falsifying or not providing information is necessary. Profit manipulation involves a range of fraudulent activities aimed at misleading others. One of an accountant’s main roles is profit reporting. Fraudulent reporting of financial statements must be prosecuted if the public is to regain confidence in the construction industry. Accountants need to be given the authority to report unlawful behaviour to regulators along with appropriate income and witness protection. This is a lower priority because it will be difficult to introduce and implement necessary policy changes, so this is seen as a longer term set of actions.

Priorities 6 and 7 fall into quadrant 4 (top left hand corner) of figure 5.3. These two activities, inappropriate payments and payroll tax, is where the accountant is isolated from the social practice associated with unlawful behaviour. In these activities, unlawful activities may be hidden from the accountant or the accountant is not consulted. Much of the processes involved are the core work of accountants. Unscrupulous individuals would know that accountants must be involved at some point in the unlawful activity, however, the unlawful behaviour is disguised so the accountant is not aware. For example, giving a financial gift to a union official in return for industrial peace but
disguised as a donation or a purchase of goods and services which were not actually delivered. Policy may be introduced to give accountants the authority to question disguised payments and other unlawful processes and to enforce appropriate payment and payroll tax payments under law. While the word ‘disguised’ suggests such a policy may be ineffective because the behaviour is hidden from accountants, the point is that enabling accountants to look for hidden inappropriate behaviour would be effective.

7.3.3 Implementation

If these policy outcomes are to be successfully implemented, there are three necessary steps:

1. Regulators must be persuaded of the need for change. This must come from the Federal Government. Relevant Ministers must be convinced that these policy changes will help repair legitimation of the construction industry and that the effort is worthwhile.

2. Income protection. Accountants will need protection. Given their primary motivation in engaging in unlawful behaviour was self-interest, more specifically to protect their employment and income, the regulators need to ensure there are no negative consequences for accountants in changing their role. If they are to be internal industry regulators, their employment and career development must be protected. Legislation must be introduced, along with appropriate penalties for non-compliance, to ensure that accountants are protected. This could emerge in employment legislation associated with unfair dismissal and Fair Work Practice.

3. Stakeholder involvement. The accounting industry, including accounting bodies, auditors, and accountants practicing in the construction industry must work together
and give full commitment if these policy changes are to be successfully introduced. This is discussed in the next section.

7.4 Practical Outcomes

7.4.1 The Accounting Bodies

This study’s findings present an opportunity for accounting bodies to take action to improve accounting practice within the construction industry. Consideration needs to be given to the role the professional accounting bodies can play in helping accountants as internal regulators of the construction industry.

In Australia, there is no single body responsible for regulating the accounting profession. The bodies that are involved in the regulation of the profession and the activities in which accountants may be engaged, are outlined below:


Tax Practitioners Board: Tax practitioners

Australian Prudential Regulation Authority: Auditors/trustees of superannuation funds, Directors and senior managers of insurance companies

Australian Financial Security Authority: trustees in bankruptcy

(Institute of Chartered Accountants, Australia and New Zealand 2013).

In Australia, there is a co-regulatory environment, which is comprised of government regulators, government standard-setting bodies, the Accounting Professional and Ethical Standards Board and the professional accounting bodies. “Ethics is fundamental to the accountability of the profession and its mandate to self-regulate within the broader co-regulatory regime in Australia” (Institute of Chartered Accountants, Australia and New Zealand 2013).
Zealand 2013). Under the APES 110 Code of Ethics for Professional Accountants Clause 100.1 (Accounting Professional & Ethical Standards Board Limited 2013), accountants are bound to act in the public interest as outlined below:

A distinguishing mark of the accountancy profession is its acceptance of the responsibility to act in the public interest. Therefore, a Member’s responsibility is not exclusively to satisfy the needs of an individual client or employer. In acting in the public interest, a Member shall observe and comply with this Code (APES 110, Section 100.1).

In order to act in the public interest, the principle of objectivity, in particular, must be maintained. The Code of Ethics requires the principle of objectivity to be upheld and members to avoid situations where objectivity may be compromised such as the following:

A Member shall not knowingly be associated with reports, returns, communications or other information where the Member believes that the information:

(a) Contains a materially false or misleading statement;
(b) Contains statements or information furnished recklessly; or
(c) Omits or obscures information required to be included where such omission or obscurity would be misleading. (APES 110, Section 110.2)

The principle of objectivity imposes an obligation on all Members not to compromise their professional or business judgement because of bias, conflict of interest or the undue influence of others. (APES 110, Section 120.1)

Threats to the objectivity of the accounting profession would be the greatest in a lawless industry, such as the building and construction industry. Generally, an accountant’s ability to act objectively and professionally may be threatened as follows:

Threats may be created by a broad range of relationships and circumstances. When a relationship or circumstance creates a threat, such a threat could compromise, or could be perceived to compromise, a Member’s compliance with the fundamental principles. A circumstance or relationship may create more than one threat, and a threat may affect compliance with more than one fundamental principle. Threats fall into one or more of the following categories:
(a) Self-interest threat — the threat that a financial or other interest will inappropriately influence the Member’s judgement or behaviour;

(b) Self-review threat — the threat that a Member will not appropriately evaluate the results of a previous judgement made or service performed by the Member, or by another individual within the Member’s Firm or employing organisation, on which the Member will rely when forming a judgement as part of providing a current service;

(c) Advocacy threat — the threat that a Member will promote a client’s or employer’s position to the point that the Member’s objectivity is compromised;

(d) Familiarity threat — the threat that due to a long or close relationship with a client or employer, a Member will be too sympathetic to their interests or too accepting of their work; and

(e) Intimidation threat — the threat that a Member will be deterred from acting objectively because of actual or perceived pressures, including attempts to exercise undue influence over the Member (APES 110, Section 100.12).

Given the economic and financial pressures faced by the building and construction industry, there were cases exposed by the RC, previously mentioned, where accountants were placed under pressure to process certain transactions. Whilst these accountants were able to withstand the pressure, there are likely to be those who are unable to do so. In these cases, there needs to be a form of recourse. However, the principle of confidentiality requires members of the accounting profession to refrain from disclosing confidential information unless required to by law or there is a professional duty or right to disclose confidential information as outlined below:

The principle of confidentiality imposes an obligation on all Members to refrain from:

(a) Disclosing outside the Firm or employing organisation confidential information acquired as a result of professional and business relationships without proper and specific authority or unless there is a legal or professional right or duty to disclose; (APES 110, Section 140.1)

The following are circumstances where Members are or may be required to disclose confidential information or when such disclosure may be appropriate:

(a) Disclosure is permitted by law and is authorised by the client or the employer;

(b) Disclosure is required by law, for example:

(i) Production of documents or other provision of evidence in the course of legal proceedings; or
(ii) Disclosure to the appropriate public authorities of infringements of the law that come to light; and

c) There is a professional duty or right to disclose, when not prohibited by law:

(i) To comply with the quality review of a member body or professional body;
(ii) To respond to an inquiry or investigation by a member body or regulatory body;
(iii) To protect the professional interests of a Member in legal proceedings; or
(iv) To comply with technical standards and ethics requirements. (APES 110, Section 140.7)

In the late 1990s the procedures known as the Corporate Law Economic Reform Program (CLERP) placed accounting standards as a major agenda item (Treasury 1998). Whilst Corporate Law Economic Reform Program 9 (CLERP 9) and section 1317AA of the Corporations Act 2001 provide protection to the ‘discloser’, the Code of Ethics cautions members. Apparently, the “circumstances described in paragraph 140.7 do not take into account Australian legal and regulatory requirements”. “A Member considering disclosing confidential information about a client or employer without their consent is strongly advised to first obtain legal advice” (APES 110, Section AUST140.7.1). Apart from any possible legal implications, an accountant needs to consider the social ramifications of being a “whistle-blower” or “dobber”.

7.4.2 The Accounting Standards

This study’s findings present an opportunity for the accounting standards associated with the construction industry’s unlawful activities to be reviewed and perhaps changed. There may even be an opportunity to introduce a set of industry-specific standards for the construction industry.

A major finding of this study has been the identification of unlawful processes involving accountants (see table 5.2 in chapter 5). This creates a roadmap for revision of accounting standards. It lists the accounting practice which might be reviewed with new
standards. The study found that accounting is a subjective rather than an objective process. This means that accountants use their judgment, intuition, and experience, as well as their organisational context, to interpret and apply the accounting standards when doing their work. This means accountants have a degree of flexibility in doing their work. The study has found that accountants do not, and perhaps cannot, always follow the standards objectively. However, the study also found that accountants were involved in unlawful activities in the construction industry. This suggests that accountants had too much flexibility in the way they did their work in the construction industry. There was too much creative accounting. The result was a loss of control and adherence to the principles of good financial management which is the role of accountants. Rather than make accounting completely objective, the study argues that it be made ‘less subjective’ if accounting is to help the construction industry repair legitimation. This may be done by reviewing and revising relevant accounting standards.

Accounting standards such as reduced accounting disclosure requirements should not apply to construction companies, given its fragmented industry structure. The construction industry needs to repair its legitimacy and disclosures complying with accounting standards would contribute towards legitimation. Given the lawlessness of the construction industry, construction entities have public accountability and should not have the option to elect to comply with some or all of the excluded reporting requirements of AASB 111, Construction Contracts, paragraph Aus. 1.8 under the reduced disclosure requirements relating to Tier 2 of AASB 1053, Application of Tiers of Australian Accounting Standards, paragraph 13(a). However, this would put an intolerable cost burden on all of the 200,000 plus small businesses in this industry.
The definition of public accountability in AASB 1053 is different but perhaps should include the construction industry because of its unlawful behaviour. The standard defines public accountability as;

Public accountability means accountability to those existing and potential resource providers and others external to the entity who make economic decisions but are not in a position to demand reports tailored to meet their particular information needs.

A for-profit private sector entity has public accountability if:

(a) its debt or equity instruments are traded in a public market or it is in the process of issuing such instruments for trading in a public market (a domestic or foreign stock exchange or an over-the-counter market, including local and regional markets); or

(b) it holds assets in a fiduciary capacity for a broad group of outsiders as one of its primary businesses. This is typically the case for banks, credit unions, insurance companies, securities brokers/dealers, mutual funds and investment banks (2010, p.12)

The option for this exists in AASB 1053 whereby it is stated:

Whilst Tier 2 requirements would be available to all not-for-profit private sector entities and most public sector entities, regulators might exercise a power to require the application of Tier 1 requirements by the entities they regulate (2010, p. 5 and para. 15, p. 9 – slightly more detailed)

Except for the presentation of a third statement of financial position under Tier 1, the presentation requirements under Tier 1 and Tier 2 are the same (2010, para. 9).

The Corporations Act 2001’s definition of a Disclosing Entity would exclude most of the small participant in the construction industry. However, this allows small business to avoid the accountability of disclosure in their financial reporting. This means that the majority of firms in the construction industry (that is, small businesses) can avoid public accountability typically provided by accounting disclosures. This is the subject of recent debates on the definition of a reporting entity being considered by AASB Exposure Draft ED 264 Conceptual Framework for Financial Reporting 2015. The construction
industry provides an accounting in practice example to support some of the proposed changes to the International Accounting Standards Board’s (IASB) Conceptual Framework for Financial Reporting 2010. The construction industry example particularly supports the comments made by the University of Melbourne Comments letter November 2015 on the definition of a reporting entity.

There have been considerable debates in Australia as to which entities should report. This question has come to the fore in the area of differential reporting and in the extension of accounting standards into the public and not-for-profit sectors. The IASB has so far only considered the borders of the reporting entity and not when one should exist. This is left to local jurisdictions to consider, except that the dividing line drawn between IFRS and SME accounting has effectively deemed publicly listed entities to be reporting entities. However, there is no exploration of whether very small entities should account on the same basis as SMEs. Conceptually, the IASB must have some implicit idea when an entity should be a reporting entity. We would have expected that when there is a range of users dependent upon general purpose financial reports to make decisions about allocating scarce resources that the entity should be, prima facie, a reporting entity (Pinnuck 2015, para. 11).

Accounting disclosure requirements for the construction industry should be increased considering much of the industry’s unlawful behaviour occurred due to poor or inappropriate financial management. The construction industry had the second highest number of insolvency reports lodged with ASIC, with financial record keeping identified as the highest cause. In 2013–14, of the three industries with the highest number of reports lodged, construction came second with “2,153 reports or 22.8% of reports: see Table 9” (ASIC 2014, p. 17, para. 34). One of the top three causes of failure were inadequate cash flow or high cash use with construction amounting to “46.4% of reports” (ASIC 2014, p. 19, para. 38a). Further evidence of inappropriate behaviour was indicated by these ASIC findings: the construction industry scored the highest (78 out of 247) for possible pre-appointment criminal misconduct for Sections 286 and 344(2), and also obligation to keep financial records of the Corporations Act 2001(1 July 2013 to 30 June 2014): see table 20 (ASIC 2014, p. 17, para. 34).
The regulation effected by the RC was fundamentally focused on unlawful industrial action and workplace rights. Commissioner Cole was appointed to conduct the RC, excluding the domestic housing sector, by Letter Patent on 29th August 2001 to investigate:

a. the nature, extent and effect of any unlawful or otherwise inappropriate industrial or workplace practice or conduct, including, but not limited to:
   (emphasis added) i. any practice or conduct relating to the Workplace Relations Act 1996, occupational health and safety laws, or other laws relating to workplace relations; and
   ii. fraud, corruption, collusion or anti-competitive behaviour, coercion, violence, or inappropriate payments, receipts or benefits; and
   iii. dictating, limiting or interfering with decisions whether or not to employ or engage persons, or relating to the terms on which they be employed or engaged;

b. the nature, extent and effect of any unlawful or otherwise inappropriate practice or conduct relating to:
   i. failure to disclose or properly account for financial transactions undertaken by employee or employer organisations or their representatives or associates; or
   ii. inappropriate management, use or operation of industry funds for training, long service leave, redundancy or superannuation;

c. taking into account your findings in relation to the matters referred to in the preceding paragraphs and other relevant matters, any measures, including legislative and administrative changes, to improve practices or conduct in the building and construction industry or to deter unlawful or inappropriate practices or conduct in relation to that industry (Commonwealth of Australia 2001)

No specific regulation was put in place to overcome, the TOR Part b. i., failure to disclose or properly account for financial transactions (Commonwealth of Australia 2001).

Most regulation to date has been externally driven and reactive. Consequently, cultural change has not been effected and regulation has been haphazard with the involvement of a number of regulators. Whilst there is clearly a need for regulation, an alternative, more
proactive approach, would be internal regulation. Both forms of regulation need to be considered, particularly in light of effecting cultural change. Internal regulation may be a way of transforming the culture of the construction industry, from one of lawlessness to one of more law abiding.

7.4.3.1 External regulation

External regulation is predominately conducted by ASIC through the _Corporations Act 2001_ by classifying companies as public companies or proprietary companies. Proprietary companies are further classified as large proprietary company or small proprietary company on the basis of satisfying two of the following three criteria; consolidated revenue for the financial year of $12.5M or less, gross assets of $12.5 million or less, and 50 employees or less at the end of the financial year (S45A).

However, the compliance requirements for proprietary companies are less stringent than for public companies yet proprietary companies account for 98.87% of all registered companies (Governance Institute of Australia 2012). Breaches of regulation are typically uncovered when a company collapses and external administrators are appointed. This is illustrated by the following example;

> During the life of a small, private, unaudited Australian company, breaches of company law by its directors usually go unnoticed by the regulator because nobody other than the offenders (the directors) and perhaps one or two employees are aware that offences have occurred. Moreover, there are often no immediate victims, so there is not likely to be a complaint as long as the company continues to pay its suppliers, employees and taxes.

> However, when a company collapses and an external administrator is appointed, a supplementary branch of law enforcement comes into existence. The external administrator is required by the Act to make a formal report to ASIC about any alleged offences by a past or present director or other officer of the company that they detect. This requirement to report is not confined to offences under company law but relates to suspected violations under a law of the Commonwealth or a state or territory in relation to the company (ASIC 2008b). Where the suspected crime is not within ASIC’s province—for example,
restrictive trade practices or recklessly polluting the environment—the matter is referred to the appropriate regulatory authority.

External administrators, especially liquidators, are ideally positioned to uncover offences. They have the right to examine all the company’s records, the right to question directors and employees, and the right to examine the directors and others under oath in court. They may also apply to a court for arrest warrants and for search and seizure warrants (Keenan 2013, pp. 2-3).

Alternatively, financial reporting and accounting should be made a requirement for all of the construction industry, including small proprietary companies which account for a large proportion of the industry. In 2011-12, small construction businesses (employment range 0-19) accounted for 97.7% (204,949) of all construction businesses and the largest share of total income with 49.0% (or $149.8b) (ABS, 2013). While there is a need to recommended that section 292 of the Corporations Act 2001 be expanded to include financial reporting by all proprietary companies in the construction industry, the cost burden of such a recommendation on all the small businesses would need to be considered.

The construction industry, an industry renowned for lawlessness, has been permitted to self-regulate in terms of accounting. There is a need to eliminate self-regulation in a lawless industry. As Gaffikin (2005a, p.17) said there needs to be regulation to act as a deterrent. There clearly needs to be regulation of the building and construction industry.

Enforcement is often a criticism of self-regulation (Gaffikin 2005a, p. 17). Although, professional accounting bodies have disciplinary committees designed to enforce the relevant regulations, their effectiveness is questionable. This is due to the fact the effectiveness of the process is undermined by power and politics. Gaffikin (2005a, p. 17) proffers the following example, “would the accounting bodies have taken action against a major accounting firm if there was evidence of some of its member acting
inappropriately? Some suggest had they done so there may have been fewer corporate scandals”.

7.4.3.2. Internal regulation

Self-regulation is a defence against the Federal government enforcing regulation on accounting practitioners (Gaffikin 2008, p. 97). Self-regulation is seen as necessary to maintain the integrity of the profession of accounting, “as the capacity to effectively self-regulate is viewed as one of the hallmarks of a profession” (Gaffikin 2008, p. 97). In other words, if accounting is to command respect it needs to self-regulate.

Regulation of a profession, such as accounting, needs a significant event to trigger societal interest and develop pressure on the profession. Gaffikin (2008) describes how the Great Economic Depression of the 1930s created the impetus for reform of the accounting profession. It was felt that accountants tended to try to satisfy management rather than portray economic reality. The Depression led to calls for accountants to produce financial information people rely on, and for uniformity of practice by practitioners (Gaffikin 2008, p. 96). The focus shifted from satisfying internal users of financial reports, that is management, towards external users, for example, investors. The desire for uniformity came from the need for investors to compare financial performance of different companies. Gaffikin (2008) explains the evolution of the regulation of accounting from that time, including the establishment of various accounting bodies and attempts to reconcile differences globally.

Gaffikin (2008, p. 101) explains how the very early approach to accounting standards began in Australia in 1946 with the Institute of Chartered Accountants in Australia (ICAA), however, they had “little impact on accounting practice and a high degree of non-compliance”. He discusses the evolution of accounting standards and the various
bodies responsible. The problem with accounting standards has always been their enforcement (Gaffikin 2008, p. 103). Gaffikin (2008 p. 103) suggests that the introduction of legal enforcement ‘put an end to the accounting profession’s self-regulation’. In its place, accounting became part of effective corporate governance. Self-regulation has been replaced by statutory regulation. However, Gaffikin (2008) sees this as a positive move because it recognises that accounting is an important part of the nation’s economic framework. However, this has resulted in still further problems with the regulation of accounting, as now even regulations are subject to official interpretations (Gaffikin 2008).

Clearly, there is a need for improved regulation in the construction industry, which is due to both the public interest and institutional practices of the construction industry (Gaffikin 2005). Regulatory practices since the RC (2003) have not been successful with continued unlawful behaviour. Gaffikin (2008, p. 113) describes accounting regulation as a “very unsatisfactory story”. Gaffikin’s (2008) solution is a theoretical framework. In an ideal world, argues Gaffikin (2008), theories would exist to explain and lead practice. Theories, in this sense, would represent shared mental models of best practice which accountants everywhere would embrace because it simply makes sense to do things this way. However, as Gaffikin (2008) concludes with some despair, “there is no acceptable theory of accounting”. Other forms of regulation need to be examined.

This study also recommends internal regulation for the building and construction industry more broadly. The solution is to internally regulate via improved social practice. Accounting as a social discipline is the ideal regulator (Hopwood & Miller 1994). This means that agreement on appropriate behaviours in social practice is a way forward. In practice, this means making accountants aware of their roles in social networks when practicing accounting; who they will be interacting with; the dangers of
high intensity, harmony and cohesion in unlawful activities; the use of power and politics to coerce them to engage in inappropriate behaviours; how stakeholders perceive their purpose, that is, their differing social contracts, and the expectations of society; and how to draw a line between creative accounting and inappropriate or unlawful activity. The identification of the unlawful activities and the social practice associated with accountants’ work in these activities would lead to an awareness campaign for accountants. External regulators would need to work with accountants to give them a mechanism to report inappropriate behaviours, as well as the power to address them and the protection of job security and no career damage. Internal regulation of the building and construction industry by the accounting profession must be led by practising accountants who develop a shared mental model of appropriate social practice and professional safety to operate within the social networks where they may be vulnerable to pressure by stakeholders.

A problem for the construction industry is caused by the size of its companies. While large companies such as head contractors will have internal accountants, the majority of companies are small and would not employ an internal accountant. This presents several problems in terms of regulation. Small companies may defend themselves against poor financial management or even inappropriate or unlawful behaviour by way of ignorance, that is, honest mistakes or errors of judgment because they could not afford to pay an accountant. This study recommends reform of the construction industry by mandating the use of accountants for companies of every size. While small companies do not have sufficient revenues to be able to afford a full-time internal accountant, they must be required to engage the services of an external accountant and be required to produce regular financial reports that comply with the accounting standards. The economic consequences of this change to public accountability and financial disclosures would be
significant. This initiative would add a cost to companies already under financial pressure. It is likely that the increased cost would be passed onto customers in the form of increased process. However, it is possible that the benefits to society in addressing many of the issues found in the construction industry’s social contract breach would outweigh the costs. To offset the increased costs for small business, the study recommends that the cost of employing an accountant, whether internal or external, be rewarded with substantial tax offsets to encourage small companies to comply with this mandate and to follow the advice of the accountant. Only if all companies, large and small, use accountants can the industry successfully self-regulate and effect cultural change. It is acknowledge that this is an aspirational goal and would be very difficult to implement in practice. For example, the majority of small construction firms could not afford to employ a full-time accountant. However, they could be required to use an accountant to comply with public accountability requirements, which would require employing an accountant on a casual basis similar to doing tax returns. It is also important to recognise that using an accountant is only a step in the reform necessary to address the construction industry’s unlawful behaviour. Industry self-regulation requires a complex set of inter-related interventions. This is discussed further in the next section.

7.4.3.3 A Framework

There has not been the structural and cultural reform in the construction industry which Commissioner Cole indicated was an urgent need. Cultural reform is changing the way business is done. Social transformation is yet to occur in this industry. This is in part due to not only the fragmented structure of the industry but also the patchwork legislation in addressing the lawlessness of the construction industry. A new approach is needed.

While the recommendations from Gyles and Cole did become legislation, perhaps the real underlying issue that should be addressed is why the building
and construction industry operates the way it does. Neither of those Royal Commissions produced a vision of a different industry, apart from a law abiding one, and made no recommendations on the direction that strategic development of the industry might take (de Valence 2014).

As Zimmermann (2007, p. 31) concludes ‘the realization of the rule of law is as much a cultural achievement as it is a legal-institutional one’.

There are multiple social systems within the construction industry (see chapters 5 and 6). Practical solutions to structural and cultural reform must embrace a systems thinking approach. This study recommends a construction industry community of action research be established to implement the policy and practical outcomes outlined in this chapter. “A community of action research embeds change-oriented projects within a larger community of practitioners, consultants and researchers, to produce knowledge that is useful to people in their everyday lives” (Senge & Scharmer, 2001, p. 238).

7.5 Theoretical Outcomes

The study contributes to CAT by explaining how accounting practice was influenced by stakeholder interests, that is, the construction industry’s political economy. CAT aims to develop a more self-reflexive and contextualized perspective on accounting which sees the connections between society, history, organisations, accounting theory, and accounting practice (Lodh & Gaffikin 2005, p. 156). The study examines the role of sectional interests, in this case construction industry stakeholders, in accounting practice. Figure 1.1 illustrated the study’s theoretical approach and how it contributes to CAT.

PET (Gray, Owen & Adams 1996, p. 47) provides the social, political and economic framework for this thesis. This theory explicates that the strategic outcomes of
accounting practices favour specific interests in society and disadvantage others (Cooper & Sherer 1984, p. 208). The study explains how socio-political power inequities amongst construction industry stakeholders created conditions leading to unlawful behavior. PIT explains how regulation is introduced to protect the public and that regulators seek to maximize the overall welfare of the community. This study explores how regulation of the construction industry failed. PIT assumes that the regulator, which is usually the government, is a neutral arbiter of the public interest and does not let its self-interest impact on the regulatory process. The study’s contribution to PIT is to examine the reasons why regulation of the construction industry was so difficult and to suggest how this may be improved. A key finding is the need to empower stakeholders with the capacity to self-regulate, including accountants. More specifically, the study contributes to the PET of regulation. The study advances our understanding of accounting regulation by going beyond the purely economic perspective of the neo-classical approaches, to reflect the broader cultural and societal values at the time of the RC (2001-2003). It also frames guidelines for industry reform (chapter 7) around regulatory strategies and, in doing so, advances the importance of the role of accounting in legitimising an industry with a long history of unlawfulness.

The study contributed to LT by defining the nature of the social contract breach between the construction industry and Australian society, and strategies to repair legitimacy. Legitimation is the process that leads to legitimacy (Deegan 2005; Lindblom 1994). The only real difference between gaining and repairing legitimacy is that gaining is a proactive approach and repairing is a reactive approach. Repairing involves responding to a crisis. The RC definitely created a crisis for the construction industry. The study explains what happens if an industry is unwilling to accept the regulator’s demand to repair legitimacy. The analysis in the period following the RC, post 2003, shows that the
construction industry continued unlawful behaviour despite being told it had breached its social contract. This poses questions about the social reality of LT and whether it applies in all industry contexts.

The contribution to LT was to identify factors creating a situation where some stakeholders’ socio-political power exceeds the public interest, that is, the power of the regulator, meaning the industry ignores the need to repair legitimacy. The tables in chapters 3 and 4 illustrate the factors which create this situation where legitimacy is ignored by industry stakeholders. More specifically, the socio-political themes in table 4.2 highlight the power of the unions and a culture of intimidation and conflict characterised by self-interest, rivalry and jealousy. There is a sense of succeeding at the expense of others and a lack of empathy. This helps explain why the public interest was ignored. Table 4.5 provides insight into stakeholders’ motivations and behaviours. LT’s pragmatic construct explains that the politics in stakeholder relationships were defined by greed, exploitation, and stand-over tactics; while the moralistic construct was characterised by being irresponsible or powerless.

The study contributed to ST from the managerial perspective by exploring how the constructs of relationships, impact and expectations help us understand the social practice of accounting within the context of a social contract breach. At a broad level, the study’s contribution to ST, therefore, is to explain why industry practices favour specific interests in society and disadvantage others (Cooper & Sherer 1984, p. 208). This helps understand the social praxis underlying the behaviour leading to the construction industry’s legitimacy gap explained by the differing interests of the social actors, that is, stakeholders. This broad contribution lies in the empirical evidence of the socio-political power inequities defining the social interaction between industry stakeholders which have breached their social contract. The ST constructs of
relationships, impact and expectations explain why unlawful behavior emerged in this industry.

The study makes several specific contributions to ST. First, it uses the theory of SNA construct of density to explain the social network interaction of stakeholders, contributing to our understanding of relationships. Figure 5.1 summarises the roles identified for stakeholders from this analysis. Second, it uses the SNA construct of heterogeneity and homogeneity to examine behaviour between these stakeholder groups, with a particular focus on their harmony and cohesion, contributing to our understanding of ST’s ethical perspective. Whereas, previous research argues that cohesion is a positive social practice, this study’s findings show that it can be a negative factor, particularly if the rest of the network is behaving unlawfully. In these circumstances, traditional measures of cohesion such as democracy are actually unfavourable because it reveals that accountants, in this case, are agreeing with the unlawful behaviour of the others within their social network. Therefore, the finding that three quarters of the accountants’ social networks are democratic is actually a negative result. It suggests that accountants did agree with unlawful behaviour in the following activities: tax evasion, employee entitlements, payroll tax, and inappropriate payments. Unlawful behaviour in these activities could not have occurred without accountants’ participation and, the findings suggest, without their agreement. Table 5.2 explains accountants’ social behavior using the SNA constructs of interaction, harmony and cohesion leading to 15 scenarios. The study developed a conceptual framework explaining four types of roles for accountants: trust, police, isolated, and hostile (see figure 5.2).

Third, the study makes a further important contribution to ST by using types and causes of power to explain political behaviour contributing to our understanding of the construct, impact. It identified coercive, reward and expert power. Fourth, the study
identified four societal expectations to explain the social contract breach contributing to our understanding of the construct, expectation. It identified accountants’ differing social contracts with industry stakeholders.

In summary, the study’s theoretical contribution to the aims of critical accounting research is by advancing our understanding of the social practice of accounting. Figure 1.1 shows that the bridge is PIT, which connects critical accounting to LT and ST. The societal contract breach, which is defined by LT, identifies the opportunity for accounting to improve society, and ST enables us to understand why the legitimacy gap exists and how accountants might help close the gap. More specifically the use of power and language by stakeholders to influence the role of accounting. An appreciation of language is vital to understanding the practice and theory of accounting (Gaffikin 2008, p. 234). The study has used CDA and CA to explore the use of language in the research data analysed by this thesis, for example the RCR and associated documents. This was applied explicitly in chapter 4 and implicitly in chapters 5 and 6. In chapter 4 it was used to illustrate how these methods could explain the socio-political inequities between stakeholders in the construction industry, and also the behaviours which had become cultural norms. In the later chapters, the methods were used implicitly to ensure the analysis flowed like an historical narrative and was not too mechanical.

Figure 7.3 summarises the study’s theoretical outcomes:
Figure 7.3 presents three areas of outcome. First, the left hand side of the figure looks at the study’s contribution to PIT. It highlights the importance of establishing the significance of the industry in maintain legitimacy, the need to clarify and communicate the social contract, understanding the nature of the social contract breach and its causes, and how those breaching the contract perceive themselves and the need for significant consequences if legitimacy repair is to be achieved. Second, the middle part of the figure explains how to define social practice. It measures interaction also showing how some constructs can actually have a negative impact if there is an unlawful culture, it develops fifteen scenarios of social practice and evidence that accounting is subjective practice, and these are combined into four types of social practice. Impact is measured in terms of type of power and source of power. Expectations are measured in terms of three summary concepts. The right hand side of the figure presents suggestions on how to
address social contract breach focusing on the role of accountants. It looks at creative accounting and inappropriate behaviours and how to address these by looking at motives, social practice, and accountability. It proposes policy outcomes in terms of the role of lead regulators in the seven unlawful activities, motivation for these regulators and protection for those willing to fight the unlawful behaviours. Finally, it looks at practical outcomes in terms of the role of accounting bodies in regulating accounting behaviours and the possibility of using accountants to regulate the industry.

Gaffikin quotes Aristotle who said “practice proceeds from theory” (Gaffikin 2008, p. 239). “There are many significant societal problems in which accounting needs to play a role” (Gaffikin 2008, p. 239). The unlawful behaviours by the construction industry in this study provided an opportunity to address a criticism of ST by critical accounting researchers regarding lack of empirical evidence about its application.

7.6 Conclusions

The chapter developed a preliminary conceptual model on the role of accounting as a legitimisation process, based on the findings presented in this study. There were four groups of findings: first, the role of accounting, second, policy outcomes, third, practical outcomes, and fourth, theoretical outcomes.

In the first group of findings, several questions were explored. Why do accountants act subjectively rather than objectively when doing their work? By subjectively, it is meant that accountants have scope to act independently of the accounting standards; that is, to use their own judgment, intuition, experience, or organisational context to adapt the standards. By objectively, it is meant that accountants always follow the standards. This
study has shown that accountants in the construction industry acted subjectively. They did this because accounting allows scope for what is called creative accounting. Why did accountants in the construction industry become involved in activities they should have known were unlawful? This was explained in chapter 6 by the pressure placed on accountants by other stakeholders (see the section 6.2 on Impact). Despite this, accountants still have free will and choice about how they behave. To understand this behaviour, accountants’ motivation was explored. Accountants’ interaction with construction industry stakeholders was personal and impersonal. It was personal in the sense that accountants interacted socially with others in doing their work and in helping others find meaning and interpretation in their work outputs, that is, their reports. On the other hand, interaction was impersonal in the sense that the work produced by accountants would have been read and interpreted by others without any personal contact with the accounting staff who produced the report. This different interaction is explained by the type of work output, internal versus external, and the type of decision.

In the second group of findings, the study provides regulators with information about the social practice of accounting which might be used to improve regulation of the industry. This could be done by empowering accountants to act as internal regulators. Given much of the industry’s unlawful behaviour occurs due to poor or inappropriate financial management, improved accounting practice in the industry could help restore public confidence and repair legitimation. Policy improvements could be led by the lead regulator within each unlawful activity (see section 7.3.1). The chapter examined financial management regulation, and the role accountants could play.

The third group of findings suggest practical outcomes in terms of opportunity for accounting bodies to take action to improve accounting practice within the construction industry, addressing accounting standards, and a knowledge translation framework.
There are multiple social systems within the construction industry (see chapters 5 and 6). Practical solutions to structural and cultural reform must embrace a systems approach. This study recommends a community of action research be established for the construction industry to implement the policy and practical outcomes outlined in this chapter.

Finally, the fourth group of findings presents the theoretical outcomes. The study contributes to CAT by advancing our understanding of organisational power and politics, and its impact on the role of accounting. Critical study of accounting aims to comprehend the social contexts within which accounting issues exist. This approach examines how accounting may serve a useful social purpose and how its practice may be continually improved. The study explores the role of accounting in legitimising an industry characterized by unlawful behaviour. The findings show that accountants were placed under considerable pressure by other industry stakeholders to become involved in seven unlawful behaviours. The study provides evidence that accounting is a subjective rather than objective practice. It concludes with recommendations about how accounting practice may be improved to repair legitimisation in an industry that appears to ignore public interest.
CHAPTER 8: CONCLUSIONS

8.1 Introduction

This chapter provides a conclusion to the thesis and proceeds as follows. Section 8.2 presents a summary of the chapters, outlining the historical narrative of the construction industry focusing on the period of the RC (2001-2003), and the role of accountants in the unlawful activities identified by Commissioner Cole. Section 8.3 revisits the research questions (initially proposed in section 2.4) and summarises the response to those questions. Sections 8.4, 8.5, and 8.6 discuss potential contributions in terms of theory, methodology, and substantive practice. Section 8.7 identifies limitations to the study. Section 8.8 suggests areas for future research, and section 8.9 offers concluding comments.

8.2 Summary of Chapters

Chapter 1 presented the foundation for this study. The research background indicated that the current study is important and useful. The primary objective of this study was to examine the underlying conflict between a lawless culture and accounting practices within the context of the construction industry. It provided an opportunity to test accounting’s role as a legitimising process, within the context of the CAT debate of whether accounting practice is objective or subjective. At the beginning of the thesis, it was proposed that accounting may have stood above the unlawful behaviour that was associated with many aspects of this industry’s activities, or it may have succumbed to stakeholder pressures. It set the scene for the exploration of the role of accounting within
this complex industry at a period of time, the 2003 RC, where its lawlessness had become such that society recognised its social contract was breached, and told the industry it would no longer be tolerated.

Chapter 2 explained that the research is an historical narrative of the construction industry in the period 2003-2011, with a primary focus on the period surrounding the RC into the industry and its immediate aftermath (2003-2005). The data collection, analysis, and reporting uses CA and CDA. The study focused mainly on the text contained in (a) the RC (Cole 2003) and (b) the BIT Reports (2004, 2005); along with other publicly available information on the industry and its behaviour. CDA was used to examine the societal and political themes emerging from the CA coding categories. The outcomes of the CDA were examined from a critical accounting perspective, with a particular emphasis on PIT, and ST and LT. The chapter discussed the ‘what’, ‘why’, and ‘how’ of the study. It defined the ‘what’ as the construction industry, with a particular emphasis on the industry’s private and public stakeholders. The ‘why’ explained that the industry is socially and economically important to Australia and its conduct is in the public interest. The ‘how’ outlined the methodology and the theoretical framework used to examine accounting’s role in legitimising this industry. The methodology is an historical narrative embedded case study which uses CA and CDA to find meaning in the RCR. The social reconstruction of the industry and its stakeholders mainly using ST, with some help from LT and PIT, as well as sociology’s SNA theory.

Chapter 3 explained the phenomena under investigation, the ‘what’ in this case study, in more detail, and also its significance, the ‘why’ in this case study. The chapter showed that the construction industry has had a long history in Australia, it is important to society, its structure has created intense competition with small profit margins and a short-term profit focus, and its culture has created a propensity towards unlawful
behaviour. Given this thesis is a historical narrative of the construction industry, it is important to know what happened before the period under focus, 2001 to 2003, to understand some of the factors which led to the social contract breach. The behaviours which led the RC to conclude that the industry was unlawful did not suddenly emerge. These behaviours were embedded in organisational practices, systems, norms and values. By looking at the history of the industry from a sociological perspective, it can be seen why these unlawful behaviours became the norm. The turning point appears to be a change in political ideology, brought about by the emergence of communism and its adoption by union leaders, particularly from the 1950s onwards. The prosperity of the 1960s boosted union membership and strength. The 1970s saw a fundamental shift in the industry’s socio-political landscape with unions taking control and dictating the rules of stakeholder interaction. This evolved in the 1980s and 1990s into a culture that felt those in power could ignore the law and do things their way.

The construction industry has significant economic and social importance. The second paragraph in the RCR explained that the industry “is critical to welfare and prosperity in Australia” (Cole 2003, vol. 1, p. 3). Furthermore, the industry has widespread indirect impact on other sectors of the economy. However, it is not just economically important. In terms of LT, it provides services that make it highly desirable to society. The industry structure which existed prior to the RC was characterised by competition between construction firms (macro-level) and between industry stakeholders (micro-level). These stakeholders were dominated by owners/managers and the trade unions. However, there was a range of internal and external stakeholders involved in the construction industry’s unlawful behaviour. The intensity of competition was so high that it caused dysfunctional behaviour.
Chapter 4 examined the history of the regulation of the construction industry. The purpose of this chapter was to examine society’s expectations of this industry, that is, its social contract, and its behaviour compared with expectations, using the RC’s findings and associated documents. The chapter includes a discussion of what happened after the RC in terms of legislative change and other regulation, including the activities and reports of a new body, the ABCC. The chapter explains the need for regulation of this industry, how this was done, and the industry response.

Chapter 5 reconstructed the social reality of how accountants work within the construction industry from a stakeholder perspective. The aim was to examine the social system that accountants work within this industry. The first findings relate to the nature of social interaction. The construction industry’s social networks were dominated by interaction between a few stakeholders, owners/managers, trade unions, and regulators, who had high density within these networks. The remaining stakeholders, including accountants, had lower density. The research found that social interaction within the construction industry contradicted previous research on network density. High network density was not always a positive factor; rather it often had a negative impact on social relations. This finding is explained further by the different types of interaction between stakeholders identified by this research (see figure 5.1 in chapter 5). It describes the social roles played. Whereas unions play multiple roles as advocates (for members), adversaries (for owners/managers), and whistle blowers (for regulators); owners/managers are negotiators (for staff), and avoiders (for regulators), as well as adversaries (for trade unions); and accountants play the role of providing information and reporting. The study, therefore, contributes to understanding of explanatory mechanisms within SNA theory by explaining that high network density can create
negative social interaction and that this is conceptualised by different social roles which distinguish positional interaction rather than people interaction.

Two measures were used to explain the social behaviour of accountants associated with the unlawful activities identified by the RC: harmony and cohesion. The first measure, harmony, was defined by levels of homogeneity and heterogeneity within the social network. The list of processes associated with the unlawful activities identified by the RC had more homogenous than heterogeneous social networks. Almost two thirds (62%) of the 37 processes listed in table 5.2 in chapter 5 were heterogenous, while about one third (38%) were homogeneous. This finding indicates that accountants’ social networks, defined as the social practice around each process outlined in table 5.2, were more likely to have harmony because they were respected or tolerated by other stakeholders. This was evident in certain unlawful activities including tax evasion, employee entitlements, payroll tax, and inappropriate payments. On the other hand, a significant proportion of accountants’ social networks had disharmony and lacked cohesion because they were seen as outsiders or the enemy. This was evident in phoenix company activities, security of payments, and profit manipulation.

The study here makes an important contribution to SNA theory. Whereas, previous research argues that harmony is a positive social practice, this study’s findings show that it can be a negative factor, particularly if the rest of the network is behaving unlawfully. In these circumstances, traditional measures of harmony such as homogeneity are actually a bad thing because it reveals that accountants, in this case, are accepting of the unlawful behaviour of the others within their social network. Therefore, the finding that two thirds of the accountants’ social networks are homogenous is actually a bad result. It suggests that accountants did comply with unlawful behaviour in the following activities: tax evasion, employee entitlements, payroll tax, and inappropriate payments.
Unlawful behaviour in these activities could not have occurred without accountants’ knowledge and, the findings suggest, without their cooperation. On the other hand, there is some defence for accountants doing the right thing. More than one third of social networks were heterogeneous, which means that accountants were excluded, mainly because unscrupulous individuals knew accountants would not cooperate with their unlawful behaviour. This suggests that in the following activities: phoenix company activities, security of payments, and profit manipulation, was hidden from accountants or their advice was ignored.

The second measure, cohesion, indicates efficient teamwork. It is defined by the democracy of accountants’ social networks in each process. This measures how much accountants’ opinions were listened to by other stakeholders. Almost three quarters (73%) of the 37 processes listed in table 5.2 in chapter 5 were democratic, while about one quarter (27%) were undemocratic. This finding indicates that accountants’ social networks, defined as the social practice around each process outlined in table 2, were more likely to have democracy because they were considered experts or advisors by other stakeholders. This was evident in certain unlawful activities including tax evasion, employee entitlements, payroll tax, and inappropriate payments. At the same time, a significant proportion of accountants’ social networks were undemocratic and lacked efficiency because their opinion was challenged or ignored. This was evident in phoenix company activities and security of payments. Profit manipulation had elements of both but was slightly more undemocratic.

The study makes a further important contribution to SNA theory. Whereas, previous research argues that cohesion is a positive social practice, this study’s findings show that it can be a negative factor, particularly if the rest of the network is behaving unlawfully. In these circumstances, traditional measures of cohesion such as democracy are actually
a bad thing because it reveals that accountants, in this case, are agreeing with the unlawful behaviour of the others within their social network. Therefore, the finding that three quarters of the accountants’ social networks are democratic is actually a bad result. It suggests that accountants did agree with unlawful behaviour in the following activities: tax evasion, employee entitlements, payroll tax, and inappropriate payments. Unlawful behaviour in these activities could not have occurred without accountants’ participation and, the findings suggest, without their agreement.

The findings then presented several social network scenarios which summarised the three measures of accountants’ social practice: interaction, harmony, and cohesion. Fifteen scenarios were presented in section 5.3 summarising accountants’ social behaviour, each illustrating different combinations of the three measures. Of these fifteen scenarios, nine provided evidence for subjective accounting, and six for objective accounting. Overall, the analysis provides support for the argument that accounting is a subjective practice.

The analysis identified four types of social practice involving accountants and other stakeholders in the construction industry, which was conceptualised as four quadrants: trust, police, isolated, and hostile (see figure 5.2 in chapter 5). The four quadrants are identified based on the three themes of interaction, harmony and cohesion used as the analytical framework for this section.

In summary, the chapter provided understanding of the relationships within the construction industry. It provided evidence for the managerial perspective of ST which argues that management will be likely to respond to the expectations of particular (typically powerful) stakeholders. The results do not provide evidence for the ethical perspective argues that all stakeholders should be treated equally and that the (economic)
power of various groups should not allow them to have differential influence over the firm. The outcome of this analysis is the social contracts which are ‘negotiated’ with different stakeholder groups. The results argue that accounting is a subjective rather than objective process. Ideally, the seven unlawful activities mapped in figure 5.3 in chapter 5 should be in the top right hand quadrant, trust, and accountants should be working closely with other stakeholders to ensure these activities are performed lawfully. Unfortunately that was not the case in the construction industry. In chapter 6 the two remaining stakeholder constructs, impact and expectations, were examined to understand why accountants behaved this way and the outcomes in terms of the different social contracts.

Chapter 6 continued to reconstruct the social reality of how accountants work within the construction industry from a stakeholder perspective. The aim is to examine the social system that accountants work within this industry. The first findings relate to use of power by stakeholders within the construction industry. Construction companies operated under tight profit margins and were often under financial pressure to be profitable and solvent. Individuals, including owners/managers and accountants would also have felt job insecurity in an industry where companies regularly went out of business. On the other hand, trade unions had long-term interests to improve the working conditions for their members. They were able to use political behaviour to exploit the short term interests of others.

The study makes a further important contribution to SNA theory by using causes of power to explain political behaviour contributing our understanding of the construct, impact. The analysis produced these findings. The first battle for power between stakeholders was owner/managers and unions. In this battle, the trade unions used coercive power by threatening to expose employers to regulators. The most common
threat was to expose tax evasion. There was evidence of the level of threat posed by the trade unions by the use of language such ‘go down the tube’. The trade unions leveraged the short-term focus of owners/managers by reminding them of the consequences if they did not comply with union demands, that is, business closure, which re-enforced the threat.

What was the role of accountants in this political behaviour? Accountants had expert power based on their financial management capability. This provided them with opportunities to be advisors and even decision makers within construction companies regarding the seven activities listed as unlawful by the RC. However, this expert power had differing influence on other stakeholders. Chapter 5 showed that accountants were often shown respect and tolerance (heterogeneity), as well as being allowed to participate in decisions (democracy). However, they were also excluded as outsiders or enemies (homogeneity) and their opinions were challenged or ignored. Therefore, while they had expert power, this was not always enough to over-ride the reward power of owners’/managers who had the fundamental short term power of hiring and firing.

The findings indicate that two types of power dominated relationships between stakeholders in the construction industry: reward power and coercive power. The main problem was the need for reward. In an industry with tight profit margins and the constant threat of business closure, owners/managers and employees were always focusing on the short-term and survival. The trade unions, on the other hand, were aware of the vulnerability of owners/managers and used coercive power to try to address their long-term goal to improve working conditions in the industry. A way forward would be to decrease the reward power of owners/managers. This would reduce employees’ need for reward and the need for trade unions to exercise coercive power. This might be
achieved by getting all stakeholders to adopt a long term perspective which embraces the viability of the industry as a whole rather than competing at the expense of one another.

The main societal expectations of the construction industry were: first, contribute to public funds, second, pay employees their entitlements, third, pay suppliers their entitlements, and fourth, provide accurate performance reporting (see section 6.3.1 for explanation). Commissioner Cole was scathing in his criticism of the construction industry’s unlawful behaviour. While he is often highly critical of unions and sympathetic towards employers, he concludes that “every participant bears some responsibility” (Cole 2003, vol. 3, p. 211). Accountants played a role in the social contract breaches found in this chapter 6.

Chapter 7 developed a preliminary conceptual model on the role of accounting as a legitimisation process, based on the findings presented in this study. There were four groups of findings: first, the role of accounting, second, policy outcomes, third, practical outcomes, and fourth, theoretical outcomes.

In the first group of findings, several questions were explored. Why do accountants act subjectively rather than objectively when doing their work? By subjectively, it is meant that accountants have scope to act independently of the accounting standards; that is, to use their own judgment, intuition, experience, or organisational context to adapt the standards. By objectively, it is meant that accountants always follow the standards. This study has shown that accountants in the construction industry acted subjectively. They did this because accounting allows scope for what is called creative accounting. Why did accountants in the construction industry become involved in activities they should have known were unlawful? This was explained in chapter 6 by the pressure placed on accountants by other stakeholders (see the section on impact). Despite this, accountants
still have free will and choice about how they behave. To understand this behaviour, accountants’ motivation was explored. Accountants’ interaction with construction industry stakeholders was personal and impersonal. It was personal in the sense that accountants interacted socially with others in doing their work and in helping others find meaning and interpretation in their work outputs, that is, their reports. On the other hand, interaction was impersonal in the sense that the work produced by accountants would have been read and interpreted by others without any personal contact with the accounting staff that produced the report. This different interaction is explained by the type of work output, internal versus external, and the type of decision.

In the second group of findings, the study provides regulators with information about the social practice of accounting which might be used to improve regulation of the industry. This could be done by empowering accountants to act as internal regulators. Given much of the industry’s unlawful behaviour occurs due to poor or inappropriate financial management, improved accounting practice in the industry could help restore public confidence and repair legitimation.

Policy improvements could be led by the lead regulator within each unlawful activity:

- For payroll tax, the lead regulator is the Australian State and Territory Revenue Offices.
- For employee entitlements, the lead regulator is Fair Work Commission and the Fair Work Ombudsman.
- For inappropriate payments, the lead regulator is Australian Industrial Relations Commission.
- For security of payments, the lead regulator is the BCISP Act 1999 in all States and Territories, apart from Western Australia and the Northern Territory, where
regulation is by the CC Act 2004 and is administered by various bodies in each State and Territory, for example, the Office of Fair Trading in NSW.

- For phoenix company activities, the lead regulator is the Australian Securities and Investments Commission (ASIC).
- For profit manipulation, the lead regulator is Australian Securities and Investments Commission (ASIC).
- For tax evasion, the lead regulator is the ATO.

The chapter examined the current regulation of the construction industry, areas for improvement, and the role accountants could play.

The third group of findings provide practical outcomes in terms of opportunity for accounting bodies to take action to improve accounting practice within the construction industry, addressing accounting standards, and a knowledge translation framework. There are multiple social systems within the construction industry (see chapters 5 and 6). Practical solutions to structural and cultural reform must embrace a systems approach. This study recommends a construction industry community of action research be established to implement the policy and practical outcomes.

Finally, the fourth group of findings presents the theoretical outcomes. The study contributes to CAT by advancing our understanding of organisational power and politics, and its impact on the role of accounting. Critical study of accounting aims to comprehend the social contexts within which accounting issues exist. This approach examines how accounting may serve a useful social purpose and how its practice may be continually improved. The study explores the role of accounting in legitimising an industry characterized by unlawful behaviour. The findings show that accountants were placed under considerable pressure by other industry stakeholders to become involved in seven unlawful behaviours. The study provides evidence that accounting is a subjective
rather than objective practice. It concludes with recommendations about how accounting practice may be improved to repair legitimisation in an industry that appears to ignore public interest.

Whereas section 8.2 summarizes the research findings by chapter, section 8.3 summarizes the research findings by research question. These 16 questions were posed in section 2.4 – research objectives. They were then discussed in the context of each chapter summary, thereby linking the findings by chapter and by research question. Section 8.3 organizes the discussion of the research questions in terms of the two broad themes, pre and post RC. Theme 1 – What Led to the RC (up to 2003), explained why and how society intervenes in business activity. In this study, it was used to explain why the regulator, the Federal Government, felt it needed to take action to improve behaviour in the construction industry. It is also used to explain the types of regulation used by the Government and accounting bodies. This theme includes research questions 1 to 9. Theme 2 – Post RC (after 2003), explained why and how non-compliance with the social contract occurs and the response of industry stakeholders. This theme includes research questions 10 to 16.

8.3 Research Questions

The research questions are outlined below followed by a brief discussion of the research findings for each question.

Theme 1 – What Caused the Royal Commission (up to 2003)

1. Why was the construction industry sufficiently important for the Australian Federal Government to launch a Royal Commission? (chapter 3)
The construction industry has significant economic and social importance. The second paragraph in the RCR explained that the industry “is critical to welfare and prosperity in Australia” (Cole 2003, vol. 1, p. 3). Furthermore, the industry has widespread indirect impact on other sectors of the economy. However, it is not just economically important. In terms of LT, it provides services that make it highly desirable to society (Suchman 1995, p. 574). It provides essential residential and commercial accommodation, as well as infrastructure essential to society and it also improves the standard of living.

2. Why did the Federal Government choose to conduct a Royal Commission into the construction industry? (chapter 4)

The Australian Government’s main interest in the construction industry was concern that it was not operating productively. In other words, it was not using the resources allocated to it by society in an effective manner. The lack of productivity meant that there were market inefficiencies, capital and other resources, such as labour, not being used by society in a way that met its best interests.

There was another serious concern for government. Many of its constituents were being directly affected by the industry’s behaviour. As the second Business Industry Taskforce Report (Hadgkiss 2005) stated, many Australians seeking an honest living, both business owners (contractors) and workers, suffered social inequities such as financial hardship, job loss, violence, and intimidation, as a result of behaviour in the construction industry. It was in the public interest that this behaviour, stop.

The construction industry did not always misbehave. The industry began with a strong sense of social justice, and the friendly societies in the period 1790-1820 created a benevolent culture based on sharing and support for the less fortunate. The industry’s culture changed in the 1900s as the friendly societies became trade unions. The
relationship between employers and employees became more adversarial. The 1930s marked the most dramatic change in behaviour of the unions, as communism infiltrated the union movement, and people with communist ideology assumed leadership. From this period, the unions became increasingly militant and aggressive in negotiating demands from employers on behalf of their members.

3. Did regulation of accounting practice in the construction industry act in the interests of the public or its constituents? (chapter 7)

The RC findings and recommendations covered a range of cultural and structural reform. However, they focused mainly on owners/managers and trade unions. There was no specific mention of changes to accounting practice or improved regulation. Therefore, this question was not examined in the main historical narrative of the thesis, that is, chapters 5 and 6. However, chapter 7 provided guidelines emerging from this thesis which could improve the role of accounting in legitimising the construction industry.

4. Why does the construction industry need to be perceived as legitimate? What resources are conferred as a result? (chapter 3)

Legitimacy is “a generalised perception or assumption that the actions of an entity [organisation or industry] are desirable, proper, or appropriate, within some socially constructed system of norms, values, beliefs, and definitions” (Suchman 1995, p. 574). It is considered essential because it means society agrees to allow the organisation or industry access to necessary resources for survival. These resources could be any factor of production such as raw materials, land, office, retail or manufacturing space, and employees. Legitimacy is a status conferred upon by society, in other words, it has to be earned. The construction industry has access to the input factors it needs for production
which includes staff, building materials, technology, and finance. Society might deny construction companies access to these resources if it engages in illegitimate activity.

5. What criteria does society set in adjudging legitimate status? How can it be known if the industry is legitimate? (chapter 4)

Two scenarios were presented to explain why the regulator, the Federal Government, increased its regulation of the industry and led to the RC in 2003. The first scenario, IIS, is where the regulator suddenly loses patience does not explain what happened, because the Government had a history of enquiries and action to discipline the industry, particularly the unions.

The second scenario, DSS, more accurately explains what happened. The analysis of the government enquiries shows that the regulator was unsatisfied with the behaviour of the construction industry for at least a decade before the RC. Therefore, the social contract breach was not something that was hidden and suddenly emerged. The catalyst was probably the Four Corners media investigation, which gave wide public exposure to the behaviour of the trade union officials within the industry. While the information provided by the media investigation was not new, it highlighted for many people the seriousness of the cultural problems within the industry. The CDA of the Four Corners transcript shows a blatant disregard for others’ opinions, that is society, and suggests some of the union officials saw themselves a law unto themselves. The lack of respect for society opinion showed a disregard for the social contract. It suggested some union officials did not care what society expected. The self-interest of some individuals was further highlighted by the union in-fighting. The pursuit of power was not limited to conflict between stakeholders, it occurred within the unions themselves. The publicity
surrounding this media report suggested to the Government that they must act and that society would no longer tolerate the industry’s behaviour.

In terms of LT, the construction industry’s behaviour was considered no longer proper or appropriate. While its services were still desirable, the benefits provided were outweighed by the costs of the inappropriate behaviour. Society, through Minister Abbott and the Australian Federal Government, indicated it was unhappy with the construction industry’s behaviour and launched the RC to investigate the size and true nature of the social contract breach.

6. What processes does society expect of the industry to close the legitimacy gap?

What information or disclosures are required to measure legitimacy? (chapter 4)

The CDA shows that the PM’s Statement announcing the RC was conservative in its use of language (see significance) but critical of the range of activities involved in the social contract breach. It clearly identifies the unions as being at fault but also includes, implicitly, management and sub-contractors. The connections reveal illegality, inequity, and lack of accountability as the important themes in this document. The Government wanted to communicate to the industry that it would not tolerate this behaviour any further (see deter) and that it wanted to introduce fairness and accountability to the industry, particularly in terms of industrial relations and funds management and disclosure. Accounting is implicated in terms of the latter point.

In terms of the individual CDA themes, the following conclusions were drawn. First, the analysis distinguishes between explicit and implicit social contract expectations. Explicit expectations are legal requirements, for example legislation or activity required by law (Deegan 2009). The analysis showed what the regulator expected of the construction
industry in terms of the law, and why these expectations were not being met. The main issues were industrial relations and employment practices, where the language used by the PM’s statement suggests connections of illegality and inequity. It allocates identities as union leaders being villains and workers and employers as victims. Implicit expectations are areas outside the law but still deemed desirable by society (Deegan 2009). The main issue here was financial disclosure, where the language used by the PM’s statement suggests connections of unaccountability. It uses strong words to describe the significance of this behaviour, failure, and allocated identities in terms of management doing deals. It did not identify accountants specifically. However, financial disclosure is an activity that involves accountants, so they are implicated.

Second, the analysis distinguished between pragmatic and moral motives. It showed the regulator’s perception about why the construction industry misbehaved. Pragmatic motives are self-interest, for example profit (Deegan 2009), which led to corruption. Moral motives involve responsibility, desire to do the right thing, for example good corporate citizenship (Deegan 2009), which involved appropriate use of funds. In both cases, the language used by the PM’s statement suggests connections of illegality. The identities were all those with self-interest, and while union leaders were implicated, the language is cautious, using the word ‘inappropriate’. Deegan (2009) identifies a third motive, cognition, which is shared mental models, for example peer group pressure, norms, or just the way things are done in the industry. This involves the cultural problems later identified by the RC report in 2003, however, at that stage the PM’s statement did not specifically use language regarding cognition, possibly because the cultural behaviours were unknown at that time.

Third, the analysis explained the legitimacy gap, in terms of expectation change; how society expectations have changed over time, current requirements which were different
from the past; and organisational shadow, when previously unknown information about an industry or organisation becomes known (Deegan 2009). The analysis showed that the language in the PM’s statement identified expectation change as the main factor. As a result of the regulator perceiving the construction industry was not meeting its social contract, both explicitly and implicitly, and the nature of the industry’s pragmatic and moral motives, the government required changes to the way the industry was being regulated. The connections were about prevention and the regulator wanted identity as taking charge. However, the sign symbols showed that the regulator’s history of powerlessness showed it was dis-privileged in terms of the socio-economic power inequities amongst construction industry stakeholders. While the PM’s statement suggested the regulator wanted a relationship with the industry where it was a watchdog with a policing role, the social reconstruction of the reality of the industry at the time was that the regulator was often ignored.

7. How did the construction industry perceive its role as a corporate citizen? (chapter 4)

The RC lays the blame for the social contract breach mainly with the unions and for the reasons of self-interest and lack of fear of consequences. However, blame may be shared amongst all stakeholders. The ultimate cause of the industry’s behaviour is competition and profit. Industry structure meant intense competition, tight profit margins and a short term focus. Customers were demanding and wanted projects to finish on time and on budget. The unions were aware of these pressures and used them to their advantage. They set themselves up as the industry regulator, interested in the long term, due to their concerns for employment of their members. The sustainability of the industry was the unions’ goal because it meant safe and secure long term employment for members. They used tight profit margins and contractors’ need to meet time schedules demanded by
customers to negotiate a powerful industry position. They knew that industrial action would lead to delays, projects over-schedule, and unhappy customers. They used this to coerce contractors to cooperate with their self-interests in return for no industrial action. It was essentially industrial blackmail according to the RC. This assists our understanding regarding the nature of the social contract breach, that is, why and how the industry misbehaved.

Evidence that the construction industry did not wish to repair its public image and seek to regain legitimacy status is provided in the previous sections. The evidence comes in two forms: the continued unlawful behaviour found by the BIT after the RC was completed and the creation of various regulatory measures (for example legislation) and authorities since the RC.

There were clear signs that the union leaders actively sought to maintain unlawful behaviour. Indeed, rather than seek to regain legitimacy status, union leaders openly defied the Government and sought to challenge the laws imposed on them. The second BIT Report cites evidence that unionists “continue to break these laws” and other examples of civil disobedience (Hadgkiss 2005, p8). Rather than seek legitimacy, the tactic of the unions was to continue to challenge social expectations by often breaking the law.

On the other hand, there is considerable evidence in the second BIT Report that some contractors tried to repair legitimacy by standing up to the unions (Hadgkiss 2005). The contractors employed the communication tactic, explain how you are doing what society expects, by reporting efforts to confront the unions to the BIT. These actions were then communicated to the broader public by the BIT Report. However, these actions did not work. The BIT Report lists several tragic stories of contractors facing bankruptcy or
substantial financial loss as a result of trying to stand up to the unions. Most accepted the unlawful behaviour as necessary if they were to survive, after trying to behave according to society’s expectations and it failed.

8. How did society perceive the industry’s role as corporate citizens? (chapter 4)

LT is used to interpret the RC’s main recommendations for cultural change in the construction industry. LT examines three aspects of the recommendations: social contract, breach, and legitimacy gap. Social contract explains the ‘what’, in terms of what society expected from this industry. Breach explains the ‘how’, in terms of the behaviour that the regulator found unsatisfactory. Legitimacy gap explains the ‘why’, in terms of the reasons for the gap occurring.

The analysis showed that explicit expectations required industry stakeholders to follow appropriate legislation as law (statute), being aware of the consequences of illegal behaviour (law enforcement); while implicit expectations involved cultural change essentially related to fair work practice and employee empowerment and freedom. The breach explains why society felt the industry was not fulfilling its contract, that is, why it was misbehaving. The analysis shows that there was bullying, inadequate financial management, disempowerment, conflicting relationships, unfair workplace practices, industrial disputation, and unsatisfactory law enforcement. The legitimacy gap explains how this situation has occurred and how the industry behaviour came to differ from society’s expectations. The analysis shows that there was a culture of industrial pressure which led to organised financial mismanagement; failed moral responsibility to do the right thing by society and the owners of the resources conferred by society; and a shared cognitive denial of freedom of individuals to act without fear of consequences.
9. What was the nature of the social contract between the construction industry and Australian society? What did society expect from this industry? (chapter 4)

Society’s expectations of the construction industry may be understood from two perspectives:

1. Explicit: legal requirements, for example legislation or activity required by law

2. Implicit: areas outside the law but still deemed desirable by society

Society’s legal requirement of the construction industry is what is explicitly stated by law, that is, legislation or other legal document, and endorsed by Government as the representative of the society in which the industry operates. This assists our understanding regarding what society expected of the industry, that is, what was social contract.

Using the CDA to examine the RC’s view of the social contract, the language used is assertive and prescriptive. The significance of the RC’s recommendations is highlighted by the phrase requires significant cultural change. The desired activity is the rule of law. The politics are individual freedoms. The sign system is that the recommendations will privilege all sectors of the industry. The legal expectation, therefore, is that industry stakeholders need to change their cultural behaviours to abide by the law and give all individuals their freedom to act in accordance with the law without unfair workplace pressure. In order to achieve cultural change, the recommendations included establishing an authority to police the industry’s behaviour, with sufficient power to punish unlawful behaviour, and that the consequences of unlawful behaviour be clearly communicated to all stakeholders. Commissioner Cole’s frustration is evident throughout the RCR; with
industry participants but also with the lack of capacity for authorities to deal with unlawful behaviour.

Implicit requirements in the social contract are those that are desirable but not enforceable by law. A cynical perspective might argue that the industry’s social contract prior to the RC was entirely implicit because it did not seem enforceable by law. However, the regulator had established a legal framework, as far back as 30 years before the RC, with the Workplace Relations Act 1974 and the Trade Practices Act 1974, which aimed to provide the legal tools to deliver industry reform. Therefore explicit requirements did exist. Implicit requirements are more related to moral motives, for example a sense of doing the right thing. Commissioner Cole’s recommendations include the implicit requirement of attitudinal change. Attitudes are difficult to monitor and perhaps impossible to police. However, attitudinal change was essential if cultural change was to be successful.

The RC outlined the social contract in explicit terms by requiring industry stakeholders to follow appropriate legislation as law (statute), being aware of the consequences of illegal behaviour (law enforcement), and only dealing with union officials with proper accreditation and behaviours. Implicit expectations involved cultural change essentially related to fair work practice and employee empowerment and freedom. These themes would carry on throughout the next decade of regulation of the industry.

10. How did the construction industry’s stakeholders interact with accountants? (chapter 5)

The construction industry’s social networks were dominated by interaction between a few stakeholders, owners/managers, trade unions, and regulators, who had high density within these networks. The remaining stakeholders, including accountants, had lower
density. The research found that social interaction within the construction industry contradicted previous research on network density. High network density was not always a positive factor; rather it often had a negative impact on social relations. This contradiction with previous research is explained by differences in interacting with people and positions. When interacting with people, high network density will often lead to positive social interactions, as individuals get to know one another and build a sense of trust and reciprocity. However, when dealing with positions, the individual becomes somewhat obsolete, particularly in adversarial situations such as the construction industry. People see the person they are interacting with as being from management or from the trade unions and they immediately adopt an adversarial position irrespective of their frequency of interaction. Their positions mean they are not allowed the opportunity to like each other on a personal level.

This finding is explained further by the different types of interaction between stakeholders identified by this research. It describes the social roles played. Whereas unions play multiple roles as advocates (for members), adversaries (for owners/managers), and whistle blowers (for regulators); owners/managers are negotiators (for staff), and avoiders (for regulators), as well as adversaries (for trade unions); and accountants play the role of providing information and reporting. The study, therefore, contributes to understanding of explanatory mechanisms within SNA theory by explaining that high network density can create negative social interaction; and this is conceptualised by different social roles which distinguish positional interaction rather than people interaction.

The findings then presented several social network scenarios which summarised the three measures of accountants’ social practice: interaction, harmony, and cohesion. Fifteen scenarios were presented, each illustrating different combinations of the three
measures. Of these fifteen scenarios, nine provided evidence for subjective accounting, and six for objective accounting. Overall, the analysis provides support for the argument that accounting is a subjective practice. A conceptual framework was designed incorporating the three SNA measures, interaction, harmony and cohesion, into a two dimensional matrix with four quadrants. These quadrants summarise the social practice of accounting in the construction industry in terms of trust, police, isolation, and hostility. The seven unlawful activities identified by the RC were mapped onto this matrix, with two, tax evasion and employee entitlements, being in the trust quadrant suggesting they are the most serious concerns for accounting practice because accountants were most likely to be cooperating with unlawful behaviours in these activities.

11. What is the willingness of the construction industry’s management to listen to various stakeholder groups and adjust their behaviour accordingly? Who had the power in this industry? What power did accountants have? (chapter 6)

Accountants had expert power based on their financial management capability. This provided them with opportunities to be advisors and even decision makers within construction companies regarding the seven activities listed as unlawful by the RC. However, this expert power had differing influence on other stakeholders. Chapter 5 showed that accountants were often shown respect and tolerance (homogeneity), as well as being allowed to participate in decisions (democracy). However, they were also excluded as outsiders or enemies (heterogeneity) and their opinions were challenged or ignored. Therefore, while they had expert power, this was not always enough to override the reward power of owners'/managers who had the fundamental short term power of hiring and firing.
The findings indicate that two types of power dominated relationships between stakeholders in the construction industry: reward power and coercive power. The main problem was the need for reward. In an industry with tight profit margins and the constant threat of business closure, owners/managers and employees were always focusing on the short-term and survival. The trade unions, on the other hand, were aware of the vulnerability of owners/managers and used coercive power to try to address their long-term goal to improve working conditions in the industry. A way forward would be to decrease the reward power of owners/managers. This would reduce employees’ need for reward and the need for trade unions to exercise coercive power. This might be achieved by getting all stakeholders to adopt a long term perspective which embraces the viability of the industry as a whole rather than competing at the expense of one another.

12. What is the social contract the construction industry’s stakeholders had with accountants? (chapter 6)

The main societal expectations of the construction industry were:

First, contribute to public funds. This was an expectation that construction companies would meet their corporate citizenship responsibilities and pay taxes. In this way, they would contribute to the funds gathered by government to be shared with all of society through government services. Tax evasion was the main problem in this area, but phoenix company activity was also a problem.

If it is accepted that accountants must have played some role in these activities (see chapter 5), then it may be concluded that accountants breached their social contract and may have bent the rules, that is the accounting standards, in their work with company directors involved in these activities. However, accountants’ social contract may have been unreasonable in this case. Evidence on how difficult it may have been for
accountants to change phoenix company activity, for example, is provided by how
difficult the regulators found it to police unlawful behaviour. Anderson (2012) explains
how frustrated the Federal Government was with continued phoenix activity six years
after the RC. If the ATO felt powerless to enforce the law regarding phoenix activity,
how could accountants employed by the construction industry have felt any differently?
This evidence suggests that accounting practice regarding phoenix activity had not
changed based on two assumptions. First, phoenix activity was actually increasing in the
period after the RC. Second, accountants were unlikely to have the authority or
disincentives to prevent fraudulent phoenix activity. Therefore, it is concluded that there
were no observable changes to accounting practice regarding phoenix activity in the
period after the RC. Accounting may be considered a subjective practice in regards to
phoenix company activity. It was unable to stand above this activity and to enforce
accounting standards to prevent fraudulent phoenix activity. Accountants employed by
the construction industry were most likely applying subjective judgements in their work
associated with phoenix activity depending upon the amount of pressure exerted on them
by others, for example the company directors.

Second, pay employees their entitlements. This was an expectation that individuals
employed by construction companies would receive their salary and non-salary reward
for their work. Underpaying employees or avoiding payment altogether through
insolvency was the main problems in this area. In an industry with intense competition
and small profit margins (see chapter 3), owners or investors and management would
have been under pressure to reduce expenses and improve profitability. Given
entitlements are an expense in the IS it is easy to see how underpayment of employee
entitlements would have occurred in these operating conditions. The social contract
breach affected relationship between owners/managers and staff in three ways. First,
employees pretended to be contractors. Second, was the use of cash payments. Third, was the use of pyramid subcontracting. These issues illustrated the systemic structural and cultural problems in the construction. This is a significant social contract breach. Society expects organisations to pay staff what they are entitled to. Australian culture has a legacy of ‘getting a fair day’s pay for a fair day’s work’, which was discussed in chapter 3 in the history of the trade union movement. The consequences of non-compliance and underpayment of employee entitlements, is that society suffers, through the financial impact for employees who do not receive their full entitlements. Yet, it was not just about underpaying staff. The industry developed systemic ways of avoiding its social contract with a deliberate intent to breach this contract and avoid its moral and ethical obligations to pay people what they are entitled to. Given the high involvement of accountants in employee entitlements (see chapter 5), they must accept responsibility for participating in this systemic breach of social contract.

Third, pay suppliers their entitlements. This was an expectation that companies and individuals who provide materials and services to construction companies, including sub-contractors, be paid appropriately in return. There were two types of payment issues associated with the unlawful behaviour within the construction industry identified by the RC. First, delaying or withholding payments in the normal course of completing a construction project. Second, delaying or withholding payments as the result of business failure, that is, liquidation. These payment issues had a significant impact on security of payments.

Fourth, provide accurate performance reporting. This was an expectation that construction companies would honestly and accurately report on their business activities, including profit reporting. Society includes public and private investors; as well as other stakeholders interested in the financial position of construction companies such as
customers, creditors (for example, banks), suppliers, and regulators. These stakeholders want to know if they will get a return on their investment, have their building project completed, and whether they will be paid. Profit manipulation was the main problem in this area. The consequence of profit manipulation is significant because the financial position and the results of operations do not fall into fair presentation of financial results. This means that the profit reported will not represent the long-term capacity of the firm to generate earnings. It is misleading the public. However, profit manipulation is not considered to be fraud. It is a matter of interpretation. This indicates that accountants engaged in profit manipulation are perhaps behaving inappropriately, particularly if their interpretation does not involve honest mistakes, that is, it is intentional; but it is not illegal, unless they engage in fraudulent activities. There is a grey area between creative accounting and deliberately misleading the public by providing false information. Accountants involved in profit manipulation in the construction industry might argue they were simply trying to serve the best interests of their company, for example creative accounting. Chapter 5 also found that this activity typically excluded accountants wherever possible, that is the relationship with stakeholders was hostile because they were seen as the enemy. Therefore, profit manipulation is the area where accountants would be seen as having the least contribution to the social contract breach. It may also be argued it was an area where they were placed under the most pressure by owners/managers using reward power to coerce them. It is certainly evidence that accounting is a subjective rather than an objective process.

Commissioner Cole concluded that “every participant bears some responsibility” (Cole 2003, vol. 3, p. 211). Accountants played a role in the social contract breaches found in this chapter.
13. What measures of legitimacy were imposed by the Royal Commission on the construction industry? (chapter 4)

Chapter 4 showed that explicit expectations required industry stakeholders to follow appropriate legislation as law (statute), being aware of the consequences of illegal behaviour (law enforcement), while implicit expectations involved cultural change essentially related to fair work practice and employee empowerment and freedom. The measures of legitimacy were also defined by the social contract breach because Commissioner Cole specified the inappropriate behaviour society expected the construction industry to change: bullying, inadequate financial management, disempowerment, conflicting relationships, unfair workplace practices, industrial disputation, and unsatisfactory law enforcement.

Further evidence to support these findings is provided by the RC Recommendations listed below.

1. The building and construction industry in Australia requires significant cultural change. Such change is necessary if the rule of law is to be reintroduced to conduct and activities within the industry, if individuals’ freedoms are to be maintained, and if the industry is to achieve its economic potential. Change is required in the attitudes of all sectors of the industry, including governments, clients, head or subcontractors, industrial organisations and employees.

2. In summary, I recommend that cultural change be achieved by:

   • The Commonwealth Parliament enacting a statute of special application to the industry.
   • Creating a new statutory norm which clearly delineates between unlawful and lawful industrial conduct.
   • Creating a Commission with responsibility for investigating unlawful conduct occurring in the industry.
   • Rendering those causing loss from unlawful industrial action liable for such loss and prosecuting such conduct.
   • Establishing a just, quick and cheap method of assessing and recovering loss caused by unlawful industrial action.
   • Imposing a statutory obligation to report actual or threatened industrial action to the Commission.
   • Providing that only fit and proper persons may hold office in, or exercise official functions on behalf of, industrial organisations.
3. The nature and extent of the unlawful and inappropriate conduct disclosed in the hearings before me and recorded in this report should not continue uncorrected. (Cole 2003, vol. 11, p. 3)

Section 2.4 (chapter 2) in Theme 2 – Post Royal Commission (after 2003) provides the context for these findings. Section 2.4 explained how non-compliance with the social contract can also have a negative impact on the organisation or industry’s market reputation or image (Deegan et al. 2000). In other words, organisations need to see compliance with their social contract important enough to take action. This leads to questions about the RC’s findings and how the construction industry reacted. However, it also raises issues about the regulators’ response. Commissioner Cole was frustrated by the lack of authority allocated to regulators. This is illustrated by his specification about unsatisfactory law enforcement. The study recommended allocating responsibility for policy improvements to the lead regulator in each unlawful activity (see section 7.3.1 and 7.6).

Chapter 7 discusses the research findings and suggest ways that accounting may be used to address these social contract breaches and legitimise the construction industry.

14. Did the construction industry’s non-compliance with the social contract have a negative impact on its market reputation/image? If so, how did this negative impact affect the industry? (chapter 7)

The Federal Government continues to be frustrated with the construction industry and its ongoing social contract breaches. At the time of writing, twelve years after the RC, a Royal Commission into trade union behaviour is underway, including court proceedings against union officials. While these allegations are not proven, it is still reasonable to assume that the regulator has still not successfully reformed the construction industry. The social contract breach remains.
While the regulator is unhappy with the industry, it is difficult to say whether this has had a negative impact in terms of broader society, construction industry customers. People need homes to be built, roads and bridges to be constructed, and companies need offices and factories to be built. This raises questions about the consequences of social contract breach. The ultimate consequence would be that society would deny companies engaging in illegitimate behaviour access to resources. To fully enforce punishment of social contract breach, customers of construction companies could refuse to pay if the company is found guilty of unlawful behaviour. The Government, as a major purchaser of construction services, has the power to deny companies government tenders and building contracts. However, the construction provides a necessary service (see chapter 3) which implies that some behavior may be overlooked. This suggests that social contract breach is able to be addressed only if there are significant consequences for non-compliance. The construction industry appears to carry on with unlawful behaviours because the consequences are not sufficiently serious.

15. What role did accountants play in activities identified as unlawful by the Royal Commission? (chapters 5 and 6)

Accountants were involved in seven unlawful activities identified by the RC. They were involved in 37 processes associated with these activities (see table 5.2 in chapter 5). Their main role was to provide information and reports. However, these processes involved the full range of accounting activities including identification, measuring, communicating, and decision making. For example, the tax evasion activities are mainly measuring, and the profit manipulation activities are mainly communicating. The measurement role mainly involved classification of assets with the aim of reducing the amount of tax payable. In the communication role, the accountant needs to consolidate financial information and produce regular reports (Birt 2010). Therefore, if the
accountant was involved in unlawful behaviour associated with these activities, it mainly involved financial reporting.

When the processes characterised by this behaviour were examined, it is clear that only accountants are qualified to do this type of work, therefore, they took a leadership role in social networks involved in these unlawful activities. This has implications for this study in the examination of the role of accounting. Given the nature of the social behaviour in processes with these characteristics, accountants were heavily involved in these unlawful activities. Given the nature of these activities, the decision makers must have sought the involvement of accountants. The question then emerges: did accountants respond by telling decision makers that they must follow accounting standards at all times? If so, this would support the argument for accounting as objective practice. Or did accountants respond by doing creative accounting to help their employers’ goals? If so, this would support the argument for accounting as subjective practice. The results indicated that accounting was a subjective practice, which meant they responded to pressures exerted by their employers to engage in creative accounting and, at times, inappropriate or unlawful behaviours.

16. Did accountants change their role in the activities identified as unlawful by the Royal Commission after 2003? (chapter 7)

There is no evidence that accountants changed their behaviours as a result of the RC. Chapter 7 provides suggestions on how these behaviours might be changed.
8.4 Theoretical Contribution

The study contributes to CAT by explaining how accounting practice was influenced by stakeholder interests, that is, the construction industry’s political economy. The study’s contribution to PIT is to examine the reasons why regulation of the construction industry was so difficult and to suggest how this may be improved. Furthermore, the study contributes to the PET of regulation reflecting broader cultural and societal values and, in doing so, advances the importance of the role of accounting in legitimising an industry with a long history of unlawfulness. The study contributed to LT by defining the nature of the social contract breach between the construction industry and Australian society, and strategies to repair legitimacy. The contribution to LT was to identify factors creating a situation where some stakeholders’ socio-political power exceeds the public interest, that is, the power of the regulator whereby the industry ignores the need to repair legitimacy. LT’s pragmatic construct explains that the politics in stakeholder relationships were defined by greed, exploitation, and stand-over tactics; while the moralistic construct was characterised by being irresponsible or powerless.

The study contributed to ST from the managerial perspective by exploring how the constructs of relationships, impact and expectations help us understand the social practice of accounting within the context of a social contract breach. The contribution lies in the empirical evidence of the socio-political power inequities defining the social interaction between industry stakeholders which have breached their social contract. The ST constructs of relationships, impact and expectations explain why unlawful behavior emerged in this industry. The study makes several specific contributions to ST. First, it uses the theory of SNA construct of density to explain the social network interaction of stakeholders, contributing to our understanding of relationships. Second, it uses the SNA
construct of heterogeneity and homogeneity to examine behaviour between these stakeholder groups, with a particular focus on their harmony and cohesion, contributing to our understanding of ST’s ethical perspective. Third, it uses types and causes of power to explain political behaviour contributing to our understanding of the construct, impact. Fourth, the study identified four societal expectations to explain the social contract breach contributing to our understanding of the construct, expectation.

8.5 Methodological Contribution

The study contributes to the debate between traditional conceptions of accounting history and new historians. The debate centres around the importance of facts and the pursuit of truth by traditional historians (Funnell 2005, p. 138). Traditional historians aim to agree on the reality of the past and on the relevance of the facts (Himmelfarb 1989). “It has been the traditional historian’s role to seek out the facts of history from hard evidence” (Funnell 2005, p. 135). It is the definition of evidence which might persuade traditional historians to criticise this study. The main source of evidence used by this study is the RCR, along with associated other reports and publicly available information about the construction industry at the period under investigation. However, these documents say little about accountants or accounting practice. The analysis presented in this study infers the role of accounting from this evidence. Traditional historians might argue that this is insufficient. The study should have gathered more evidence, perhaps by interviewing people who worked in the industry at the time. The study acknowledges this is a limitation. However, it defends this criticism on two points. First, it is highly unlikely accountants working in the industry would admit to participating in unlawful behaviour, therefore, the ‘truth’ would have been very difficult,
perhaps impossible, to discover. Second, this study is not about forensic accounting. It
does not seek to find blame or to discover the truth of unlawful behaviour. It does not
even seek to argue that accountants behaved unlawfully. The RC had already
investigated the construction industry’s unlawfulness. Rather, the study sought to
explore the role of accounting as social practice in an industry that placed pressure on
accountants to be subjective.

The study’s approach, therefore, was similar to post-modern historians which have used
historical narrative as a form of “discursive engagement”, which is far from neutral
(Funnell 2005, p. 135). This approach has used the text of the RCR, and the other
associated documents, to allow the researcher to put herself into the minds of the
historical actors, in this case accountants who worked in the construction industry at that
time, and to construct a “readable invention” of the social practice of accounting
(Funnell 2005, p. 135). This allowed the researcher, who has spent most of her career as
a practicing accountant, to find interpretation and meaning in the text of the research
sources, and to reconstruct the social reality of accounting practice in the construction
industry. The researcher has also worked for the construction industry making it easier to
engage with this discourse.

While both the new and old history approaches aim to improve our understanding of the
environment in which accounting operates, they differ in terms of their focus.
Traditional accounting history tends to have a macro-economic perspective, which
places accounting within the broader social context of society and its need for
accounting (for example, see Littleton 1933). The new history of accounting explores the
reflexive relationships between accounting and the socio-political system in which it is
embedded (Funnell 2005, p. 144). New accounting history tends to have a sociological
perspective, which explores accounting as social practice using social theory.
Accounting history has become less econometric and more socio-centric (Funnell 2005, p. 147).

The study contributes to the current rivalry between new and old history in two ways. First, it examines the existence of multiple stakeholders within an industry and not just the political or social elites, in this case owners/managers within the construction industry. Whereas traditional accounting history might have written this thesis from the perspective of those with economic power, that is, owners/managers; the new history approach adopted allows for exploration of stakeholders with little power, such as employees and also accountants, and how this has influenced accounting as social practice in this industry. Second, it questions the role of facts and truth in accounting history. Whereas traditional accounting history has had a pursuit of truth, evidence, and objective knowledge; new accounting history questions the need for such a rigorous approach. New accounting history has a more subjective perspective about events, allowing for multiple truths and even facts, depending upon the lens from which the events are written. This study has illustrated how unlawful activities might be justified from the perspective of one stakeholder, deemed necessary for survival, but criticised by others as unfair or unjust, such as trade unions or employees. History depends upon perspective. The contribution is to advance our understanding of socio-political behaviour from multiple stakeholder perspectives, and to demonstrate that subjective truth and evidence still allows for a realistic portrayal of the truth of social practice. It does this by addressing Funnell’s (2005) guidelines on writing accounting history for new history researchers:

It requires researchers whose primary focus is on the “what” and “how” of history which verifies dates and the specifics of historical chronology, the province of the traditional accounting historians, and those whose overwhelming concerns are to interrogate the historical record and ask “why” or “how did we get into this state?” (p. 147)
This study has embraced Funnell’s challenge. It has asked how did the construction industry breach its social contract and why did accounting allow this to happen.

Social science researchers have been described as taking a ‘hermeneutic turn’, which is a realisation that the knowledge of an event can only be determined through interpretation, and that meaning comes through the interpretation of the researcher (Gaffikin 2008, p. 235). All meaning comes from the interpretation of text, and interpretation is always contextual (Gaffikin 2008, p. 236). When reviewing documents, such as in this study, the context comes from the explanatory power of the knowledge, which varies depending upon the reader. This meaning is created in the relationship, the internal discourse, between the reader and the words written by the writer. The study is an example of how to use the context dependent method to better understand accounting as social practice. It allows us to understand the power of language to interpret the power between stakeholders within the social practice of accounting in the construction industry.

8.6 Substantive Contribution

The study makes a substantive contribution by advancing our knowledge of accounting practice. In his discussion of understanding accounting theory, Gaffikin (2008) explains that research may be undertaken to improve practice. This type of research tends to focus on understanding behaviour. As Gaffikin explains:

This is done to better explain elements of practice or to understand phenomena such that predictions can be made as to their behaviour (Gaffikin 2008, p.5).

From this perspective, the study contributes to the debate over whether accounting is an objective or subjective practice. The results argue that accounting is a subjective
practice. More specifically, it explains how accounting is subjective. Accountants use their judgment and experience to respond to their operating context. In response, they adopt creative accounting to provide solutions to their context. They might also step outside the boundaries of creative accounting and into inappropriate or even unlawful behaviour.

The study also provides findings to predict behaviour by explaining why accounting is subjective. More specifically, chapter 5 explains the relationships involving accountants and other stakeholders. It makes substantive contributions by developing a new theory of social practice, based on the SNA constructs of interaction, cohesion, and harmony (see figure 5.2 in chapter 5). This produced four types of accounting social practice: trust, police, isolation, and hostility. Chapter 6 examined the use of power and politics by other stakeholders to coerce accountants to engage in creative accounting, and sometimes inappropriate or unlawful behaviour. Chapter 6 also mapped the different social contracts between stakeholders as an outcome of this social practice, and how this influences their expectation of accounting practice, that is the social contract for accountants. It finds that accountants will not always behave in ways that society expects, rather they may behave inappropriately if their social contract with their employer requires other behaviours. These findings allow us to predict accounting practice based on the social interaction (roles), use of power and politics (impact), and social contract (expectations).

Gaffikin (2008) also explains that research may be undertaken to understand the role of accounting in inappropriate behaviour. He uses the example of business failure:

This century has already witnessed some of the largest ever business failures. Such failures are not new and not purely the result of poor or inadequate accounting. However, the fact that they exist and seem to be getting bigger is reason to examine what possible role accounting played in these corporate
demises and whether improvements in accounting practices could have assisted in preventing them. In addition, where accountants have been accused of negligent or inappropriate behaviour, what accounting practices could have been developed to prevent such undesirable actions? (Gaffikin 2008, p. 5).

From this perspective, accounting research may make a substantive contribution by examining the role of accounting in corporate disasters. Gaffikin is highlighting breach of social contract in terms of business failure, but the same objectives apply with other inappropriate corporate behaviours such as tax evasion, profit manipulation and the other unlawful activities covered by this thesis. The study provides guidelines for improving the social practice of accounting. It identifies the unlawful activities and whether accountants would be involved in these activities. It defines the accounting processes where unlawful behaviour may exist. Accountants would be aware of these processes and the pressures that may be placed on them when conducting them. Regulators may then focus their attention on these unlawful processes and work with accountants to develop industry self-regulation. The Code of Ethical Conduct expects that accountants do what is referred to as 'the right thing', and this is an expectation of ethical in any profession but perhaps impossible to guarantee in practice. The other difficulty is that in the construction industry, not all accountants are members of the professional bodies and, therefore, do not fall within the scope of the Code of Ethics. The recommendation about accountants self-regulating the industry are, therefore, aspirational and would represent an ideal outcome.

The study makes sense of the complexity of social practice of accounting by developing theoretical frameworks designed to summarise the behaviour, for example see section 5.3. It recognizes the multiple realities of the social practice of accounting; for example section 5.3 identifies fifteen scenarios of social interaction, and four roles for accountants, and chapter 6 identifies numerous socio-power situations (see section 6.2)
and social contracts (see section 6.3). The study reconstructed the social practice of accounting within the construction industry to examine the issue of whether accounting is objective or subjective, and then how to improve the social practice of accounting so that it may benefit society. These goals align with critical accounting research.

### 8.7 Limitations of the Study

The research is limited in several ways. First, there are methodological limitations. The study is a historical narrative. Critics of this method argue that, perhaps out of necessity, narratives are incomplete in the story which they tell and are therefore a weak form of history (Previts, Parker & Coffman 1990). These critics suggest historical narrative researchers should reconsider the way they reconstruct the socio-political context of accounting. This study has tried to address this criticism by embracing the new history accounting method, which explores the historical narrative of the role of accounting in the construction industry from a social practice perspective. However, Funnell (2005, p. 145) raises concerns that if the new history moves too far into post-modernism then narrative “may no longer provide a source of common ground for all accounting historians”. Despite this, Funnell (2005) recognises the need for accounting historians to be open to alternative interpretations. Only then can the discipline ensure it does not digress into “dogmatism” and “intra-disciplinary intolerance” (Funnell 2005, p. 147). This study embraces Funnell’s philosophy and his love of accounting history and is evidence of this tolerance in action. In response, the analysis was spatially and temporally broad, in order to cover the complexity of an industry in breach of its social contract. The main source of data, the RC (Cole 2003), contained 23 volumes. Given this
breadth, it was impossible to incorporate every aspect, and such detail may have detracted from the overall account.

Second, there are theoretical limitations. CAT may be seen as a controversial field. Over the past three decades, a “range of studies have been conducted using alternative theoretical stances and strategies to mainstream accounting research” (Lodh & Gaffikin 2005, p. 155). CAT aims to “develop a more self-reflexive and contextualized perspective on accounting which sees the connections between society, history, organisations, accounting theory, and accounting practice” (Lodh & Gaffikin 2005, p. 156). There are various views of critical accounting including: accounting significance as everyday practice, the role of sectional interests, for example stakeholders in accounting practice, and to apply fresh insights into the effects of accounting. This study is interested in all three perspectives but has the most focus on the second, particularly exploring the role of socio-political power inequities using ST.

Critics of CAT may see limitations in this study from two perspectives. First, those with a socio-theoretical rationality perspective (for example, see Booth 1991) may argue that accounting as social practice is bounded by human rationality, and it may be explained by logical decision making. In the context of this study, this means that accountants should always be objective, that is rational, and that the subjectivity inherent in the study’s discussion of accounting practice in the construction industry, that is subjectivity, is incorrect. The study’s findings argue against this socio-theoretical rationality perspective because it finds that accounting is a subjective practice.

The second limitation relates to Habermas’s distinction between “lifeworld” and the “systems” (Habermas 1988, p. 44). In their discussion of Habermas’s work, Lodh and Gaffikin (2005) propose that the above distinction represents two fundamentally
different ways of approaching the study of society. This is particularly relevant to this study as it is examining the breach of the social contract by the construction industry. These two views seem to be influenced by the researcher’s sense of self and society. The controversy in this debate is how the researcher’s sense of self is made conscious in the methodological approach (Habermas, 1988). Critics may argue that this study is too ‘lifeworld’ and, therefore, too subjective as an interpretation by the researcher of social practice in the construction industry. These critics might suggest a more systems or objective approach would be better. The researcher’s defense is that the researcher has been a practicing accountant for many years, including in the construction industry, and the researcher’s view of the reality of social practice in the industry was influenced by the researcher’s own perceptions. However, this perception was based on a degree of experience which qualified the researcher to reconstruct this reality with some confidence. Despite this, it is acknowledge that it is the researcher’s reconstruction, and the researcher was influenced by the researcher’s own experiences as an accountant.

8.8 Opportunities for Further Research

The historical narrative in this thesis is broad, encompassing a complex industry, substantial data, from the RC volumes, activities, social networks, and social practice. Future research might focus on one or more of these areas to provide further insight. The analysis was based on publicly available information. Future research might involve interviews with individuals involved in the construction industry representing the various stakeholders, to gain further knowledge about motivation, behaviours, and culture. However, as pointed out in the section on limitations, it would be difficult to get
individuals to admit unlawful behaviour, so such research would need to recognise the challenges involved.

There is a promising opportunity to investigate the future of the construction industry and the role of accounting in legitimising the industry. Chapter 7 provided suggestions for accounting emerging from this study. Future research could examine these ideas in more detail, perhaps working with regulators and other stakeholders to explore the implementation of some of the ideas. The construction industry continues to pose problems for Australian society and it has not yet repaired the legitimacy gap first established by the RC in 2003, now more than 13 years ago. It is in the public interest to legitimise this industry. The study has shown that accountants played a role in the unlawful behaviour, but also that accounting may help address the problems, particularly in the financial management of some of the processes associated with the seven unlawful activities identified by the RC. Rather than looking backwards, future research might learn from the lessons of the history presented in this thesis, and look forward, and consider how accounting might improve its role in this industry by implementing some of the ideas presented in chapter 7.

Finally, the study began with an aim to explore the role of accounting, and whether it is an objective or subjective practice. The findings indicate that accounting is a subjective practice. However, the study also found that accounting in the construction industry was too subjective, allowing too much opportunity for creative accounting and even some inappropriate or unlawful behaviour. While this study concluded that subjective accounting is a realistic portrayal of the reality of accounting and indeed necessary due to the pressures placed on accountants by more powerful stakeholders, it also finds that too much subjectivity is undesirable. Future research might consider the following dilemma: how much subjective accounting is too much, and what is the appropriate
balance or tipping point? Chapter 7 argued that steps must be taken to reduce the amount of subjectivity in accounting in the construction industry, moving towards more objectivity. At what point may success be measured? When is the right amount of subjectivity reached?

8.9 Concluding Comments

The thesis has been an interpretative social reconstruction of the construction industry in the period 2001 to 2003, with some following narrative in the period up to 2011. As such, it may only be a partial coverage of this complex topic. The thesis has been shaped by the views of the researcher and the methodology employed. It has adopted a critical accounting approach based on using ‘new history’ narrative to examine the role of accounting from a socio-metric rather than econometric lens. Therefore, it has been interested in people, the industry’s stakeholders, and understanding their behaviours.

The construction industry was characterised by a fierce battle for power between owners/managers and the trade unions. It seems that all other stakeholders, including accountants, were swept up in the momentum of this ongoing conflict. People made conscious decisions to engage in unlawful behaviour. It was so widespread that it had become normal, part of industry and organisational culture, and accepted as common practice. People broke the law routinely to survive. Commissioner Cole was highly critical of the trade unions, but also the owners/managers. However, he felt everyone in the industry shared responsibility for the unlawful behaviours, and that includes accountants.

The thesis did not set out to identify unlawful behaviour or to lay blame. This is not a forensic accounting study. The RC has already investigated the unlawful behaviour. The
study does not attempt to prove that accountants were engaged in unlawful behaviour. Rather, it focused on the role of accountants who operated under extreme pressure by other stakeholders, their employers, in this complex industry. Evidence was presented that seven unlawful activities identified by the RC involved processes normally done by accountants. The study raised important questions about whether accountants were simply engaging in creative accounting in undertaking this work, if so it is evidence that accounting is a subjective practice, or whether sometimes they stepped over the boundaries of acceptable practice, into inappropriate or unlawful behaviour.

In writing this thesis, it has been necessary for the researcher to engage in the story itself. As a practicing accountant for many years, the researcher has considerable experience in dealing with some of the pressures which would have been placed on accountants in the construction industry. Therefore, the researcher has written the thesis with a practical lens, reconstructing the social practice of accounting from a pragmatic perspective, rather than a theoretical perspective. As noted by Gaffikin (1998, p. 633), “it is not possible to separate the past from our perceptions of it. It is through our interpretation that we make the past coherent”. The researcher’s interpretation of accounting practice has influenced this thesis. For example, the identification of processes associated with the seven unlawful activities identified by the RC is an interpretation of how these activities occur and the involvement of accountants. It is based on the work of other researchers, but is also influenced by the researcher’s views of how accounting is practiced. Similarly, the analysis of the relationships between stakeholders and accountants (chapter 5), the use of power and politics and the outcomes of this (chapter 6), and the lessons learned from the role of accounting in this industry (chapter 7), are all influenced by the researcher’s experience as a practicing accountant. While this is a strength, as it provides a realistic, rather than purely theoretical,
perspective, it is also a weakness as it presents only one interpretation of this historical narrative. An owner/manager or trade union official might have a very different interpretation of events, and the role of accountants in this industry.

The thesis concludes with optimism: optimism for the role of accountants, and for the future of the construction industry. It believes that accountants play an important role in legitimising industry and company behaviour and in repairing legitimisation, even in industries with such a significant and long standing breach of social contract as the construction industry. Accountants need to have the power and job security to self-regulate this industry. Regulators might implement some of the ideas presented in chapter 7 and learn from the lessons of history presented in this study. The historical narrative constructed in this thesis is about fear. The construction industry operated, and still operates, with a fear culture. Commissioner Cole described this as conflicting stakeholder interests between the short-term and long term. It is really about fear for survival and employment. Only once this fear culture is addressed and individuals, including accountants, can feel safe in their workplace, can the construction industry achieve reform and be legitimised. Accountants deserve to feel safe in their workplace. Unfortunately, it seems that accountants in this industry did not feel safe, and some, perhaps many, engaged in behaviours they knew were wrong because they felt they had no choice. The future for accounting should be that accountants always have choice. Accountants must be empowered. They deserve to have respect, to be trusted, and to be valued.
APPENDIX 1 THE ACCOUNTING PROCESS

A1.1 Introduction

This section provides a brief overview of the accounting process. The aim is to describe what accountants do, in simple terms, and who they interact with in doing their work. The overview is simple because this study does not seek to reconstruct the social reality of the accounting process in the construction industry. It would be difficult, and perhaps impossible, to reconstruct how accountants employed by the industry carried out their work during the period of the RC. To do so would probably require interviews with accountants who worked in the industry at that time and access to accounting documents, which would be very difficult when Commissioner Cole found it difficult to get industry stakeholders to cooperate with his investigations. Rather, the study seeks to reconstruct the social reality of the ‘role’ of accountants employed by the construction industry. This investigation of the role of accountants aims to examine whether accounting was an objective or subjective process within the overall social reality of what was happening in this industry.

In exploring whether the accounting process was objective or subjective, chapter 6 placed the activities identified by the RC as misbehaving, for example tax evasion, within the context of the accounting process. The purpose is to situate the unlawful activities within the day-to-day operations of accountants. As stated above, the truth of how accountants behaved on a daily basis cannot be known, but it is possible to infer their role in these misbehaving activities from two perspectives. First, by generalising about the processes that accountants normally do, this may be linked to the misbehaving
activities by concluding whether accountants would normally become involved in these activities, tax for example, as part of normal duties. This allows the study to draw conclusions about the possible level of accountants’ involvement in these misbehaving activities which will be explored in later sections in this appendix. Second, by generalising about the nature of accountants’ interaction with stakeholders, inferences may be made about the socio-power political inequities in accountants’ relationships within the construction industry. This allows the study to draw conclusions about whether accountants were playing an objective or subjective role in these misbehaving activities, which was also examined further in chapter 6.

Accounting can be defined as a process of identifying, measuring, and communicating economic information about an entity to a variety of users for decision making purposes.

Accounting information is designed to meet the needs of both internal and external users. As discussed in chapter 2, the construction industry has a range of internal and external stakeholders. All of these are potential users of accounting information. Accounting researchers typically examine the interaction of accountants with stakeholders in terms of decision making. Accountants’ interaction, therefore, may be socially reconstructed by looking at how stakeholders use accounting information and the role accountants play in helping them understand and use the information.

Internal users need accounting information to:

1. Make decisions concerning the operations of the business entity.
3. Resource allocation. This involves how best to allocate the entity’s resources.
External users need accounting information to:

1. Assess the entity’s growth potential.
2. Evaluate the entity’s capacity to repay debt and the level of risk involved with lending funds to it.
3. Review the entity’s future prospects.
4. Assess the entity’s profitability.
5. Appraise the tax paid.
6. Evaluate whether management are using the entity’s resources effectively.

Unions, managers, project managers, and accountants are involved in each of the three internal decisions; engineers and human resources are mainly involved in business performance and resource allocation; while other staff are involved in resource allocation and future prospects, external work. In terms of external use, owners/investors are involved in all six decisions; regulators and banks/suppliers mainly involved with debt payment, profitability and taxation; and society is mainly concerned with taxation.

**A1.2 Taxation Process**

Taxation is a complex activity. The first of the seven unlawful activities identified by the RC was tax evasion. It is the not the purpose of this section to provide a detailed analysis of how taxation is done. Rather it aims to explore accountants’ role in company taxation. If accountants are heavily involved, then they may have been also part of tax evasion.

The process for accounting for company income tax involves the following steps: first, recognising the tax base of assets and liabilities, second, treatment of tax losses, and third, minimising tax payments.
In step one, the aim is to calculate a tax base. The BS approach to accounting for taxation focuses on comparing the carrying amount of an entity’s assets and liabilities (using accounting rules) with the tax base for those assets and liabilities (Deegan 2013, p. 630). This compares two BS’s: the one produced by following accounting rules and the one produced by following taxation legislation. The profit declared by following accounting rules can be very different from the profit declared following taxation legislation. Given tax is paid on profit; these differences create tensions in societal expectations. This tension may also spill-over into step two: the treatment of tax losses. The reason for these differences occur is differences in recognition rules. Some examples are provided by Deegan (2013) in the table below:

<table>
<thead>
<tr>
<th>Item</th>
<th>Generally Accepted Accounting Rule</th>
<th>Tax Rule</th>
</tr>
</thead>
<tbody>
<tr>
<td>Many accrued expenses (for example long service leave, warranty costs)</td>
<td>An expense when accrued</td>
<td>Recognised as a Tax Deduction When Paid</td>
</tr>
<tr>
<td>Many prepaid expenses (for example prepaid rent, prepaid insurance)</td>
<td>Initially an asset – expensed when economic benefits used</td>
<td>Typically a tax deduction when paid</td>
</tr>
<tr>
<td>Revenue received in advance (for example rental revenue)</td>
<td>Treated as a liability – recognized as revenue when earned</td>
<td>Typically taxed when received</td>
</tr>
<tr>
<td>Entertainment and goodwill impairment</td>
<td>Treated as an expense</td>
<td>Not a tax deduction in current or subsequent periods</td>
</tr>
<tr>
<td>Doubtful debts</td>
<td>Treated as an expense when recognised</td>
<td>Treated as a tax deduction when debtor is actually written off in subsequent period</td>
</tr>
<tr>
<td>Development expenditure</td>
<td>Often capitalized and subsequently amortized</td>
<td>Typically a tax deduction when paid for</td>
</tr>
</tbody>
</table>

(Deegan 2013, p. 630)

The use of words such as “often” and “typically” in this table; further illustrate the subjective nature of accounting. If the word “always” was used; this would support the
case for accounting as an objective process. It is interesting to note that these softer words are used more frequently in the interpretation of tax rules, suggesting more subjectivity in taxation compared with accounting. This perhaps helps explain why taxation was a major problem found by the RC; it creates more scope for creative accounting and unlawful behaviour.

Step three aims to minimise tax payments. The first process is re-evaluation of non-current assets (see process 3b. in figure A1.1). When non-current assets are revalued, the tax base is not affected because depreciation for accounting purposes will continue to be based on the original cost (Deegan 2013, p. 643). However, if there is an increase in the carrying value of a non-current asset as a result of re-evaluation, there is an implication that this should be recognised as an expected increase in the future flow of economic benefits (Deegan 2013, p. 643). Minimising tax payments is not illegal. However, it creates opportunity to push the boundaries too far and move into the area of tax evasion, which is illegal.

The following figure A1.1 provides a summary of the processes involved in income tax activity. It defines the three steps outlined above, along with associated processes. The processes in bold are the main opportunities for unlawful behaviour associated with taxation activity. The other processes may be considered lawful. The legend on the right outlines the internal and external stakeholders involved in the construction industry. At this stage, it is helpful to highlight where accountants might be involved. It is reasonable to assume that accountants would have been involved in steps 2 and 3. They would probably have been involved in the unlawful activities 2a and 3a to 3e in particular.
A1.3 Employee Entitlements Process

The second of the seven unlawful activities identified by the RC was underpayment of employee entitlements. It is not the purpose of this section to provide a detailed analysis of how employee entitlements is done. Rather it aims to explore accountants’ role in employee entitlements. If accountants are heavily involved, then they may have been also part of underpayments.

Employee entitlements are governed by law and are part of good corporate governance. For example, payment of superannuation by entities is regulated by the Australian Securities and Investments Commission under the Superannuation Industry (Supervision) Act 1993(C’wth). Most companies typically follow the law with employee entitlements in order to demonstrate best practice and good business ethics. However, successful protection of employee entitlements is not straightforward. Anderson (2014, p.
118) found in her review of employee entitlements across multiple Australian cases that it “is often a matter of timing, strategic choices, innovative approaches, regulator intervention, gritty determination by insolvency practitioners, union pressure, political expediency or a happy confluence of circumstances”. This suggests that best practice employee entitlements is the result of pressure from groups with vested interests, particularly regulators and unions, as well as chance.

The management of employee entitlements involves the following steps: first, determine employee entitlements, second, distributive justice (fairness), and third, procedural justice (equity).

In the first step, the company determines the level of employee entitlements it is willing to provide for its employees. This may be done lawfully or unlawfully. If done lawfully, the correct level of employee entitlements is recorded in the IS as an expense (see process 1b in figure A1.2), and the company seeks legal advice to ensure it is compliant (see process 1d. in figure A1.2). If unlawful, the company may seek to manipulate employee entitlements payments by under paying (see process 1c. in figure A1.2), and declare insolvency to avoid paying employee entitlements (see process 1f. in figure A1.2). The following case explains how insolvency works to avoid paying employee entitlements:

As in McCluskey, the employees (at Steel Tank and Pipe) had been transferred, without their knowledge, to five different companies that had no assets, ostensibly for tax reasons. All of the companies within the Group were undercapitalized, and the family shareholders had placed charges over the assets of the company in the weeks prior to the Group’s collapse (Anderson 2014, p. 123).

Insolvency aims to avoid paying employee entitlements by declaring bankruptcy and claiming the company cannot afford to pay its employees what they are entitled to. The
regulators are well aware that some unscrupulous individuals will seek to avoid their legal obligations in terms of employee entitlements. As a result, the Federal Government has introduced various legislation aimed to deter unlawful behaviour and encourage company directors comply (see process 1d. in figure A1.2). For example, the Explanatory Memorandum which preceded the enactment of the Corporations Law Amendment (Employee Entitlements) Act 2000 (C’wth), the object of s 596AB explained that the introduction of a liquidator to try to save struggling companies was a way to protect employee entitlements (Anderson 2014).

In the second step, the aim is to ensure that employees feel their employee entitlements is fair. This involves philosophical debate about the nature of work and social exchange theory. Perceptions of fairness about the level of employee entitlements is based on whether the employee sees entitlement as a right (see process 2b. in figure A1.2) or entitlement as something to be earned (see process 2c. in figure A1.2). For many employees, entitlements such as wages, superannuation and leave are seen as a right. In return for giving their services to their employer, individuals would expect to receive these entitlements. It gets more ambiguous when the level of entitlements is discussed. Employees covered by an industrial award or an enterprise agreement would expect to receive the level of employee entitlements relevant to their work. Under these circumstances, the agreement should ensure that employees’ expectations would be aligned with what the employer offered (see process 2f in figure A1.2) if both the employer and the employee meet their obligations under the agreement. However, employees not covered by an agreement may see differences in levels of employee entitlements, particularly wages, which could also translate into other employee entitlements areas if a percentage of wages is the denominator. In this latter group in particular, entitlement is probably more something to be earned in the sense that good
work performance is rewarded with higher wages and then higher employee entitlements.

Perceptions of fairness about the level of employee entitlements are also based on the nature of the employees’ emotional relationship with their employer. Individuals with low levels of psychological contract with their employer (see process 2d. in figure A1.2), are probably more likely to accept lower employee entitlements. On the other hand, individuals with high levels of psychological contract with their employer (see process 2e. in figure A1.2) will probably want higher levels of employee entitlements. They expect higher reward for their extra loyalty and commitment. This creates a tension in aligning employers and employees’ employee entitlements (see process 2f in figure A1.2). In industries such as construction, where employees expect low ambiguity due to their perception that employee entitlements is a right and governed by industrial agreements, individuals expect that employers should meet their employee entitlements expectations. For the employees, this is only fair. However, employers may see their employees having low psychological contract, that is committed to the job and not the organisation, and therefore deserving lower levels of employee entitlements. Unscrupulous company directors might extend this thinking to justify avoid paying employee entitlements. This creates misalignment in employee entitlements levels and perceptions of unfairness. At this point, this is where the construction industry’s trade unions become involved in employee entitlements. Anderson (2014) provides case study examples of union involvement in employee entitlements.

In the third step, the aim is to ensure that employees feel their employee entitlements is equitable. This involves discussion of legitimacy and opportunity for both employers and employees to ensure that employee entitlements is provided equitably. Perceptions of equity in employee entitlements is examined by theories about equity sensitivity. One
of the ways that construction companies could engage in legitimate performance bonuses (process 3b in figure A1.2) was reward for early project completion. In its submission to the RC, the Australian Industry Group (AIG) argued that “some project agreements had also provided for performance-related payments to employers through gain-sharing systems to encourage early completion” (Cole 2003, vol. 5, p. 115). This was a performance incentive offered to companies for good work; which in the construction industry included completing the project before the expected due date. This provided employers with flexibility to offer performance bonuses (process 3b). A more effective method would be for the whole workforce to negotiate with their employer an early completion bonus to be shared amongst each employee. Another means for implementing legitimate performance bonuses (process 3b in figure A1.2) was penalty and overtime payments.

The following figure A1.2 provides a summary of the processes involved in employee entitlements activity. It defines the three steps outlined above, along with associated processes. The processes in bold are the main opportunities for unlawful behaviour associated with employee entitlements. The other processes may be considered lawful. The legend on the right outlines the internal and external stakeholders involved in the construction industry. At this stage, it is helpful to highlight where accountants might be involved. It is reasonable to assume that accountants would have been involved only in step 1. They would probably have been heavily involved in the unlawful activities 1b, 1c, and 1e in particular.
A1.4 Payroll Tax Process

The third of the seven unlawful activities identified by the RC was non-compliance with payroll tax. It is not the purpose of this section to provide a detailed analysis of how payroll tax is done. Rather it aims to explore accountants’ role in payroll tax. If accountants are heavily involved, then they may have been also part of non-compliance.

PTA (2010) explain that payroll tax is state tax on wages paid by employers and it is a self-assessing tax. The process for accounting for payroll tax involves the following steps: first, recognising the payroll tax liability, second, seeking exemptions, and third, minimising tax payments.

In the first step, the aim is to measure the company’s payroll tax obligations (see process 1a in figure A1.3). Payroll tax is a self-assessing tax, which means that the onus is on the

APPENDIX 1 THE ACCOUNTING PROCESS
company to do the right thing and calculate and pay the tax required. This is done by calculating the company’s tax debt using PTA tax guidelines on thresholds and rates.

The threshold figures are the total wages paid by the company as wages to its employees. For example, once a company reaches the figure of $689,000 in wages in NSW, it must then pay payroll tax. If its wages are below $689,000, the company does not have to pay payroll tax. As payroll tax is an additional tax burden and an unwanted expense for companies, it is easy to see how small companies in the construction industry would want to avoid paying it. Given the high proportion of very small companies in the construction industry, that is with one to five employees (see chapter 3), many would be so small in terms of their wages bill that they would be below the threshold and could avoid paying payroll tax legitimately. However, in this step the company must determine its legal obligations to pay payroll tax (see process 1b in figure A1.3) and accountants would have been involved in this activity, as it would involve measuring the wages bill which is a company expense and would need to be reported in IS’s. The list of items defined by the PTA as comprising the wages bill may have been an opportunity for creative accounting in the construction industry, that is, not disclosing certain payments or not disclosing their full amount with the aim of avoiding the payroll tax threshold or reducing the threshold.

The next process in the first step is to calculate the amount owing using the tax rate (see process 1c in figure A1.3). For example, a NSW company with an annual wages bill of $1 million would need to pay 5.45% payroll tax on the wages above the threshold of $689,000 (that is, $321,000). Accountants would have been involved in this activity, as it would involve calculating the expense payroll tax posed for the company. However, companies may try to reduce the threshold figure (see process 1d in figure A1.3). Companies could do this by determining levels of part-year employment, interstate
wages (it is possible for a multi-state employer to be liable for payroll tax in some states and not others), and group membership (one threshold per group) (Payroll Tax Australia 2010). This activity could be an example of creative accounting where the company’s accountants are directed by management to find ways to reduce their payroll tax obligations.

In the second step, the aim is to reduce the company’s payroll tax obligations by seeking exemptions (see process 2a in figure A1.3). A common way to try to avoid paying payroll tax was to classify employees as contractors. In this way, the company can reduce their wages bill and, therefore reduce their threshold. Similarly, the “employee” may avoid paying payroll tax because they do not reach their individual wages do not reach the threshold figure. The PTA recognised this problem and explained that “a worker can be an employee even if they have an ABN and that ‘many ‘contractors’ have been found by courts to be employees” (Payroll Tax Australia 2010). The next activity in the second step is to determine employee versus contractor employment status (see process 2b in figure A1.3). This is likely to have involved HRM staff rather than accountants, as it was a personnel classification decision. Whereas management would have probably told HRM staff who to classify as an employee versus a contractor; accountants would most likely have only become involved when measuring the wages bills of employees versus contractors, not who was in each group.

The use of subcontractors was widespread in the construction industry (see chapter 3). Construction companies had a legal responsibility to ensure their use of contractors to do work for them met payroll tax obligations. Companies were required to pay payroll tax for both employees and contractors. Companies were allowed to try to reduce their payroll tax threshold by seeking exemptions as outlined above. This was process 2c in figure A1.3. Accountants would have been involved when the company is receiving
invoices from contractors for payment. At that point, accountants may have wanted to know who the contractors were and the type of services provided. However, it is reasonable to conclude that accountants would probably not have been primarily responsible for seeking exemptions regarding contracts.

The next activity was to seek exemptions for contractors who were part of corporate groups. As stated above, one way of reducing the threshold for payroll tax was group membership (one threshold per group). In this way, companies could employ contractors who were part of the same group, and only pay payroll tax for the group as a whole. As shown in chapter 3, the construction industry had a complex structure (see chapter 3). This created opportunity for unscrupulous individuals to manipulate company ownership to engage in unlawful behaviour (see the next section on phoenix company activity). The one threshold per group payroll tax exemption opened the door for unscrupulous behaviour. Groups are created when two businesses are controlled by the same person or group of people. Grouping had two primary effects in terms of payroll tax: first, only one threshold for the group and second, each is liable for the tax of the others (Payroll Tax Australia 2010). Companies may try to avoid paying payroll tax via grouping. This activity, process 2d. grouping, in figure A1.3 is the responsibility of management. Directors of companies have a legal responsibility to know who they are doing business with under the Corporations Act 2001. It is unlikely that accountants or human resource management staff would have been involved, or even interested, in the grouping activities of contractors. However, they might have become aware of unscrupulous activity in the course of their work, particularly if the company was dealing with the contractor group regularly and over a considerable time period.

The third step in payroll tax is appeals (see process 3a. in figure A1.3). The PTA explains that in administering payroll tax, companies have two appeal mechanisms: first,
objections and reviews, and, second, reassessments (Payroll Tax Australia 2010). It is likely that accountants would have been involved in process 3a. However, it is unlikely that this activity was unlawful or inappropriate as the appeal mechanisms involved the regulator and the courts. Under these circumstances, accountants would have had no choice but to follow the PTA’s requirements for payroll tax, including all exemptions and other opportunities for creative accounting, to the strict letter of the law.

The following figure A1.3 provides a summary of the processes involved in payroll tax activity. It defines the three steps outlined above, along with associated processes. The processes in bold are the main opportunities for unlawful behaviour associated with payroll tax activity. The other processes may be considered lawful. The legend on the right outlines the internal and external stakeholders involved in the construction industry. At this stage, it is helpful to highlight where accountants might be involved. It is reasonable to assume that accountants would have been involved in all three steps. They would probably have been involved in the unlawful activities 1b in particular. The other unlawful activities (see bolded) would probably not have involved accountants.
A1.5 Phoenix Company Process

The fourth of the seven unlawful activities identified by the RC was creation of phoenix companies. It is the not the purpose of this section to provide a detailed analysis of phoenix company activity. Rather it aims to explore accountants’ role in phoenicing. If accountants are heavily involved, then they may have been also part of unlawful behaviour.

The concept of phoenix activity broadly centres on the idea of “a new company arising from the ashes of its failed predecessor” (Anderson 2012, pp. 411-412). There can be lawful and justifiable reasons to start a similar business when an earlier company fails; but often the behaviour exploits the opportunity to harm creditors by not paying liabilities. A 2009 Proposals Paper entitled ‘Action against fraudulent phoenix activity’ issued by the Treasury describes a newly-incorporated company taking over the business of a previously liquidated entity, which had no intention of repaying its debts, as the
“basic” form of phoenixing; and phoenix activity within corporate groups as the “sophisticated” form (Treasury 2009, p. 2).

The creation of phoenix companies involves the following steps: first, create new company name, second, transfer assets of existing company to the new company at little or no value, third, avoid liabilities of existing company, and fourth, avoid punishment from the taxation office or other creditors.

In the first step, the directors of a business which is struggling to remain solvent, identify an opportunity to establish a new company. While phoenix companies may exist in parallel with the existing business, it seems that directors who face insolvency tend to declare bankruptcy, and start again with the new company. There are two main processes in this first step: identify insolvency – this creates the need for a phoenix company, and apply for and register a new company - this creates the phoenix company. The same directors of the old company will operating the new company (Cowan 2012). The new company will trade under a similar name to the liquidated company in an effort to exploit the goodwill of the old company (Cowan 2012). Directors tend to establish the phoenix company in the same industry as the previous insolvent industry. This is important because it enables the directors to build on their business capabilities for example industry knowledge, customer relationships, as well as being able to utilise the assets of the insolvent company.

In second step, the assets of the insolvent company are transferred to the new phoenix company. “In a typical ‘phoenix’ company scenario a limited company will have transferred its assets to a new company for little or no consideration” (Cowan 2012, p. 17). In third step, the directors of the new phoenix company try to avoid paying the liabilities of the previous insolvent company, whilst attempting to trade under a similar
name to the old company. In fourth step, the directors of the new phoenix company may try to avoid punishment from the taxation office or other creditors if they tried to avoid paying the liabilities of the previously insolvent business or other fraudulent activity. Directors can choose to do this legally or illegally. In the United Kingdom, section 216 of the *Insolvency Act 1986* allows for the possibility for a director of a failed company to “buy out” the company’s name and business and to genuinely re-establish the business (Cowan 2012). However, to achieve this, the director will have to obtain the court’s approval (Cowan 2012). If this is not done the director will not only have committed a criminal offence but, in addition, will no longer have the benefit of limited liability (Cowan 2012).

If the directors try to avoid punishment illegally, there are two main processes in this fourth step: declare bankruptcy of the insolvent company as this avoids payment of outstanding debts, and avoid detection through a different company name. In terms of the second process, Cowan (2012) found that some directors seem to try to avoid detection by creating a new name for the phoenix company which is so different from the previous insolvent business that others may not realise it involves the same directors. However, the High Court found this activity to be illegal (Cowan 2012, p. 19).

The following figure A1.4 provides a summary of the processes involved in phoenix company activity. It defines the four steps outlined above, along with associated processes. The processes in bold are the main opportunities for unlawful behaviour associated with phoenix activity. The other processes may be considered lawful. The legend on the right outlines the internal and external stakeholders involved in the construction industry. At this stage, it is helpful to highlight where accountants might be involved. It is reasonable to assume that accountants would have been involved in steps
1 to 3. They would probably have been heavily involved in the unlawful activities 1c, 2a, and 3a in particular.

A1.6 The Making of Payments Process

The fifth of the seven unlawful activities identified by the RC was inappropriate payments. It is not the purpose of this section to provide a detailed analysis of making payments. Rather it aims to explore accountants’ role in making payments. If accountants are heavily involved, then they may have been also part of inappropriate payments.

The making of payments involves the accounts payable function. In the payable function, the accounts payable staff match all three documents: the invoice, purchasing order, and proof of receipt, to ensure that the underlying goods have been received and
the payment is authorised, prior to making the payment. When the accounts payable staff authorize payment, funds are transferred from the company to the supplier. It is recorded as an expense on the IS, and as a cash outflow in the CSF.

The payments process involves the following steps: first, matching support documents and authorising payment, second, recording transaction, and third deciding when to pay. In the first step, the accounts payable staff ensure that appropriate goods and services are received and authorise payment. The accountants’ role in the accounts payable function is to ensure relevant documents match before authorising payment.

In the second step, accounts payable staff record the transaction appropriately in the financial statements and transfer funds to the supplier. One of the problems in the accounts payable function is ensuring that goods and services purchased are appropriate. By appropriate, the goods and services are allowable under the company’s policies. It is the accountants’ role to ensure accounts payable are appropriate and company funds are only used to purchase goods and services relevant to the business and approved under its policies.

In the third step, deciding when to pay, the company directors will determine the payment behaviour which, as outlined above is influenced by the owners (customers) payment behaviour, but might also be pre-determined by company policy or random. Delaying or withholding payment is common in many countries (Tran & Carmichael 2012). It has become an entrenched culture in parts of the construction industry across the world (Tran & Carmichael 2012). Companies engage in this activity to improve their own financial position; and it is referred to as opportunistic behaviour (for example, see Wu, Kumaraswamy & Soo 2011, p. 16). This behaviour is clearly desirable for those
delaying payment, and undesirable for those waiting for payment. It is unscrupulous in the sense that one company attempts to profit at another’s expense.

The contractual relationships in the construction industry make decisions on payment a complex issue. In general, the contractor is responsible for the satisfactory completion of the work by a subcontractor and for the payment of subcontractors' claims (Tran & Carmichael 2012). This means that the owner, customer, pays the contractor and not the sub-contractors. The contractor is expected to manage their subcontractors without any involvement from the owner. Under these conditions, the owner may never be aware of when or even if the contractor pays their sub-contractors. It is reasonable, therefore, to remove owners from blame in unlawful behaviour associated with the third step in the payments process. Owners are indirectly involved in the sense that if they delay payment to contractors, this will be passed onto subcontractors. However, the main focus of the RC’s findings in terms of payments was on contractors or construction companies rather than those purchasing buildings. The relationship between contractors and their subcontractors now becomes our focus. Typically the conditions of contract for a subcontractor involve the subcontractor doing the work, submitting or lodging a claim, and being paid at a nominated later time or times (Tran & Carmichael 2012).

Waiting until the owner pays and then pay subcontractors, was much more common (see process 3b. figure A1.5). This could usually be built into contracts. For example, owners might be required to provide regular progress payments over the life of the project (for example, every month). If the contractor knows they will receive this regular payment, they could build this into their contracts with subcontractors. Money received in March, for example, would be used first to pay any bills due at that time, for example including invoices received from subcontractors. Companies could plan this payment behaviour based on their known payment schedules from owners. However, complexities emerge
when projects are delayed, which happens regularly in the construction industry. For example, a project might be delayed by four weeks due to problems with an electrical subcontractor. Subcontractors associated with other trades for example, bricklaying or plumbing, may have completed their work and submitted invoices. But the owner refuses to pay that instalment of the payment schedule until all work planned for that time period, including the electrical work, is completed. Therefore, the contractor has to wait until the electrical subcontractor finishes their work until the owner will pay and they can then pay the other subcontractors. Under these circumstances, this is a legitimate delay in payment.

However, not all delays are legitimate. Some contractors delay payments to subcontractors in order to improve their cash flow (Tran & Carmichael 2012). As outlined above, the contracting arrangements in the construction industry are complex. They include power differentials, which some individuals tend to exploit. For example, unscrupulous contractors may take advantage of smaller subcontractors by delaying or deducting payment without good reason (Uher & Brand 2008). Contractors know that many subcontractors in the construction industry are very vulnerable and struggling to survive. They know that subcontractors may not wish to damage relationships with people who provide them with work by complaining about payment. They will also know that subcontractors will usually have limited financial resources to pursue legal or other action to recover delayed payments through formal dispute resolution mechanisms (Tran & Carmichael 2012). Therefore, contractors may use their power to delay or withhold payment to subcontractors. Research has found that subcontractors are often not aware of the retained amount withheld by the owner from the contractor (Hinze & Tracey, 1994). Unscrupulous contractors could essentially lie to subcontractors by falsely blaming owners.
Research has also found that contractors are well aware of their actions when delaying payment. It is not an honest mistake. Wu, Kumaraswamy & Soo (2011, p.16) claim that payment delays seem “to arise from a deliberate choice of opportunism; rather than ignorance of the potential from ‘partnering’ or a long-term collaboration”. This means that rather than failing to see the damage caused or the need to build better working relationships with their suppliers, that is subcontractors, unscrupulous contractors deliberately choose to delay payment at the expense of their subcontractors. Finally, research has found that there is a correlation in this bullying behaviour and power differentials within the construction industry’s complex contractual system. There are differences in the incidence and degree of late payment between contractors and subcontractors related to company size (Brand & Uher 2010). In New South Wales of Australia, “firms with less than five employees and turnover less than $500,000 receive late payments more often than firms with more employees and higher turnover” (Brand & Uher 2010, p. 15).

The final process in the third step, is payment during insolvency, referred to as bankruptcy at personal and individual levels while at the corporate level it connotes a broader term covering liquidation, receivership and the administration of firms. Insolvency is covered elsewhere in this appendix,

The following figure A1.5 provides a summary of the processes involved in making and receiving payments. It defines the three steps outlined above, along with associated processes. The processes in bold are the main opportunities for unlawful behaviour associated with making and receiving payments. The other processes may be considered lawful. The legend on the right outlines the internal and external stakeholders involved in the construction industry. At this stage, it is helpful to highlight where accountants might be involved. Accountants would have been involved in steps 1 and 2. They would
probably have been heavily involved in unlawful activities in all nine processes outlined in the figure for these steps.

**A1.7 Security Payments Process**

The sixth of the seven unlawful activities identified by the RC was absence of adequate security of payments for sub-contractors. It is not the purpose of this section to provide a detailed analysis of security of payments. Rather, it aims to explore accountants’ role in security of payments. If accountants are heavily involved, then they may have been also part of absence of adequate security of payments for sub-contractors.

The RC defines “the term ‘security of payment’ as attempts to redress a consistent failure to ensure that participants in the building and construction industry are paid in
full and on time for the work they have done, even though they have a contractual right to be paid” (Cole 2003, vol. 8, p. 229).

Legislation to address security of payment in the construction industry was initially introduced in New South Wales and Victoria (Cole 2003, vol. 8, p. 245). The legislation provides a best practice approach to security payments, as it helps identify what regulators wanted in terms of societal contract, that is, desired behaviour associated with security payments. Both of the state’s legislation establish a system of progress payments, rapid adjudication of payment disputes, and contract reform (Cole 2003, vol. 8, p. 245). The Victorian legislation is modelled upon the New South Wales legislation. The other states later introduced legislation that built on the New South Wales model. Therefore, the focus is on the New South Wales legislation for illustration.

In New South Wales, security of payment is regulated by two different sets of laws – the Contractors Debts Act 1997 (NSW) and the BCISP Act 1999. Commissioner Cole (2003, vol. 8, p. 239, para. 50) explains that:

The Contractors Debts Act 1997 (NSW) enables a subcontractor who has not been paid by a building contractor to obtain payment directly from the principal. This may be achieved through two mechanisms – attachment of moneys and assignment of debt. Attachment means freezing moneys in the hands of the principal so that the principal cannot pay the building contractor until the subcontractor has obtained judgment in the Magistrates Court for the amount owed by the contractor to the subcontractor. Assignment occurs once such a judgment has been given by the court. In these circumstances, the court may issue a debt certificate for the amount of the judgment. The subcontractor can then serve this on the principal, with a formal notice of claim, thereby obligating the principal to pay the subcontractor directly out of the moneys otherwise owed to the contractor (Cole 2003, vol. 8, p. 239).

The BCISP Act 1999 initiated a system of progress payments, adjudication of payment disputes and security over payments (Cole 2003, vol. 8, p. 240). The BCISP Act 1999 safeguarded entitlement to receive payment for construction work performed under a
construction contract (Cole 2003, vol. 8, p. 240). Section 3(3) of the BCISP Act 1999 provides that:

The means by which this Act ensures that a person is able to recover a progress payment is by establishing a procedure that involves: (a) the making of a payment claim by the person claiming payment, and (b) the provision of a payment schedule by the person by whom the payment is payable, and (c) the referral of any disputed claim to an adjudicator for determination, and (d) the setting aside of money as security of payment of the progress payment so determined (Cole 2003, vol. 8, p. 240).

Commissioner Cole (2003) found that:

Under the *Building and Construction Industry Security of Payment Act 1999 (NSW)*, progress claims for payments may be made by subcontractors against contractors; subcontractors against other subcontractors; contractors against certain clients; and suppliers against purchasers. Where payments are not made, the claimant, for example a subcontractor, may seek to recover the moneys claimed. If the respondent, for example a contractor, does not either pay a progress claim in full, or provide a ‘payment schedule’ within a specified time of receiving a progress claim setting out the amount of the progress claim that is disputed, the claimant may seek summary judgment in relation to the unpaid moneys. If a payment schedule is provided, then both parties are required to prepare submissions concerning the validity of the claim within a short period, and the matter is submitted to an appointed adjudicator. The adjudicator’s decision can be enforced via the summary judgment procedure. Each party retains the right to litigate in the courts in the normal way, but until a court determines the matter, the adjudicator’s decision prevails. Hence, a builder is required to pay money found to be owing by the adjudicator, even if the builder is disputing a subcontractor’s entitlement to that money in the courts. Only if the court action is successful is the subcontractor required to return the money. This adjudication procedure greatly speeds up the process of resolving disputes concerning security of payments in the New South Wales building and construction industry. It substantially reduces the cost of having such disputes resolved (vol. 8, p. 240).

The following figure A1.6 provides a summary of the processes involved in security payments. It defines two steps outlined above, along with associated processes. The processes in bold are the main opportunities for unlawful behaviour associated with security payments. The other processes may be considered lawful. The legend on the right outlines the internal and external stakeholders involved in the construction
industry. At this stage, it is helpful to highlight where accountants might be involved. It is reasonable to assume that accountants would have been involved in both steps. They would probably have been involved in unlawful activities in six of the process outlined in the figure for these steps.

A1.8 Profit Reporting Process

The final of the seven unlawful activities identified by the RC was profit manipulation. It is not the purpose of this section to provide a detailed analysis of profit reporting. Rather it aims to explore accountants’ role in profit reporting. If accountants are heavily involved, then they may have been also part of profit manipulation.

Profit reporting involves communication of financial performance; more specifically profitability to users of financial statements. It is an important measure of past performance, and also a good indicator of future performance. Therefore investors and
other stakeholders interested in future financial performance will rely heavily upon profit reporting.

Profit reporting involves the following steps: first, profit or loss disclosure, second, exceptions to accounting standards, third, creative accounting, and fourth, fraud.

In the first step, profit and loss is disclosed via financial statements (see process 1a. in figure A1.7). In financial reports, profit is disclosed in a statement of comprehensive income. Profit manipulation involves two simultaneous activities: first profits are inflated in reports to capital markets, and second profits are understated in reporting to tax authorities (Desai 2005, p.171). This then poses the question of how a firm can inflate and understate profits at the same time. The answer to this question is “firms keep two sets of financial statements: a financial statement that reports ‘book profits’ to the capital markets, and a separate financial statement that reports on ‘tax profit’ to the government” (Desai 2005, p. 171) (see process 3b. in figure A1.7 in this appendix). The two types of reports bear little resemblance to one another and follow distinctly different rules (Desai 2005, p. 171).

Desai (2005, p. 184) asks whether the “degradation of profit reports to capital markets and tax authorities”, illustrated by the cases of Enron and Xerox among others, was indicative of random behaviour or “representative of some broader trends in the reduced quality of profit reporting”. He then explains that “the quality of corporate profit reporting can be measured in several ways” (Desai 2005, p. 184). “First, it is useful to identify the degree to which profits reported to capital markets and tax authorities are related” (Desai 2005, p. 184). In a historical analysis, Desai (2005, p. 184) found that whereas “simulated book income tracked actual book income fairly well until the mid-1990s, actual book income has diverged considerably from both tax income and
simulated book income since then”. Desai (2005, p. 184) concluded that “while book and tax profits were once closely related, they now appear to have distinct dynamics”. The second measure of the quality of profit reporting is the “accuracy of forecasts of corporate profits and the accuracy of initial estimates of corporate profits” (Desai 2005, p.184) (see process 2d. in figure A1.7). He found significant differences between forecasts and initial estimates “usually associated with unexpected moves in interest rates and sharp economic contractions” (Desai 2005, pp. 184-185). This suggests that profit manipulation had reached the levels of severe macroeconomic factors; a finding that Desai (2005) called striking.

Creative accounting (see process 3c. in figure A.110) “can directly affect the profit and loss account and also the balance sheet and it is also related to measurement or disclosure, the latter referring to the extent of to the method of presentation” (Matis, Vladu & Cuzdriorean 2012, p. 73).

This raises the question of whether profit manipulation is inappropriate behaviour and, if so, is it unlawful. The generally accepted accounting principles (GAAP) allow for a certain degree of interpretation in most countries” (Stlowy & Breton 2004, p. 11). Stlowy and Breton (2004, p. 11) explain that “to be legal, interpretations may be in keeping with the spirit of the standard or, at the other extreme, clearly stretch that spirit while remaining within the letter of the law” Interpretations may be erroneous (see process 3f. in figure A1.7), but never fraudulent (Dechow and Skinner 2000).

Fraud occurs when somebody commits an illegal act (see process 4a. in figure A1.7). Stlowy and Breton (2004, p. 11) state that “in terms of financial statements, for instance, “fabricating false invoices to boost sales figures is fraud, while interpreting consignment sales as ordinary sales is an error”. The difference, however, does not appear clear to
everyone. Stlowy and Breton (2004) list classification of fraudulent behaviour: falsifying or altering documents (see process 4b. in figure A1.7), deleting transactions from records (see process 4c. in figure A1.7), recording forged transactions (see process 4d. in figure A1.7) or concealing significant information (see process 4e. in figure A1.7). They also include elements that fall under the definition of accounts manipulation: those related mainly to interpreting accounting standards.

The following figure A1.7 provides a summary of the processes involved in profit reporting. It defines the four steps outlined above, along with associated processes. The processes in bold are the main opportunities for unlawful behaviour associated with profit reporting. The other processes may be considered lawful. The legend on the right outlines the internal and external stakeholders involved in the construction industry. At this stage, it is helpful to highlight where accountants might be involved. It is reasonable to assume that accountants would have been involved in all four steps. They would probably have been involved in unlawful activities in the nine processes outlined in the figure for these steps.
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