Submission to the Royal Commission into Trade Union Governance and Corruption

22 August 2014

Issues Paper 4: Relevant Entities






AUSTRALIAN INDUSTRY GROUP

Introduction

The Australian Industry Group (Ai Group) makes this submission in response to *Issues Paper 4: Relevant Entities* released by the Royal Commission on 23 July 2014.

Ai Group represents employers in the manufacturing, construction, transport, information technology, telecommunications, food and many other industries.

This submission focusses on the following entities:

- Worker entitlement funds;
- Entities wholly or jointly controlled by unions which offer insurance products, e.g. income protection insurance.

It is evident that the existing laws regarding governance arrangements for the above entities need major overhaul to protect employers, employees and the broader community. Even though some of the current practices described in this submission are not unlawful, they are certainly inappropriate and need to be stamped out without delay.

Construction industry unions are deriving very lucrative and inappropriate revenue streams from the contributions made by employers to worker entitlement funds and from insurance products which employers are coerced to purchase at inflated prices. As union membership revenue has declined, these revenue streams from employers have become central to union finances. The revenue streams need to be closed off to break the current business model of some construction industry unions where compliance with the law is evidently not seen to be necessary or important, and fines for unlawful behaviour are budgeted for as part of their normal business operations.

The existing inappropriate practices and inadequate laws are leading to the following adverse outcomes for the community:

- Higher costs for construction projects and electrical work, with reduced capacity for Governments to fund vital community infrastructure;
- Higher costs for businesses, with consequent negative effects on their competitiveness and their ability to retain or increase employment levels;
- Lucrative revenue streams which unions are able to divert to industrial and political activities, or donate to political parties;
- A higher incidence of unlawful industrial activity than would otherwise be the case;
- Disadvantages to employees who would in many cases receive more favourable insurance arrangements if their employer was free to choose the best insurance provider, rather than the provider forced upon them by unions; and

- Discrimination against non-union members.

1. Worker entitlement funds

1.1 Introduction

The most common worker entitlement funds are the redundancy funds in the construction and electrical contracting industries, but other worker entitlement funds also exist. Worker entitlement funds had relatively modest beginnings but nowadays they control billions of dollars and the existing governance arrangements are not appropriate.

Sections 58PA and PB of the *Fringe Benefits Tax Assessment Act 1986* provides for an exemption from fringe benefits tax to ensure that contributions which employers make to 'Approved Worker Entitlement Funds' are not taxed twice. The main construction and electrical contracting industry redundancy funds are 'Approved Worker Entitlement Funds'.

Various inappropriate practices of construction and electrical contracting industry employee entitlement funds are identified in Volume 10 (Reform – Funds) of the Final Report of the 2001-2003 Royal Commission into Building and Construction Industry ('**Cole Royal Commission'**). Unfortunately the inappropriate practices were not addressed following the handing down of Commissioner Cole's Final Report in 2003 and since this time the problems have worsened.

The inappropriate practices of many worker entitlement funds include:

1. Coercion of employers to contribute to these funds;

2. Inadequate governance arrangements, including:

    - The absence of specific legislation setting out the duties of Directors / Trustees / Office-bearers of employee entitlement funds;

    - The absence of oversight by an appropriate regulatory body such as the Australian Prudential Regulation Authority ('**APRA**');

    - Inadequate privacy protections to prevent unions gaining access to information about contributing employers and fund members;

    - The failure to make key information such as the following readily available to the public:

        - Annual reports and financial statements;

        - Details of the financial relationship that sponsoring unions and employer associations have with insurance companies and other providers of benefits offered by the funds;

- Allowing unions to receive millions of dollars each year in commissions and so called 'management fees' from providers of insurance products by forcing employers to buy products at grossly inflated prices which in many cases provide less generous benefits to employees than other products readily available in the market;

3. Distribution of surpluses to the unions and employer association sponsors of funds;

4. Redundancy funds making payments to fund members in circumstances where the member is not genuinely redundant, including:

    - Enabling employees to access redundancy payments if they resign or are terminated by an employer for poor performance;

    - Sending fund members a cheque each Christmas for a share of the investment earnings instead of crediting each employee's account with an annual return;

    - Providing a wide and ever-expanding range of payments to fund members beyond redundancy payments, which provides an incentive to unions to push for higher and higher contribution rates;

5. The absence of a scale of redundancy benefits within redundancy funds to avoid employers being coerced to contribute amounts that exceed what is required to provide reasonable redundancy benefits;

6. The use of funds contributed to pay employees who are on strike;

7. Discriminating against non-union members when providing fund benefits in breach of anti-discrimination laws and freedom of association principles.

1.2 Coercion of employers to contribute to worker entitlement funds

The modern awards in the construction and electrical contracting industries do not require that contributions be made to worker entitlement funds. However, the unions use the bargaining laws under the *Fair Work Act 2009* (Cth) ('**FW Act'**) to facilitate coercion of employers to contribute to such funds.

The coercion by unions of businesses to contribute to worker entitlement funds takes various forms including:

- Negotiating an industry-wide pattern agreement with an employer association or a group of individual employees, and including terms requiring that contributions be made to particular worker entitlement funds, e.g. Incolink and Protect.

- Refusing to agree to any enterprise agreement which does not reflect the industry-wide pattern agreement or a project-specific greenfields agreement which requires contributions to particular worker entitlement funds;

- Threatening or organising industrial action and other forms of industrial coercion (e.g. bogus safety disputes) to coerce employers to sign industry-wide pattern agreements or project-specific greenfields agreements which require contributions to particular worker entitlement funds; and

- Pressuring head contractors and major subcontractors not to subcontract work to businesses which have not signed the industry-wide pattern agreement or a project-specific greenfields agreement which requires contributions to particular worker entitlement funds.

The following examples highlight the large sums which employers in the construction and electrical contracting industries are being coerced to contribute to worker entitlement funds:

- The pattern agreement negotiated between the CEPU and the Victorian Chapter of the National Electrical and Communications Association for the 2010-2014 period (which applies to hundreds of electrical contractors in Victoria) requires that employers make the following contributions to the Protect redundancy fund:

    - $65.00 per week per employee up to 30 September 2011;
    - $70.00 per week per employee from 1 October 2011;
    - $75.00 per week per employee from 1 October 2013;
    - $80.00 per week per employee from 1 October 2014.

- The CFMEU (Construction and General Division) Victorian Branch on-site construction pattern agreement for 2011-2015 requires that employers contribute $72.15 per employee per week into the Incolink Redundancy Fund.

Industry-wide pattern agreements need to be outlawed. This would be consistent with the recommendations of the Cole Royal Commission. In Volume 5 (p.53) of the Final Report, Commissioner Cole identified the following reasons for his rejection of the contentions of those who argue that pattern bargaining is justified in the building and construction industry:

- Pattern bargaining is, by its nature, imposed in a compulsory manner without the involvement of the employer or employees in the employment relationship;

- It denies employers the capacity for flexibility, innovation and competitiveness in respect of a major aspect of project cost;

- It denies employees the capacity to reach agreement with their employer regarding their own employment conditions – including leave arrangements, participation in bonus schemes, flexible working hours and other mutually acceptable arrangements;

- It assumes that all businesses and their employees operate in the same fashion, have the same objectives, adopt common approaches to working arrangements and are content with uniformity;

- It assumes that third parties such as unions or employer associations understand better than either the employer or the employees what the business model of the enterprise is and what the wishes and desires of the employees are;

- It assumes that employees are not capable of negotiating satisfactorily on their own behalf; and

- In areas other than major centres, where pattern bargaining does not occur, there is nothing to suggest that the industry operates inefficiently or that the working conditions are not satisfactory for the employer or the employees.

Recommendations:

1. As recommended by the Cole Royal Commission, industry-wide pattern agreements should be outlawed through an appropriate amendment to the FW Act. An enterprise agreement which reflects an industry-wide pattern agreement should not be able to be approved by the FWC.

2. Industry-wide pattern agreements should also be outlawed through appropriate amendments to the *Competition and Consumer Act 2010.* These agreements have a major negative effect on competition and commerce and should not be covered by the exemptions in the Act.

3. Protected industrial action in pursuit of bargaining claims for contributions to be made to worker entitlement funds should be outlawed if the relevant funds do not meet stringent governance, reporting and supervision standards. This can be achieved through narrowing the definition of a 'permitted matter' in the FW Act to the concept of a matter pertaining to the relationship between an employer and its employees as was the focus of the decision of the High Court of Australia in *Electrolux Home Products Pty Ltd v The Australian Workers Union and Ors* [2004] HCA 40.

4. Enterprise agreement terms requiring payments to worker entitlement funds which do not meet stringent governance, reporting and supervision standards should be 'unlawful terms' under the FW Act, and prohibited from being included in an enterprise agreement.

5. A specific anti-coercion provision should be inserted into the FW Act and the *Building and Construction Industry Improving Productivity Bill 2014* (which is before Parliament) prohibiting coercion of an employer to contribute to a worker entitlement fund.

6. The *Building and Construction Industry (Fair and Lawful Building Sites) Code 2014* (which the Federal Government recently published in advance form) and State Government Construction Industry Industrial Relations Guidelines should be amended to ensure that the following breach the Code and Guidelines:

    - enterprise agreements which reflect an industry-wide pattern agreement; or

    - enterprise agreement clauses which require payments to worker entitlement funds that do not meet stringent governance, reporting and supervision standards.

1.3 Inadequate governance, reporting and supervision

It is very obvious from the evidence which has already been heard by the Royal Commission into Trade Union Governance and Corruption that the current governance, reporting and supervision arrangements for worker entitlement funds are woefully inadequate, and must be urgently addressed. These funds now contain billions of dollars contributed by employers.

Other than the Australian Construction Industry Redundancy Trust ('**ACIRT**'), construction and electrical contracting industry redundancy funds regularly distribute surplus income back to unions and some employer associations (not Ai Group). This is highly inappropriate. The money paid to the redundancy funds is contributed by individual employers for the benefit of individual employees. It is not contributed for the benefit of unions and some employer groups.

The income derived by unions from the contributions made by employers to worker entitlement funds no doubt result in the fines which militant unions regularly incur for unlawful conduct having a significantly reduced impact on their operations.

The following extracts from Volume 10 (Reform – Funds) on pages 278-281 of the Final Report of the Cole Royal Commission are relevant:

> **"Distribution of surplus income**
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> 180 Excepting ACIRT, surpluses generated by each of the funds are paid to their sponsors or for other purposes, for example education, welfare and training. ACIRT, instead, distributes any surplus income as a dividend paid annually to employee members. This largely arose from the findings and recommendations in the Gyles Report.
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> 195 Those administering the funds appear to have lost sight of the fundamental premise that employer contributions are to fund redundancy entitlements. It follows that contributions, and returns on investments of the fund, should be held by the fund and distributed only for the purpose of paying redundancy entitlements.

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197 If funds were used only for the purposes for which they were established, contributions could be reduced – thus reducing building costs – or benefits to employees could be increased."

Similar to superannuation, specific legislation should be enacted to implement and enforce appropriate governance, reporting and supervision arrangements for worker entitlement funds.

In conjunction with developing the proposed new legislation, the existing taxation, corporation and trust laws should be considered to identify and address any impediments to implementing the proposed new governance, reporting and supervision arrangements.

An appropriate title for a relevant Bill would be the *Worker Entitlement Funds (Governance, Reporting and Supervision) Bill 2015*. The Bill should contain the key elements set out in the following table.

Recommendations:

1. A new piece of legislation should be enacted to be called the *Worker Entitlement Funds (Governance, Reporting and Supervision) Bill 2015*.

2. The Bill should contain the following key provisions:

   - Duties of Directors / Trustees / Officers of Funds (modelled on Directors' duties under the *Corporations Act 2001*);
   - A 'fit and proper person' test for Directors / Trustees / Officers of Funds with procedures for the removal of persons who do not continue to meet the test;
   - Education / training requirements for Directors / Trustees / Officers of Funds;
   - The requirement that remuneration for Directors / Trustees / Officers of Funds not be excessive;
   - Oversight by APRA;
   - Reporting obligations to APRA;
   - The requirement for each Fund to publish on a publicly accessible website its annual report (including financial statements), Trust Deed and other key information;
   - A prohibition on redundancy Funds distributing any amount to a member other than for the purposes of genuine redundancy, i.e. when an employee is terminated at the employer's initiative because the employer no longer requires the job to be done by anyone, and at the time when the person is made redundant. For example, this prohibition should:

- Prevent employees accessing redundancy payments if they resign or are terminated by an employer for poor performance;

- Abolish the existing practice of some Funds of sending members a cheque each Christmas for a share of the investment earnings, rather than crediting each employee's account with an annual return; and

- Abolish the wide and ever-expanding range of payments to fund members beyond redundancy payments, which provides an incentive to unions to push for higher and higher contribution rates;

- A prohibition on redundancy Funds distributing any amount to a member beyond the amount set out in a reasonable scale of redundancy entitlements (e.g. the scale in subsection 119(2) of the FW Act;

- A prohibition on Funds making distributions to sponsoring unions and employer associations, other than the payment of reasonable Board fees to Directors;

- A prohibition on Funds making any payments to employees who are taking industrial action;

- A prohibition on Funds discriminating between union members and non-union members when providing any Fund benefit;

- Privacy protections for information relating to contributing employers and Fund members;

- A prohibition on commissions, management fees, spotter's fees, or similar payments being made to sponsoring unions or employer associations by insurers or brokers in respect of insurance products offered or promoted by the Fund;

- A prohibition on field officers employed by Funds carrying out union business (e.g. some Fund field officers appear to carry out union recruitment and organising activities);

- A prohibition on Funds paying unions for field activities such as recruiting new Fund members;

- A professional recruitment and selection process for field officers employed by Funds to ensure that the most appropriately qualified persons are employed rather than, say, militant trade unionists; and

- Penalties for breaches of the Act (modelled on the *Corporations Act 2001*).

2. Entities wholly or jointly controlled by unions which offer insurance products, e.g. income protection insurance

Some of the worker entitlement funds referred to in section 1 above offer insurance products (e.g. income protection insurance) as well as providing redundancy or other entitlements. These include Incolink and Protect. In other cases unions have established or acquired separate entities which offer insurance products. Both of these types of entities need to be subjected to new, stringent governance, reporting and supervision arrangements.

Similar to the coercion described in section 1.2 above regarding employer contributions to worker entitlement funds, unions in the construction and electrical contracting industries are using the bargaining laws under the FW Act to coerce employers to pay for particular insurance products (e.g. income protection insurance) where the insurer or broker is making very large payments to the unions. The payments are typically labelled as management fees, spotter's fees or commission in the accounts of unions or relevant entities.

Typically the insurance products which an employer is forced to pay for are much more costly for the employer and provide fewer benefits to the employees than other products readily available in the market. However, because of the very substantial payments made to the unions by the relevant insurer or broker, the unions typically refuse to accept an employer's offer to provide equivalent or better benefits to employees through an alternative provider (e.g. through an industry superannuation fund or through the insurance company which the employer is using for its other types of insurance).

Employers have advised Ai Group that they can purchase income protection insurance for as little as 1/5th of the cost of the insurance products that the union is forcing them to purchase, while providing more generous income protection benefits to employees. This highlights that unions and the insurance companies that they are aligned with are reaping massive financial rewards at the expense of businesses, and at the expense of the consumers that purchase the businesses' products and services (at consequently higher prices).

The following extracts from Volume 10 (Reform – Funds) on page 16 and pages 311-314 of the Final Report of the Cole Royal Commission are relevant. The problems identified by the Royal Commission in 2003 have not been addressed and remain a major problem:

> "54 The Commission received widespread and consistent evidence about the use of pattern enterprise bargaining agreements (EBAs) to standardise employment agreements. Many of the pattern EBAs provided for income protection insurance to be provided by employers to their employees. Some pattern agreements specifically nominate the insurance provider. Others do so implicitly by referring to a policy or fund agreed upon by the applicable employer and employee associations.
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> 55 The capacity to deliver an industry workforce to an insurer or to a fund manager has a commercial value.
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> 56 In the Income Protection Insurance chapter I refer to evidence of commissions and management fees received by employee and employer organisations arising from

these schemes. In the ElecNet (Aust) Pty Ltd case study, the commission received by a union as a result of arrangements included in a pattern EBA constituted a very significant income stream to that union. That case study illustrates a failure to disclose the commission to be received by the union at the time the EBA was negotiated

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1 Income protection insurance is provided to a large number of employees in most States, including Western Australia, New South Wales, Victoria, South Australia and Queensland. In some States pattern agreements promote specific providers of such insurance schemes.

2 The main income protection insurance case study examined related to the operation of a redundancy scheme; Electrical Industry Severance Scheme, which trades under the name of Protect. That case study is detailed in the ElecNet (Aust) Pty Ltd case study in this volume of the report.

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15 In evidence presented to the Commission, it was apparent that the capacity for employer and employee associations to derive income from delivery of a workforce to an insurer was a factor in income protection insurance becoming a commonly demanded entitlement under pattern EBAs.

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21 Between October and December 1999 representatives of the NECA Victoria and the then CEPU Electrical Division Victorian Branch negotiated a pattern agreement for the period 2000–2003. During those negotiations the parties agreed that employers would provide income protection insurance for employees through a policy and scheme agreed by NECA Victoria and the CEPU Electrical Division Victorian Branch.

23 The evidence established that NECA Victoria and the CEPU Electrical Division Victorian Branch agreed that the policy be taken out in the name of ElecNet (Aust) Pty Ltd (ElecNet), which is the trustee of the Electrical Industry Severance Scheme (known as Protect). ElecNet collects redundancy contributions from employers, and so provided an expedient means of also collecting the insurance premiums. ElecNet collected the premiums from employers paid on behalf of their employees, payed a fixed monthly premium to the broker based upon an estimate of the number of employees covered under the scheme during that month, and subsequently reconciled the correct premium payable by reference to the number of employees actually insured under the policy for each month.

24 The ElecNet premium included a ‘management’ or ‘spotter’s’ fee payable to the then CEPU Electrical Division Victorian Branch. ElecNet collected the full premium payable under the policy and forwarded it to the broker, who in turn forwarded the management or spotter’s fee to the CEPU Electrical Division Victorian Branch. Mr Dean Mighell, the Secretary of the then Communications, Electrical, Electronic, Energy, Information, Postal, Plumbing and Allied Services Union of Australia, Electrical Division, Victorian Divisional Branch, prior to March 1999, failed to disclose to representatives of NECA Victoria that the CEPU Electrical Division Victorian Branch was receiving a spotter’s fee or commission, when he was asked.

25 NECA Victoria and the employers who contribute the weekly premiums were therefore unaware of the substantial income stream to the CEPU Electrical Division Victorian Branch generated by this arrangement. My findings regarding this matter are contained in the ElecNet (Aust) Pty Ltd case study.

26 In August 2001 the then CEPU Electrical Division Victorian Branch received payment of more than $1 million as a result of this arrangement. That sum represented the management or spotter’s fees payable for the period March 2000 to June 2001.

27 In October 2002 the then CEPU Electrical Division Victorian Branch received another instalment of the management or spotter's fee totalling $632 674.04. A further amount of $627 325.96 was being held in trust by International Underwriting Services Pty Ltd to be paid as a third instalment of the management or spotter's fee.

28 Audited financial statements of the CEPU Electrical Division Victorian Branch for the year ended 30 December 2000 filed with the Australian Industrial Registry did not include money held by two trusts established by that Branch, a substantial proportion of which money was received from the management or spotter's fees."

To address the problems, we propose the changes set out in the following table.

Recommendations:

1. The recommendations in section 1.2 and 1.3 above are equally relevant to entities wholly or jointly controlled by unions which offer insurance products.

2. As recommended by the Cole Royal Commission (Recommendation 171), when bargaining for an enterprise agreement a union should be required to disclose the financial benefits that would be derived by the union from each term of the proposed agreement. A provision along the lines of the following should be included in the FW Act:

   "Disclosure of interests during bargaining

   A bargaining representative for a proposed enterprise agreement, other than an employee or employer covered by the agreement, must disclose in writing to the other bargaining representatives and to the employees covered by the agreement any direct or indirect financial benefit that the bargaining representative would derive from each term of the agreement. Such disclosure must occur as soon as practicable after a relevant term is proposed for the enterprise agreement and before any application is made for a protected action ballot order.

   Note: An example is an agreement term which requires that the employer pay for the cost of income protection insurance benefits for employees through a particular insurance provider which provides commission or pays fees to the union. The union would be required to disclose to the other bargaining representatives and to the employees the commission or fees which would be paid to the union"

3. As recommended by the Cole Royal Commission (Recommendation 172), registered organisations that receive income by way of commission, management fees or spotter's fees arising from insurance arrangements established to provide benefits to employees should be required to identify each separate commission or fee in the published accounts for the registered organisation. Similar requirements should apply to all entities controlled or jointly controlled by a registered organisation. The accounts should be published on a publicly accessible website.

4. Industrial action in pursuit of claims for income protection insurance products should not be permitted if the insurance provider is paying substantial commission or fees to a union or an entity controlled or jointly controlled by a union. Such claims are not matters pertaining to the relationship between an employer and its employees – the key concept focussed upon by the High Court in *Electrolux Home Products Pty Ltd v The Australian Workers Union and Ors* [2004] HCA 40.

5. Enterprise agreement terms requiring the employer to pay for a particular income protection insurance product should be "unlawful terms" under the FW Act if the insurance provider is paying substantial commission or fees to a union or an entity controlled or jointly controlled by a union.

6. An anti-coercion provision should be inserted into the FW Act and the *Building and Construction Industry Improving Productivity Bill 2014* (which is before Parliament) prohibiting coercion of an employer to purchase insurance products in which a union has a financial interest.

7. The *Building and Construction Industry (Fair and Lawful Building Sites) Code 2014* (which the Federal Government recently published in advance form) and State Government Construction Industry Industrial Relations Guidelines should be amended to ensure that enterprise agreement terms requiring the employer to pay for a particular income protection insurance product breach the Code and Guidelines if the insurance provider is paying substantial commission or fees to a union or an entity controlled or jointly controlled by a union.