

**SUBMISSION No2 TO SENATE INQUIRY INTO THE HOME  
OWNER WARRANTY INSURANCE SCHEMES**

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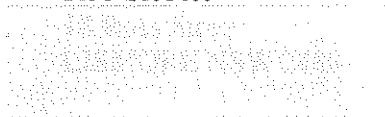
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Version 3

## **GENERAL**

My previous submission to this Senate Inquiry highlighted issues with Home Warranty Insurance and the position in which the present system of dispute resolution has placed me. In this submission I propose an alternate system to both dispute resolution, the role of Home Warranty Insurance. The alternate system proposed can be considered as an alternate to what I referred to in my first submission as the QLD Model but it should be noted that, by chance, very closely follows the QLD model.

The issues of Home Warranty Insurance and the dispute resolution process are intrinsically linked and as such must be considered together. For example the position of insurance in the dispute resolution process needs to be defined before any discussion on Home Warranty Insurance can be held.

In recognising the link my submission firstly compares the present system in NSW and a proposed system developed with the objectives of:

- Having process equally available to both builders and home owners;
- Having a short process in respect to time to reduce cost;
- Having a minimum cost process to avoid financial barriers to appellants;
- Having a process where only the issues at hand being compliance and contract are addressed and matters do not become bogged down in legal argument; and
- Having a process where the issues are addressed once only (subject to appeal).

From that system evolves a concept of Home Warranty Insurance within the dispute resolution system. There after is a discussion on the coverage of the insurance and whether that insurance should in the hands of the private sector or government.

## **ALTERNATE DISPUTE RESOLUTION SYSTEM AND IMPACTS ON THE CONSUMER, BUILDER AND INSURANCE**

### ***Comparison between Existing System and a Proposed System***

A description of the existing system of dispute resolution and an alternate system of dispute resolution and its impacts on builders, home owners and insurers is given below.

### ***Present System in NSW***

#### **STAGE 1**

Advise defaulting party that works need to be rectified, monies paid, access given etc and seek agreement with the other party on how the matter to be resolved. If the matter is resolved the process stops here.

## **STAGE 2**

In the event the matter is not resolved either party can take the matter to the HBS. Note this avenue of redress is not available to the builder.

HBS inspect the property/issue and direct the builder to do works. If the direction is complied the matter stops here.

## **STAGE 3**

If the Order not complied with the matter has to be taken by the appellant to the CTTT. Hearings are held and the CTTT makes a determination. Generally the CTTT member does not have a building background and is ignorant of many requirements of Australian Standards and the BCA.

If the Order of the CTTT is complied with the matter stops here with the exception that the home owner must source another builder and go through the building process again with the new builder.

## **STAGE 4**

If the Order is for money and is not complied with the appellant needs to seek a Court Order and serve it on the defaulting party.

If the Court Order is complied with the matter stops here with the exception that the home owner must source another builder and go through the building process again with the new builder.

## **STAGE 5**

If the Court Order is not complied with the appellant must liquidate the defaulting party.

If there are sufficient assets available to meet the costs incurred to rectify the problem the matter stops here with the exception that the home owner must source another builder and go through the building process again with the new builder.

## **STAGE 6**

After liquidation, if there are insufficient funds available for restitution the appellant needs to lodge an insurance claim. This avenue is not available to the builder. The claim is assessed and if agreed the matter stops here with the exception that the home owner must source another builder and go through the building process again with the new builder.

## **STAGE 7**

If the insurance claim is not agreed with, the matter has to be taken by the appellant to the CTTT.

## **STAGE 8**

After the directions of the CTTT are complied with by the insurer the home owner has to engage a new builder to undertake the rectification works and there is a risk the whole dispute resolution system will be invoked again with the new builder.

If the directions of the CTTT are not complied with the matter must be taken by the appellant to the Supreme Court.

A further Home Warranty Insurance premium needs to be paid for the new contract. Further prosecution of the builder by HBS will be subject to further action in the CTTT and appeals through the Supreme Court and or the Administrative Decisions Tribunal.

## **AVENUES TO CHALLENGE**

Any claim by an appellant, direction from the HBS or determination of the insurance company can be challenged in the CTTT.

In limited circumstances the CTTT may be asked to review the decision and may or may not accede to that request. The matter could be taken to Supreme Court on points of law or procedural fairness but again in limited circumstances. Neither of these necessarily relate to, nor cover issues of compliance with the DA, Standards and BCA or contract.

## **MYSITUATION**

It has taken 5 years, \$65,000 in legal fees and \$60,000 in rent to get to the end of Stage 6, where I could submit an insurance claim, as described above.

### ***Proposed System***

The proposed system was developed without detailed knowledge of the QLD system (apart from anecdotal evidence) or any preconceived notions apart from

- Having process equally available to both builders and home owners;
- Having a short process in respect to time to reduce cost;
- Having a minimum cost process to avoid financial barriers to appellants;
- Having a process where only the issues at hand being compliance and contract are addressed and matters do not become bogged down in legal argument; and
- Having a process where the issues are addressed once only (subject to appeal).

The system proposed ends up closely following the QLD system with the exception that the Order is the thing which has to be executed or challenged. The parties are not challenging each other.

## **STAGE 1**

Advise defaulting party that works need to be rectified, monies paid, access given etc and seek agreement on how the matter to be resolved. If the matter resolved the process stops here.

## **STAGE 2**

In the event the matter is not resolved, either party can take the matter to the HBS. If there is an agreement on what has to be done HBS issue an Order for whatever has to be done to be done. This can be applied to either or both the builder and the home owner.

If there is no agreement HBS determine what has to be done and issues an Order accordingly.

If the Order is complied with, the advice that it has been complied with is co signed by both parties and provided to HBS, the process stops here.

### **STAGE 3**

If the Order not complied with, defaulting party is guilty of an offence and

- Rectification works done by insurer in accordance with the Order;
- Where monies involved, District/Supreme Court order and normal recovery of monies procedures; and
- Defaulting party fined or prosecuted by HBS for non compliance with Order and any other offence.

The matter as far as the consumer is concerned is finalised here.

### **AVENUES TO CHALLENGE**

The only thing that can be challenged is the Order. The only avenues of challenge are:

- Where it is considered works found not to be in compliance with DA/Standards and BCA are in fact complying or visa versa; and
- Where it is considered works found not to be in the contract are in the contract and visa versa.

If the Order is challenged by either party the matter goes to the CTTT where

- Issues of compliance with Standards, BCA, DA etc are as determined by HBS
- Issues of law (whether it was in the contract) determined by CTTT
- Findings of CTTT include the determination of HBS.

CTTT may be asked to review the decision and may or may not accede to that request OR matter could be taken to Supreme Court.

### **MODEL APPLIED TO MYSITUATION**

Based on the time frames in the QLD model, as given to this Inquiry, it would have taken less than 3 months and no expenditure to get to a point where I could submit an insurance claim. This can be compared with the 5 years, \$65,000 in legal fees and \$60,000 in rent it has taken under the present system in NSW.

### ***Advantages of the Proposed System for Builders, Home Owners and Insurers***

Advantages of the proposed system over the existing system are;

- The process is fully available to both builders and consumers where as the existing system is not.
- The steps in the process for the home owner are significantly less resulting in both a reduced cost to the builder and home owner and a reduced time for resolution of the dispute.
- The reduced time for resolution of the dispute will result in lesser claims for items such as alternate accommodation thus reducing the cost to the insurers.

- There is a lesser involvement of lawyers as a matter only needs to go to the CTTT once and there is no requirement for liquidation, thus reducing costs.
- The CTTT is provided support in its role and as such the risk of making determinations that are wrong or will be challenged is reduced.
- The financial barriers (cost of CTTT hearings etc) which must be overcome before an insurance claim can be submitted are greatly reduced making the system more available to builders and home owners.
- As orders are either the payment of monies due under the contract or works to be undertaken, disputes about the cost of rectification works do not arise, nor can either party wrangle the system to gain advantage or a windfall gain over what was specified in the original contract.
- The avenues for challenge are only available to challenge the Order made by HBS and as such matters need only go to the CTTT once.
- The home owner does not have to repeat the steps in the construction of a house such as engaging a builder, managing that builder, progress payments, inspections etc to achieve the house specified in the original contract.
- The requirement to have to pay a second or even third insurance premium for the completion of the same works is avoided.
- The process in part limits conflict to that which is contained in the Order making the dispute resolution process less personal and easier to manage.
- There is finality for all parties in the proposed system whereas the existing system may cause the complete dispute resolution system to be repeated after the home owner has engaged a new builder.

## **COMMENT ON PROPOSED HIA MODEL**

Within the HIA Submission there is a proposal to improve the system by adding an additional trigger being the cancellation of a builder's licence. Within the submission it is specifically stated that the failure of a builder to undertake work as ordered should not be a trigger for Home Warranty Insurance. Unless the failure to undertake work as ordered triggered the cancellation of the licence and hence the insurance there is no benefit to the consumer.

In the system with the additional trigger a consumer may well have to go through Stages 1,2 and 3 of the existing system as described above. Thereafter an order would need to be placed on the builder to do work, similar to Stage 4 described above. The refusal to do the work would then be used as the trigger to cancel the licence.

The builder could then appeal extending the process further. In such a case it may provide no benefit to the consumer. The only way it could be of benefit is if the trigger for losing the license comes much earlier in the system, that is after a direction to do work but if that as the case it would deny the builder natural justice.

It would appear that the inclusion of the additional trigger would only benefit consumers if the builder's licence had been annulled through separate proceedings as the process to have a builder's licence cancelled is equally as long or longer than the process to have the builder liquidated.

Secondly the trigger does nothing to address the issues with the insurance companies and the positions they have taken in respect to providing the indemnity to the consumer. It does not address the ability of either party to drag the matter out through further litigation in the CTTT and provides no finality in respect to the actual items in dispute. Further it does nothing to address the sureties etc required of the builder.

## **COMMENT ON ADDITIONAL TRIGGER OF NON COMPLIANCE WITH ORDER**

There has been discussion about the inclusion of another trigger for access to insurance. That trigger being non compliance with a monetary order of the CTTT.

In the system with the additional trigger a consumer may well have to go through Stages 1,2 and 3 of the existing system as described above. Thereafter an order would need to be placed on the builder to pay in a similar manner to that described in Stage 4 above. The refusal to do the pay would then be used as the trigger to cancel the licence.

Although the intention of the trigger may be to speed up the process, the only step it removes from the process is the step of liquidation. I would do nothing to address the situation where the builder is ordered to do works but refuses to do so.

The trigger does nothing to address the issues with the insurance companies and the positions they have taken in respect to providing the indemnity to the consumer. The additional trigger would do nothing to prevent the insurer continuing litigation within the CTTT and other jurisdictions, causing delay and eventually causing the consumer running out of funds to pursue the matter. It would do nothing to provide finality in respect to the actual items in dispute.

In my case the inclusion of the trigger would have reduced a four and a half year process to a four year process. It is considered that this is still an unacceptably long time period during which I had to continue to pay for alternate accommodation and legal costs.

The additional trigger would do nothing to address issues with the CTTT in the assessment of building claims; that is the situation where a person unskilled in building matters was making decisions on building matters.

The inclusion of the trigger alone would do nothing to prevent the CTTT making findings contrary to the EP&A Act and the insurer using the decision of the CTTT as a reason not to fix or pay to have fixed the house such that it complies with the contract, conditions of consent and contract.

## **COVERAGE OF INSURANCE**

The NSW Home Building Regulations state the insurance policy must indemnify the beneficiaries under the policy for any loss or damage and include legal costs and cost of alternate accommodation. This is consistent with the principles of Hadley v Blaxendale.

Limitations on liability are described in Clauses 56, 57 and 58 and those limitations do not, on face value, limit the indemnity for rectification, legal costs and cost of

alternate accommodation. They do not cap the indemnity to be provided by the insurance.

At this stage, as evidenced in my first submission to the Inquiry, Home Warranty Insurance does not cover the rectification of works, legal costs incurred nor the cost of alternate accommodation. If required the documentary evidence to support this statement can be provided. Further it is considered by the insurance company (Vero) that their liability is capped at \$200,000 (now \$300,000 for contracts entered into more recently).

To provide consumer protection the insurance must indemnify the beneficiary against events and costs incurred which were

- Foreseeable
- Within the control of the builder
- As a result of the actions of the builder

It should not indemnify against things such as earthquake or terrorist attack being items outside the control of the builder nor changes in legislation or things so remote as to not be foreseeable such as loss of share market investment opportunities unless specifically included in the building contract. They should not indemnify the beneficiary against actions taken by the beneficiary which impact on the building process.

The opportunity should be made for owners to seek additional insurance for events such as earthquake or wet weather, if the beneficiary so desires. This additional cover would be provided at an additional cost.

To ensure insurance policies provide the coverage as intended by government the wording of policies should be mandated and no cap on the indemnity provided. If insurance remained in the private sector differentiation between insurers would be provided by:

- Cost of insurance (determined by risk profiling of individual builders);
- Additional coverage for items such as rain which are addressed in the building contract and the risk would normally remain with the beneficiary; and
- Additional coverage for items covered beyond those in the building contract.

### ***Advantages of Mandated Policy to Consumer***

The primary advantage is that the consumer will receive the protection intended by the Act, that is, to be placed in a position he or she would have been if the work was undertaken properly.

## **GOVERNMENT AS PRINCIPAL INSURER**

### ***Description of Proposal***

In NSW and other states with the exception of QLD and now TAS the insurance is provided and managed by the private sector. As such the collection of premiums, assessment and payment of claims and the carriage of the associated risks are all undertaken by the private sector.

At present the exposure of the private sector insurers to risk is limited to \$10m for a single event. There after the risk is assumed by government.

As principal the private insurers have historically made significant profits from home warranty insurance as demonstrated by both balance sheets and the willingness of



new insurers to enter this market. Financial reports from the Building Services Corporation in QLD also demonstrate substantial profits can be made and, if Government is the insurer, returned back into the industry.

After reading and considering the submission of the Queensland Building Corporation, if such a system was implemented the majority of concerns I have would be addressed. The only ones not addressed would be the meeting of legal costs and alternate accommodation, costs which should be met on the principals of Hadley v Blaxendale; that is the owner should be placed in a position, in so far as money can, that he would have been if the work was done properly.

The only other concern is that the insurance should not be capped. Advice from OFT in NSW has indicated very few claims exceed the present "minimum insurance requirements" of \$300,000 so to have an uncapped scheme would pose little risk to Government.

If a scheme based on the QLD model were to be implemented the insurance risk would be carried by government as they do now for incidents over \$10m and any profits made, as they are presently made, returned to government.

A view has been expressed by the Minister of Fair Trading in NSW that it would be too expensive for government to set up a new government run home warranty insurance scheme. She quoted a figure of \$66m as compared to the \$70m profit made by the previous (before privatised Home Warranty Insurance) scheme in NSW. The profits from the previous scheme could be used to set up the new scheme.

Transitional arrangements could be made by novating the existing insurance contracts to the government insurance. In doing so policies could be amended to provide a trigger for claim being the non compliance with HBS Orders thus reducing the possible payouts under these policies as outlined in the advantages of the alternate dispute resolution system.

### ***Advantages of Government as Insurer***

Advantages of Government as Insurer are

- There would be no tension between the insurer's requirement to maximise profit yet make payouts to home owners and as such the focus would be consumer protection.
- Profits from the scheme (as demonstrated as being available in the QLD scheme) would be retained by government or returned to the building industry through training programs and other support.
- A single policy would be used which would reflect and be used to fulfil the intent of government as it would be interpreted by government.

There would only be a minimal increase in risk to government as at present government assumes the risk for incidents over \$10m. In the alternate government would retain the profits present made by the insurers and commissions presently paid by insurers.

Transitional arrangements would be relatively easy to make and implement.

## **RECOMMENDATIONS**

It is recommended that

- The dispute resolution system be revised to that proposed to reduce costs to all parties including the insurer and allow the speedier resolution of disputes.

- The basic Home Warranty Insurance policy wording be mandated with options being provided for additional coverage.
- The Home Warranty Insurance be provided by Government in a manner roughly consistent with the QLD model, the exceptions being the costs to be met and the removal of a cap on insurance.