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# Submissions[1]

**Senate**
**Economics References Committee**

**Inquiry into non-conforming building products**

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Presented by
Stephen Goddard
[redacted]

## Who we are

OCN is a public interest advocacy group with chapters in 3 States and the ACT. Our role is to assist in the development and implementation of public policy in the strata space. OCN is the voice of the "end user".

## Importance of Strata Development

Using NSW as an example; there are more than 72,000 registered strata schemes in this State with a combined asset value of more than $350 billion[2]. Strata schemes represent a store of our national wealth exceeding a trillion dollars.

Across NSW, 2 million people live within strata titled dwellings. Within 20 years it is expected that half of this State's population will be living or working in a strata or community title scheme[3].

These facts alone demonstrate how critical it is to preserve and protect public confidence in strata living.

The trend towards strata living is meant to continue. The *Draft Metropolitan Strategy for Sydney to 2031* sets out the need to identify more urban renewal areas, locate housing in centres close to transport and where other community infrastructure is already available[4].

This planning trend — brought about by necessity — is national.

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1 With the assistance of Bryony Cooper and K Michael Brown - City Futures Research Centre UNSW.
2 NSW Government (NSW Fair Trading) (2013) Strata Title Law Reform: Strata and Community Title Law Reform Position Paper
3 Ibid
4 NSW Government (2013) Draft Metropolitan Strategy for Sydney to 2031, Sydney: Department of Planning

Research by the Grattan Institute[5] identified a preference for homes near jobs and community facilities amongst Australians living in capital cities. The same research also identified a mismatch between the housing stock available on the types of housing people want to live in. The locational preference was linked to an acceptance of apartment dwellings.

## Building Defects in Strata Development

Building defects, and their rectification, are major problems in residential strata buildings. Research indicates that nearly three-quarters (72%) of residents living in strata have experienced one or more defects in their scheme[6].

At best: defects cause significant social and economic harm to residents, owners, owners corporations and other stakeholders within the strata paradigm.

At worst: building defects are a real and substantial threat to life safety.

As our strata buildings become larger and more complex, fire safety ought to become a critical focus.

The reality is that failure to deliver fire safety to at least the standard prescribed in the *Building Code of Australia* (**BCA**) is now a major building defect "frequent flyer" in the Australian strata space.

A fire safety defect in a large residential strata scheme is usually "hidden" from both the purchaser buying into the scheme and the Owners Corporation responsible for the building maintenance.

Missing fire dampers and fire collars — designed to stop the spread of fire up service ducts or through slab penetrations — are all too common.

Missing fire isolation between individual apartments — that is to say ,sealing the boundary wall at the slab above — is usually hidden behind decorative cornices.

Failure to meet these basic BCA standards in buildings over 3 storeys was frightening enough.

But these every day life threatening building defects (and the escalated cost to retrofit) pale in significance when compared to the combustible building material cladding used in the *Lacrosse* apartment building.

## *Lacrosse Building* - Docklands

More than 400 people were evacuated from 673 La Trobe Street, Docklands on 25 November, 2014 when a discarded cigarette on a balcony started a fire that very quickly spread up the face of the building.

No one was injured. The fire brigade found the building's cladding material, imported from China, should never have been used.

Owners of the Lacrosse tower are claiming more than $15 million in damages from the builder saying combustible cladding installed on the apartment complex by the construction

[5] Kelly, J-F, Breadon, P and Reichl J (2011) Getting the hosing we want - Grattan Institute Melbourne

[6] Easthope, H and Randolph B (2009), "Governing the Compact City: the Challenges of Apartment Living in Sydney Australia" City Futures Research Centre, University of New South Wales – published online 24 Sept 2009

company was responsible for the spread of the blaze. Work has already cost $6.5 million including almost $700,000 to dry out the building. It is estimated it will cost another $9 million to remove and replace the remaining unburnt cladding to comply with a council order.

To these costs must be added relocation costs, the costs of alternative accommodation and loss of rent.

It is reported the builder defended this claim saying the fire was caused by the careless disposal of a cigarette and spread because of materials stored on the balcony.

**Role of the Owners Corporation**

I would, for one moment, like to put to one side the life threatening consequences set out in the *Lacrosse* facts. Instead, I would like to focus upon:

(a) What has to be done to effect removal of an identified threat to life safety from a strata development;

(b) What will it cost; and,

(c) Who pays for the remediation and delivery of BCA standards.

Inevitably building defects within a strata scheme occur in common property.

Strata legislation throughout the Commonwealth identifies the Owners Corporation as:

1. the holder of legal title to common property; and as consequence,

2. the entity responsible for repair and maintenance using funds raised from owners by way of levy.

In strata terms, *Lacrosse* was lucky. Why? It burnt — and it burnt without loss of life. That means the damage could, at least in this first instant, give rise to some form of successful building insurance claim.

But what about the non claimable remediation? What if there was a second fire at *Lacrosse* before remediation takes place — is that an insurable risk?

And what about the other buildings like *Lacrosse* with the same or similar cladding — not yet burnt but on notice they have a fire defect in need of attention. That knowledge may well prevent an insurance payout in the event of fire.

On the evidence, these questions confront 72% of all newly constructed strata schemes in this country.

## Consumer Protection

On the evidence, our State and Territory Parliaments have seen consumer protection as an obstacle to be overcome in effecting a change in the structure of our cities which delivers the benefits of high density living close to jobs and transport.

A strata plan cannot be registered until the building is complete. Not before. An owners corporation comes into existence on registration of the strata plan.

Completion of the building implies completion of the building contract between builder and developer. Completion is also meant to imply delivery of the minimum building standards set out in the BCA.

The "off the plan" purchaser in a strata scheme is joining an owners corporation which has no contractual connection with the builder identified in the building contract.

This "disconnect between end user and builder" is unique to the residential strata sector within the building industry.. It is one of two core reasons for the unprecedented high rate of building defects being an integral part of new residential strata development. A 75% experience must tell you something.

Unlike new residential strata, commercial construction usually occurs under a building contract between builder and landowner. That contract will provide for the landowner controlling a retention of funds to ensure compliance with the contract and delivery of acceptable building standards.

In the strata space it is the developer who contracts with the builder and controls builder payment.

By the time the strata plan is registered the builder will have received full payment under the building contract and "danced down the yellow brick road" with the developer into the distance — leaving behind an Owners Corporation "end user" who must rely upon statutory warranties to recover the minimum constructions standards prescribed by the BCA.

So how has the public interest faired in the statutory warranty department?

**Statutory Warranties & Insurance**

In NSW the *Home Building Act 1989* (**HBA**) contains the statutory warranties affording consumer protection to the owners corporations.

How have apartment owners been served by the HBA? Badly.

In early 2002, I gave evidence to the *Joint Select Committee on the Quality of Buildings*[7] as chairperson of the then largest strata scheme in the country (with 650 lots). I pointed out that Sydney City Council (**Council**) had inspected 15 lots between levels 14 and 35 in one of our 3 residential towers. Fourteen of the lots failed to effect fire isolation. I informed the enquiry the Owners Corporation of which I was chair, was confronting the risk of being uninsurable because of the fire order Council was about to issue.

Until 2002 the HBA provided home warranty insurance (**HWI**) as a "first resort" form of protection for home building work.

Before its collapse, HIH Insurance (**HIH**) had around 30-40% of the home warranty insurance market. The HBA required all builders to have HWI before they started work. The HIH collapse created its own chaos.

I have no doubt the evidence I placed before the Campbell Inquiry were the style of facts creating the claims history which expedited the collapse of HIH making it impossible for builders to get insurance to start new work.

7 Campbell Report.

In response to builders not having access to home warranty insurance, the NSW and Victorian Governments resolved to limit the scope of HWI cover by:

(a) reducing the period of cover from seven years for all defects to 6 years (structural defects) and two years (non-structural defects); and,

(b) providing an exemption from the insurance requirement in the HBA in relation to the construction of a building which is more than three stories high and which has two or more separate dwellings.

Those amendments placed many strata developments outside the protection of home warranty insurance. Blind to the end user, the conventional wisdom behind these amendments meant "at least the builder could build".

At no time during any of the parliamentary inquiries conducted by the Parliaments of Queensland, New South Wales or Victoria was any regard given to the cost of failing to deliver the BCA in strata developments or the deferred hidden cost of remediation.

The vulnerability of the apartment dweller seemed secondary to obvious economic imperative articulated by the building and development industry.

Without insurance, from 2002 until 2012, strata schemes over 3 storeys with building defects (like Lacrosse) could either:

- raise a special levy to repair defects in the original construction; or,
- litigate.

The litigation contemplated could only be undertaken within the limits prescribed by the HBA. That meant bringing an action within 7 years to remediate a structural defect. Structural defect was defined as a defect in a "structural element" that:

- results in the building or part of the building being closed;
- prevents or is likely to prevent the practical use of the building or part of the building;
- results in or is likely to result in the destruction or physical damage of the building; or,
- results in or is likely to result in threat of imminent collapse.

If the defect did not become apparent within 7 years, the Owners Corporation had a whole new vulnerability.

In 2015 the 7 year warranty period in which an action was to be bought was reduced to 6 years. "Structural defect" was amended to "Major Defect" causing or likely to cause:

- an inability to inhabit or use any part of the building for its intended purpose; or,
- the destruction of any part of the building; or,
- a threat of collapse of any part of the building; or,
- you are defect prescribed in the Regulations(currently none).

**<u>High Court Decision</u>**

In October 2014 the High Court of Australia handed down its decision in *Brookfield Multiplex Limited v The Owners Corporation Strata Plan 61288* (**Chelsea Case**). The High Court held

that Multiplex, under a design and construct contract to the developer, did not owe a duty of care in tort to the body corporate of the strata title scheme to avoid pure economic loss occasioned by latent defects in common property built by Multiplex.

In this decision the High Court added that if legal protection is to be now extended [to a foreseeable end user], it is best done by legislative extension of existing forms of consumer protection. —by our Parliaments.

The High Court in Chelsea is telling us in the clearest terms that if builders are to owe any duty of care to the people who purchase “off the plan” strata lots, it is incumbent upon our State and Territory parliaments to create a statutory duty of care — because the hands of the judiciary are tied by the lack of proximity between the end user and the builder, who can rely upon his contract with the developer.

## Reality

The HBA is evidence of a national Parliamentary intention to protect the builder/developer to the exclusion of the interest of the end consumer — all to deliver urban consolidation.

The High Court has now told us that the builder of a residential strata building does not owe the apartment purchasers any duty of care.

A failure by our Parliaments to take the lead of the High Court and implement a statutory duty of care within our legislation runs the risk of undermining pubic confidence in strata living as a lifestyle of choice.

How can you doubt this?

For years now builders and developers have been failing to deliver the building code in strata development. This failure has been systemic.

The costs of retrofitting life safety within strata schemes have been largely hidden by ever increasing growth in “property prices”. Until now, no matter how bad a scheme was built, property values would kept going up at a rate which hid the cost of the defect retrofit.

But this enquiry has opened a new perspective to the public interest. Your concern is to preserve life safety in a situation where you now know building defects are so prevalent and so serious, lives are at risk.

What do we want?

We want the residential strata builder and developer to owe the end user a duty of care.

Your failure to assist us in the delivery of a statutory duty of care to strata purchasers could well result in:

1. Loss of life not unlike the Grenfell situation; and inevitably,

2. A loss in pubic confidence in strata living as a lifestyle of choice in circumstances where we have already invested a trillion dollars of the national wealth.