

Chapter 8

Summary and recommendations

Issues raised by builders

8.1 It is important to assure the financial stability of builders. Industry groups argue that the discipline of the insurers in vetting builders, with the ability to demand security if necessary, has generally improved the financial strength of builders and led to a drop in the number of insolvencies.¹ It is also necessary for the insurers because the claims experience of this long-tail class of insurance may be volatile over time.²

8.2 The committee notes that insurers advise that they would not participate in a first resort scheme. This is because 'the risk of obtaining and enforcing a court order is not one the insurer can realistically insure.'³ As Vero put it:

One of the basic criteria required to create an insurable event is, such event is accidental and beyond the control of the insured or any other party with a financial interest...So-called "first resort" BWI does not and cannot work because it fails, on several counts, to meet two of the primary tests of insurance, i.e. those of Insurable/Financial Interest and Insurable Event. A builder may gain a potential financial advantage by triggering an event which is not accidental and over which he has control.⁴

8.3 It appears that the requirement for security affects approximately 10 per cent of builders if the NSW Office of Fair Trading reports are representative. The committee is concerned at the lack of accurate data that is available on the number of builders who have provided security as a condition of receiving HWI, and in what form that security takes; in particular, the use of unlimited bank guarantees. This data should be included in any national data collection model and monitored carefully with a view to decreasing the burden on builders over time.

8.4 However the committee agrees with the argument that inhibiting builders from placing assets beyond the reach of consumers and their insurers is a benefit to consumers overall.

8.5 The implication that builders who are affected by these requirements would be better off in a government operated system is unsound. A government operated system must also have its financial requirements. In the Queensland system a builder

1 NSW Legislative Council General Purpose Standing Committee No. 2, inquiry into the operations of the Home Building Service, December 2007, p.82.

2 Office of Fair Trading, submission 16a to Legislative Council General Purpose Committee No.2, Inquiry into the Operations of the Home Building Service, December 2006, p.7

3 Housing Industry Association, submission 60, p.10

4 Vero Insurance Ltd, submission 71 to VCEC inquiry into Housing Regulation, p.8,18

who cannot satisfy the requirements is not asked for other security - the builder is simply refused a licence.

8.6 The committee is sympathetic to builders' concerns that active bank guarantees and deeds of indemnity make it difficult to change insurers. It appears that the authorities and industry bodies share this concern, but have no solution apart from 'make efforts' to encourage insurers to return securities.

8.7 The committee has not received evidence that would suggest a different conclusion from that of VCEC in 2005: that while some individual builders may have genuine grievances, there is nothing to suggest a significant systemic problem. However the committee notes the continuing concerns of the major insurer about the high rate of owner-builder activity in Victoria.

Issues raised by consumers

8.8 The committee agrees that there is a need for better information to consumers about the product. The committee suggests that a copy of the insurance certificate, a summary of the insurance product and an explanation of the relevant dispute resolution procedure should be provided by the insurer to the builder. The builder should then be required to provide this information to the consumer to assist all parties understand the nature of the insurance. Where possible this information should be as standardised as possible. This disclosure process should be part of the national 'best practice' scheme.

8.9 Furthermore the committee notes that "Home Warranty Insurance" is not an effective title for the insurance and implies a misleading level of coverage for consumers. The committee recommends changing the name of the insurance.

Recommendation 1

8.10 The committee recommends that all parties receive a copy of the insurance certificate, summary of product and dispute resolution procedures. The committee recommends changing the name of the insurance.

8.11 The committee acknowledges consumer concerns regarding the requirement in some cases to force a builder into insolvency before being able to claim HWI insurance. The consumer concerns on this issue are reasonable and the suggested additional 'loss of licence' trigger of an insurance claim appears to provide a solution.

8.12 The recent collapse of Beechwood Homes demonstrated an example of delay for consumers even when the builder was clearly insolvent. The HIA's 'guarantee of completion' and related suggestions require further examination.

8.13 The committee accepts the predominant evidence that premiums are lower in NSW and Victoria than in Queensland.⁵ However there are some discrepancies, the cause of which is unclear in the absence of clear official information, similar to the NSW Office of Fair Trading reports, in other states.

8.14 The committee recommends that better information should be published on a nationally consistent basis to improve accountability about this product. Reporting of premiums should be part of this.

8.15 In comparing premiums it should also be remembered that the Queensland scheme provides better cover: apart from being first resort, it covers no-fault subsidence; cover for consumers who are not insured because of fraudulent misrepresentation by builders; and non-completion without the cap of 20 per cent of contract value.⁶

8.16 In any case, the insurance is a very small proportion of total project costs (less than 1 per cent), and the difference between Victorian/NSW premiums and Queensland premiums is even smaller. The alternative schemes should be judged mostly on their other merits.

8.17 The committee agrees that consumers should be able to access thorough information on a builder's licensing and disciplinary record (subject to possible exceptions for matters still in dispute, to ensure procedural fairness to builders).

8.18 The fact that most building disputes resolve quickly does not alleviate the stress and expense of the ones which do not. A key element of a dispute resolution system is the ability to deal with disputes expeditiously. It is not acceptable that some disputes drag on for years.

8.19 In any dispute resolution system there may be a tension between resolving disputes quickly and giving both sides reasonable opportunity to have their say. Where the right balance lies depends on the situation. On the evidence the committee suggests that in the few intractable building disputes the balance may be too far towards slow and expensive.⁷

8.20 For example, in the NSW case, a homeowner might reasonably think that once an inspector has made a rectification order, which the builder has disobeyed, the

5 VCEC reached similar conclusions in 2005: Victorian Competition and Efficiency Commission *Housing Regulation in Victoria - building better outcomes*, October 2005, p.225-6

6 Queensland Building Services Authority, submission 8, att. p.5. Mr I. Jennings (BSA), *Committee Hansard* 10 April 2008, p.20. No fault cover for subsidence applies providing the builder tested the ground according to the Australian Standard.

7 In the NSW CTTT 36 per cent of cases are finalised within 35 days of receipt, but the statistic does not show how long the other 64 per cent take. NSW Office of Fair Trading, submission 16 to Legislative Council General Purpose Standing Committee No.2, *Inquiry into the Operations of the Home Building Service*, November 2006, p.41

next step should be deregistration of the builder followed by insurance claim, rather than being forced to re-agitate the whole case before a tribunal which may have less building expertise than the original inspector.

8.21 There would probably be fewer disputes if there was clearer guidance to both builders and homeowners about what is or is not a defect. As noted at paragraph 4.24, a number of 'standards and tolerances' guides have been published as advice on this, but they do not have legal force. Clearer standards of what constitutes defective work, preferably with legal force, would help avoid and resolve disputes.⁸

Recommendation 2

8.22 The committee recommends that COAG and the Ministerial Council on Consumer Affairs (MCCA) should pursue a nationally harmonised 'best practice' scheme of consumer protection in domestic building.

The scheme should include but not be limited to:

- **disciplinary procedures and penalties;**
- **clearer definition of defective work;**
- **quicker and easier dispute resolution;**
- **the proposed 'loss of licence' insurance trigger;**
- **the HIA's 'guarantee of completion' and related proposals,**
- **and better information for consumers (including information on builders' licence record and average cost of premiums).**

8.23 The Committee does not suggest that this necessarily needs to be done by Commonwealth regulation, if consistency can be achieved by inter-state cooperation.

Need for more detailed information

8.24 A theme in submissions was the need for better information about this class of insurance for the sake of accountability and transparency, given that it is mandatory.

NSW Office of Fair Trading HWI reports

8.25 NSW since 2007 has published reports on its scheme, including information such as the number of builder eligibilities; the number of securities held by insurers;

8 Given the complexities, care would need to be taken not to prohibit sound but non-standard work methods. A standard could be incorporated into regulation to the effect that there is a rebuttable presumption that work of a listed type, not within the set tolerance, is defective.

number and value of project certificates; premiums including and excluding charges; and information about claims (though not a full break down of claims development).

8.26 The committee commends NSW for this. No other state publishes similar information. Victoria says that it 'is currently working with the insurance industry on way to improve data collection on the BWI product.'⁹ Vero noted that 'scheme transparency is up and running in NSW, work in progress in Victoria.'¹⁰

8.27 The committee agrees that better public information on this insurance is warranted for the sake of accountability and transparency, given that it is mandatory. This would hopefully allay some of the stakeholders' suspicions that insurers make unreasonable profits from it. It should include key contextual information (such as number of builders, number of owner-builders, building permits) to illuminate trends.

Recommendation 3

8.28 The committee recommends that COAG and the Ministerial Council on Consumer Affairs should pursue a nationally harmonised scheme of detailed reporting of home warranty insurance.

National Claims and Policies Database

8.29 It is not surprising that home warranty insurance was not included in the National Claims and Policies Database, since the creation of the database specifically responded to the crisis in public liability and professional indemnity insurance at that time. It appears there was no particular expectation that other sorts of insurance should be included.

8.30 In particular, the exclusion of HWI had nothing to do with the treatment of HWI in Corporations Regulation 7.1.12(2), as discussed in chapter 7.

8.31 The question arises whether it would be useful to include HWI in the database now. This would go some way to answer demands for better public reporting of this class.

9 Victorian Government, submission 38, p.5

10 Vero Insurance Ltd, confidential additional information 23 June 2008, p.23

8.32 In 2003 there were reportedly not enough insurers to assure confidentiality of information. This no longer applies: five insurers offer home warranty insurance. According to the database methodology this should dispel concern.¹¹

8.33 The Committee recommends that home warranty insurance should be included in the National Claims and Policies Database, both to promote actuarial consistency among the insurers, and to satisfy public demands for greater transparency about this class. Satisfying public demands for greater transparency is justified because the insurance is mandatory.

Recommendation 4

8.34 The committee recommends that home warranty insurance should be included in the National Claims and Policies Database.

Senator Annette Hurley

Chair

11 'Data items are not included in the NCPD reports at this aggregate level unless at least three insurers contribute to the aggregate total for that data item. For policy reports, a data item is not reported where a single insurer contributes more than 85 per cent of the aggregate total or two insurers contribute more than 90 per cent of the total. These rules may be relaxed for claim reports if there is sufficient participation in the particular market to prevent identification of individual insurer claim information.' APRA, *National Claims and Policies Database - explanatory notes*, 5 September 2007, p.5