

Chapter 4

Issues raised by consumers

4.1 The main issues or claims in submissions from consumers were:

- there is lack of information and misunderstanding about the coverage of the insurance;
- claimants may need to force a builder into insolvency, which is a slow and costly process (and legal costs are not recoverable in the insurance claim);
- alleged oppressive behaviour by insurers refusing claims or undervaluing the cost of claims;
- state licensing authorities are not diligent enough in vetting builders, and getting rid of bad builders;
- resolving disputes in the various state consumer tribunals is slow and expensive; builders or insurers may prolong proceedings to wear the claimant down;

4.2 Issues to do with dispute resolution may relate to last resort insurance (for example, a dispute with the insurer over quantum) or may relate to situations where the insurance is not at issue (disputes with builders still in operation).

4.3 Most submissions from consumers referred to their own building disputes. Some of these are extremely long-drawn-out disputes which date from before the present last resort arrangements started in NSW and Victoria on 1 July 2002. Strictly speaking these are complaints about the States' dispute resolution arrangements, not about last resort insurance. But the issues overlap, since the narrower the scope of the insurance, the more important it is that dispute resolution arrangements, which are the consumer's remedy when the insurance does not apply, are satisfactory.

4.4 Issues to do with the present last resort schemes are considered here. Other issues to do with consumer protection in home building are considered in chapter 6.

Concerns about the HWI insurance product

Inadequate understanding of the coverage

4.5 Many submissions argued that consumers have inadequate information and understanding of the last resort nature of the insurance. In NSW there is a legal obligation for the builder to give the homeowner a copy of the home warranty insurance certificate, and information about procedures for resolving contract and insurance disputes. It appears that this does not always happen. In any case,

consumers may be unaware of the true scope of the cover if they do not receive a copy of the full policy document.¹

4.6 It appears that some insurers, but not all, routinely give the policy information to the homeowner as well as the builder.² Vero agreed that there is a need for better information to consumers, but said 'our experience has been that very few homeowners really take the time to understand the product, irrespective of the amount of information that is out there.'³

4.7 Disclosure provisions under Chapter 7 of the *Corporations Act 2001* apply between the insurer and the builder purchasing the insurance. They do not apply to the homeowner.

4.8 Some submitters felt that the name itself is misleading, since 'warranty' encourages a misleading analogy with consumer good warranties that are not limited to cases where the seller is insolvent. CHOICE said:

With the labelling of it as a warranty, people think of a warranty as when they buy goods and they have a warranty that, if there is something wrong with the goods, the retailer or manufacturer will fix them up. Again, I think you are right in saying that the name of the product is part of the problem...⁴

4.9 Some terms used overseas are 'builder performance protection',⁵ 'building defects insurance' and 'completion insurance'. HIA Insurance Services suggested 'statutory default cover'.⁶

Possible difficulty forcing a builder into insolvency

4.10 Consumers complained that they may need to force a builder into insolvency, which is a slow and costly process (and legal costs are not recoverable in the insurance claim). For example:

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- 1 Mrs I. Onorati (Building Action Review Group), *Committee Hansard* 13 June 2008, p.5. Similar comments in NSW Legislative Council General Purpose Standing Committee No.2, *Inquiry into the Operations of the Home Building Service*, December 2007, p.86. NSW Office of Fair Trading, additional information 23 August 2008, p.5
 - 2 Mr D. Turner (HIA Insurance Services), *Committee Hansard* 11 August 2008 (in camera), p.22. Mr C. Lamont (Housing Industry Association), *Committee Hansard* 17 September 2008, p.12
 - 3 Mr P. Jameson (Vero Insurance Ltd), *Committee Hansard* 20 June 2008 (in camera), p.8
 - 4 Mr G. Renouf (CHOICE), *Committee Hansard* 13 June 2008, p.20. Similarly Mr P. Dwyer (Builders Collective of Australia), *Committee Hansard* 10 April 2008, p.6. Mr C. Lamont (Housing Industry Association), *Committee Hansard* 17 September 2008, p.12
 - 5 In the Alberta New Home Warranty Program
 - 6 Mr D. Farrell (HIA Insurance Services), *Committee Hansard* 11 August 2008 (in camera), p.21

I won the matter in the CTTT and was awarded costs. The builder did not pay so I had to liquidate the builder before I could submit a claim on home warranty insurance.⁷

4.11 Building Ethics Australia suggested that 'the trigger point for insolvency should be better defined to avoid the time and cost involved when a builder essentially stops trading but does not meet the insolvency criteria as per the Corporations Act.'⁸

4.12 Several submissions suggested that to avoid this difficulty the insurance should be triggered if the builder's licence is cancelled as a result of a disciplinary matter or because the builder has disobeyed a legal direction to rectify. The HIA said that 'a dispute resolution process could be expressly linked to trigger HWI if failure to comply with the process leads to licence cancellation':

We consider that State Governments could take a more pro-active position in regard to the introduction of a more robust and accessible dispute resolution process for home buyers and home builders. Such a dispute resolution process could be expressly linked to trigger HWI if failure to comply with the process leads to licence cancellation. This would have the effect of transferring the burden of pursuing a defaulting builder from consumers to the government licensing agency. In HIA's view this would address the main area of current consumer complaint about HWI without losing the advantages of the current system.⁹

4.13 Vero agreed:

The second area that we believe is worthy of consideration is an additional trigger, called termination. This is termination of the licence of a builder for noncompliance with a tribunal or court order, which, like death, insolvency or disappearance, is pretty final—that is, it cannot be rorted and, if they do not pay and lose their licence, they are probably insolvent anyhow. We believe this will further reduce the proportion of homeowners that have to pursue a builder to initiate a death, insolvency or disappearance trigger from around 10 per cent of all homeowners to single digits.¹⁰

4.14 Mr McCarthy of the NSW Home Warranty Insurance Scheme Board advised that the board agrees with these concerns and has proposed (and the NSW government has agreed) an additional trigger for an insurance claim which would be suspension of the license of a builder by the Office of Fair Trading for a builder's failure to comply with a money order of the CTTT or a court.¹¹

7 R. Siebert, submission 5, p.1. Similarly Consumer Action Law Centre, submission 32. p.4

8 Building Ethics Australia Pty Ltd, submission 113 p.3

9 Housing Industry Association, submission 60 p.13

10 Mr P. Jameson (Vero Insurance Ltd), *Committee Hansard* 20 June 2008 (in camera), p.6

11 Mr G McCarthy (NSW Home Warranty Insurance Scheme Board), *Committee Hansard* 13 June 2006 p.73

4.15 The Victorian government advised that it is 'working with the insurance industry ... to expand the grounds on which home builders warranty insurance claims can be made.'¹²

Other burdens on consumers in insolvency cases

4.16 The Housing Industry Association noted the burdens that may fall on consumers even when the builder's insolvency is clear:

Insolvency of a builder triggers liability. However a claim for 'compensation' is not payable until a loss is 'quantified'. The extent of loss is not known until the house is completed, likely to be much later... Unlike other forms of consumer insurance, with home warranty consumers are required to manage their own claims, which can be costly and time-consuming. The home owner is left to find another builder, determine to extend to work to be completed and negotiate a new contract.¹³

4.17 The HIA suggested that this situation could be improved if a successful claim triggered a 'guarantee of completion', not merely compensation:

Conceptually, that involves a change in approach. It would involve the insurer becoming responsible for managing the completion of the project rather than the consumer having to make a claim, organise builders and then recover compensation.... The obligation would be on the insurer to mobilise other builders and contractors to finish the house under the contract which had been on foot with the insolvent builder.¹⁴

4.18 It is inherent in this proposal that the concept of a cap on claims for non-completion would disappear.¹⁵

4.19 Further, in insolvency cases consumers may be left dangling by a receiver acting (as the receiver is bound to) on behalf of creditors. For example, in the recent insolvency of Beechwood Homes (NSW) in May 2008, delay was caused while the receiver tried to find a buyer for the company (which was eventually successful). The HIA commented:

Under contract law, the home owner with a partly built house cannot take steps to conclude the contract in the event of insolvency of the builder (unless the terms of the contract provide for this). It is the legal responsibility of the receiver to recover as much money as possible for

12 Victorian Government, submission 38, p.5

13 Housing Industry Association, additional information 17 September 2008, p.1

14 Mr S. Goodwin (HIA), *Committee Hansard* 17 September 2008, p.5

15 Mr S. Goodwin (HIA), *Committee Hansard* 17 September 2008, p.5. The rationale for the cap on claims for non-completion (now 20 per cent of the contract value) appears to be a view that this is a reasonable limit to the incidental costs of completing the house with another builder; given that the consumer has the value of work already done, and should not have paid for work not done.

creditors, including from contracts on foot. The outstanding contracts might be the only asset the receiver has available for sale... Home owners can be left dangling for an extended period of time while the receiver tries to sell the company as a going concern.¹⁶

4.20 The HIA suggested that this situation could be improved for consumers by legislating a standard contract condition allowing the homeowner to terminate the contract in the event of the builder's insolvency:

[This] would have the effect of causing insurers to act promptly to organise for other builder to complete contracts in an orderly way thereby removing the delays inherent in dealing with a Receiver, who must advance the interests of creditors.¹⁷

4.21 The HIA's related and consequential suggestions were:

- the consumer should have the right to use the approved plans and other intellectual property of the insolvent builder;
- increase the cap for non-completion claims to \$200,000;
- require builders to maintain an annual insurance policy for the purpose of covering 'mobilisation' moneys for plan preparations where a contract and home warranty insurance cover have not been executed (maximum payout of \$5,000 or 5 per cent of the contract price, whichever is the greater, is suggested).¹⁸

Difficulty in knowing what is defective work

4.22 The Housing Industry Association noted that home warranty insurance has potential for dispute, more than other sorts of insurance, because of the difficulty that may arise in judging what is a defect or what the value of the loss is:

It is not the same as motor vehicle insurance, where you either have an accident or you do not. It is not the same as home contents and fabric insurance where, if you have a fire, there is no doubt that the house has burnt down. The insurers come in in relation to loss adjusting. They decide how much you have lost. But in the home warranty insurance area, the issue is not how much it is going to cost to fix up that defect: the issue is, is it a defect?¹⁹

4.23 Statutory warranties in building regulations make reference to the Building Code of Australia, which sets legal minimum standards for building work. However the Building Code is cast in terms of performance measures, and does not go to the

16 Housing Industry Association, additional information 17 September 2008, p.1

17 Housing Industry Association, additional information 17 September 2008, p.2

18 Housing Industry Association, additional information 17 September 2008, p.2

19 Mr G. Simpson (Housing Industry Association), *Committee Hansard* 17 September 2008, p.19

level of detail that would help a homeowner to know whether the particular building work is defective in all cases. The HIA commented:

Where a consumer claims that building work complying with the BCA and complying with any contractual specifications is nevertheless in their opinion defective, this becomes a matter of evidence and subjective judgement.... This tends to be a grey area of opinion and doubt, in which uncertainty prevails.²⁰

4.24 A number of more detailed guidelines have been published. The Victorian Building Commission has a *Guide to Standards and Tolerances 2007* which 'aims to assist building practitioners to build quality homes and reduce or prevent disputes, since the majority of domestic building disputes arise from differing views on the quality of work and what is a reasonable standard of construction'.²¹ The Housing Industry Association has recently published a similar guide.²² However these guides are not legally binding. While they will hopefully reduce disputation, there is no guarantee that a tribunal considering a dispute will adopt the guide's standard.

4.25 Clearer standards of what is or is not defective work, preferably with legal force, would reduce the problem of disagreement over whether work is defective. The committee recommends in chapter 8 that a national 'best practice' system should include better definition of acceptable versus defective building work.

20 Housing Industry Association, correspondence 17 October 2008, p.5

21 [Victorian] Building Commission, Annual Report 2006-07, p.32

22 For example, Housing Industry Association, *Guide to Materials and Workmanship for Residential Building Work*, n.d. [2008]