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[29-541] Regulating small firm safety via the supply chain: implications of the Australian Work Health and Safety Act

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Abstract

The impact of the Work Health and Safety Act (WHS Act) highlights subcontractor working practices. By motivating contractors to influence subcontractor working practices, regulation influences the latter's health and safety performance. Indirect routes of regulatory influence, working via supply chains, might prove to be a more effective means of improving small firm health and safety than placing obligations upon subcontractors directly, and limit contractor exposure to their new liability for subcontractor breach.

Key words: regulation, compliance, health and safety, small firm, supply chain, Australia.

Small firm health and safety as a problem, supply chains and the influence of regulation

Small firms have a higher incidence of work-related injury than large employers¹,² as a result of a poorer safety culture that, in turn, generates costs in terms of the rehabilitation of injured workers.³ Poor small firm work health and safety performance is of international concern to small employers, employees, policy-makers and support providers.³,⁴,⁵,⁶,⁷

Walters and James⁸ (p 993) argue that "the adoption of comprehensive and systematic health and safety management is a necessary precondition for the establishment of effective and adequate arrangements for the protection of workers". Small firms are unlikely to have a formal workplace health and safety system in place. They typically experience resource challenges with regard to the design and implementation of effective workplace safety systems.⁹ Developing and maintaining safety systems imposes a time¹⁰ and financial burden¹¹ that structurally vulnerable or resource-poor¹² small firms may not be able to manage. Small firms' lack of formal sophistication in safety management systems¹³,¹⁴ means that the identification, management and documentation of safety risks are problematic.⁸,¹⁵ In this research report, we consider

whether, and how, the new Australian WHS Act might enable and encourage improved workplace safety in small subcontractor firms.

Supply chain influences on workplace safety

The management of workplace health and safety is complex, particularly in multi-tier supply chains where smaller firms act as subcontractors to larger contractors.¹⁶ Much of the literature assumes that supply chains are controlled by large or dominant organisations and that size and power decline as the chain descends from lead contractor through lower tiers of subcontractors.¹⁷ The limited evidence suggests supply chains influence subcontractor health and safety principally through devolution of responsibility for the management and supervision of safety to subcontractors down the chain.⁸

Recent research by Walters and James⁸ and Bahn and Rainnie¹⁶ has explored the role of supply chains in improving health and safety performance, particularly in small firms. Walters and James⁸ note the potential for supply chain relationships to enhance small subcontractor safety standards where large contractors use their market power to do so, for instance, through procurement strategies, industry certification schemes and industry, trade or organisation-based product-related initiatives. They further argue that sharing safety resources (knowledge, processes and documentation) along the supply chain is a means of increasing subcontractor compliance. Drawing on data from the Australian resources sector, Bahn and Rainnie¹⁶ report that the assumption that safety systems decline in sophistication as we descend the supply chain does not necessarily hold. Lead contractors at the top of the supply chain often expect firms operating in the middle of the chain to operate *more* sophisticated systems and achieve *better* health and safety performance outcomes than those to whom they provide services.¹⁷

Walters and James⁸ caution that market-based approaches to improving subcontractor safety practices only occur in relatively narrowly defined circumstances, namely, where accidents and ill health disrupt delivery and harm profitability. They call for safety strategies that do not rely only on voluntary supply chain cooperation as it is unlikely to be sufficient to improve subcontractor safety performance. Instead, they recommend regulatory strategies to stimulate both individual firms and trade and industry bodies to support small firms in the supply chain. The Work Health and Safety Act (WHS Act)¹⁸ constitutes such a strategy by expanding contractor liability for subcontractor safety practices and performance. As all supply chain parties are regulated, legal changes inevitably influence contractor–subcontractor relationships and shape health and safety outcomes.¹⁹,²⁰

The WHS Act, contractor liability and due diligence

By the end of 2012, all states and territories had accepted the WHS Act, albeit with some individual state changes, except Western Australia, which is reviewing the legislation to commence in 2014, and Victoria, which has refused to enact the legislation in its current form.²¹

What is new in the WHS Act is the introduction of a due diligence clause to support the previous duty of care concept; this clause describes the legal responsibilities of the “person conducting a business or undertaking” (PCBU) and its “officers”.¹⁸ The clause is intended to prevent contractors evading responsibility for workplace health and safety by outsourcing activities to independent subcontractors. The Act has flipped the notion of “control” on its head by making contractors legally liable for all subcontractors within their supply chain where they work at the contractor’s workplace.¹⁵ Any subcontractor breach of safety regulation now exposes contractors to the risk of legal penalties. A PCBU may conduct the business alone (self-employed) or with others. PCBU “officers” include decision-makers even those far removed from day-to-day operations — company directors, CEOs, board members and others. The Act makes contractors strictly liable for all subcontractors’ safety practices and performance below them in the supply chain, as

well as for their own employees, including labour hire agency workers, where they work on contractors' work sites.¹⁸

Legal liability under the Act is very complex because lead contractors (Box A) have responsibility for tier 2 subcontractors (Box B), and others with whom they have no direct contractual relationship further down the supply chain (Figure 1). Similarly, tier 2 contractors are liable for tier 3 subcontractors (Box C), and those below; tier 3 subcontractors are liable for tier 4 subcontractors (Box D) and others below, with liability extending down the supply chain to others acting as contractors for work produced on their work sites. Where subcontractor breaches occur on contractor sites, liability is shared in that managers in both firms can be fined or imprisoned. In Figure 1, the black lines display contractors' legal liability for subcontractors' safety practices and performance in a supply chain.

The Act imposes no contractor liability where subcontractors work at sites other than the contractor's and does not apply where small firms do not operate in supply chains to other contractors. Supply chains might be long and complex, rendering the task of safety management throughout the chain onerous. Penalties for officers found to be in breach of the Act can be severe, much greater than under previous state legislation — up to five years imprisonment and AUS\$3m fines.

Potential consequences of the WHS Act

Legislators may address safety issues by setting regulatory standards which apply directly to firms, or tackle them indirectly by imposing obligations on parties other than those whose behaviour legislators seek to change. Supply chains and suppliers are key potential influences on small firm safety; the WHS Act impacts small subcontractors via this indirect route. Such a radical legal innovation might lead to significant changes in supply chain relationships and in small subcontractor safety practices and performance. By motivating contractors to influence subcontractor working practices, regulation influences the latter's health and safety performance. It is an open question, therefore, whether indirect regulatory influences via the supply chain will exert a more powerful impact on small subcontractor safety practices and performance than laws imposed directly on firms that might be evaded in the absence of supply chain pressure or robust enforcement by regulatory authorities. The Act is likely to lead to changes in supply chain relationships, as contractors seek to limit their exposure to liability. Several scenarios are possible.

By imposing strict liability on contractors, the WHS Act is likely to motivate them strongly to develop new relationships with subcontractors with the intention of avoiding breaches of safety regulations and the accompanying legal liability. Failure to do so exposes contractors to the risk of serious legal sanctions. Contractors are likely to vary in their approach to managing subcontractor relations, ranging from coercion to building consensus with many possibilities in between. Contractors may seek to coerce subcontractors by imposing tight monitoring and enforcement practices to ensure compliance. Alternatively, contractors might adopt a more cooperative approach, building mutually supportive, high-trust relationships with subcontractors, with large firms seeking to enlighten small suppliers as to how they might meet their safety obligations and to offer advice and support to enable them to do so. Where contractors share expertise with smaller subcontractors and offer them support, this seems likely to contribute to improvements in safety performance. Small suppliers have the added incentive to adapt practices as requested by larger contractors in order to ensure full and prompt payment for current contracts and to continue in a position to win future contracts. Conversely, however, small subcontractors might experience various barriers to implementing large contractor practices. They may lack the absorptive capacity to interpret the support offered by large firms or the financial resources and time necessary to implement new safety practices effectively. Small subcontractors might also resist large firm interference in their internal affairs to retain as much autonomy as possible regarding their own practices.

Once the WHS Act has had time to bed down in large contractor organisations, research might investigate the impact of supply chains on small firm practices and performance in the new legal context and to identify the types of supply chain relationship most conducive to generating improvements in workplace safety.

Contractors possess some discretion regarding how to develop relations with particular subcontractors, although the latter shape these relations too. Relationships are likely to vary depending on: the contracting parties' prior experience of working together; contractor perceptions of the likelihood of subcontractor infringement of the WHS Act, or of breaches being detected by regulatory authorities; contractor dependency on particular subcontractors, which is shaped by the nature and value of the inputs supplied; contractor willingness to develop closer relations with subcontractors and to share expertise; and subcontractor capacity to absorb the knowledge contractors pass on to them, and willingness to act upon it. For instance, contractors might treat small subcontractors providing highly-valued, specialist services in a consensual, mutually supportive manner whereas subcontractors providing low value added services might be handled in quite a coercive fashion because substitute providers are readily available.

Supply chain influences on small firm health and safety practices and performance become even more complex where supply chains are multi-tiered or where small firms participate in several chains at the same time. Small subcontractors may need to be compliant with several safety systems simultaneously.

The consequence of the WHS Act with regard to small firm practice is as unpredictable as the nature of emergent contractor–subcontractor relations. There is, of course, no guarantee that the Act will produce improvements; it depends on contractor and subcontractor responses to the new regulatory landscape. There may be no clear connection between the character of contractor–subcontractor relationships and small firm safety outcomes. We might expect small firms in a supply chain supported actively by contractors to achieve a reduction in work-related accidents and injuries and the associated costs. But, if small subcontractors are unable or unwilling to understand contractors' advice or to implement recommended practices, safety records might not improve.²² Workplace health and safety might even deteriorate if changing relations with contractors impedes small suppliers' ability to manage workplace practices effectively. At the time of writing, it is too early to evaluate whether accident and injury rates have decreased as a consequence of the WHS Act. Perhaps benefits will take years to become visible as new contractor–subcontractor relationships take time to diffuse through the population.

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