LEGISLATIVE COUNCIL
STANDING COMMITTEE ON
LAW AND JUSTICE


Response by Government

August 2003
In September 2002 the Legislation Council's Standing Committee on Law and Justice published its report on the *Home Building Amendment (Insurance) Act 2002* (the Amendment Act). The Amendment Act made changes to the home warranty insurance scheme established under the *Home Building Act 1989*. The purpose of the scheme is to protect consumers against loss arising from faulty or incomplete building work undertaken by licensed builders and tradespeople. The insurance scheme commenced in May 1997 and replaced the former government-run scheme. Cover under the scheme is provided by the insurance industry.

The reforms contained in the Amendment Act followed a joint announcement in March 2002 by the NSW and Victorian Governments of changes to their home warranty insurance schemes. These changes were made in response to concerns raised by the insurers about the future viability of the schemes and the threatened withdrawal of re-insurer support. The changes to the schemes were intended to help ensure their long term viability.

In April 2002 the monetary threshold for work requiring insurance was lifted from $5,000 to $12,000 by an amendment to the *Home Building Regulation 1997*. Subsequently, Parliament passed the Amendment Act which:

- introduced 6 years cover for structural defects and 2 years cover for non-structural defects (7 years cover for all defects previously applied);
- set a cap on claims for incomplete building work equal to 20% of the original contract price; and
- provided that home owners are only able to claim against their policy as a last resort, that is, where the builder is dead, has disappeared or is insolvent. Previously, the consumer, in some circumstances, could lodge a claim immediately with the insurer where defective work was identified.

These legislative changes took effect on 1 July 2002.

When the Amendment Act was passed by the Legislative Council it resolved to refer the legislation to the Standing Committee on Law and Justice for inquiry. The Committee's terms of reference were to investigate the impact of the Amendment Act on home warranty insurance, home builders and consumers.

The Committee's report was published in September 2002. The Committee Chair, the Hon Ron Dyer MLC, in his forward to the report stated that the Committee had noted that the move to a "last resort" scheme aligns NSW with the schemes in Victoria, South Australia, Western Australia, the ACT and the Northern Territory. He went on to say that this reform and others in the Amendment Act are in line with the findings of the National Review of Home Builders Warranty Insurance and Consumer Protection conducted for the Ministerial Council on Consumer Affairs by Professor Percy Allan AM. The Committee also found that the Amendment Act has been successful in achieving its aim of stabilising the home warranty market. However, the Committee asked the Government to consider some issues relating to the manner in which the Amendment Act impacts on builders and insurers. In this regard, the Committee made 16 recommendations for consideration.
Since the release of the Committee's report, the Government has moved to introduce major reforms for the home building industry arising out of the Joint Select Committee Inquiry into the Quality of Buildings (Campbell Inquiry). In the 2002 Spring Session Parliament passed the Building Legislation Amendment (Quality of construction) Act 2002. This Act amended the Environment and Planning and Assessment Act 1979 and the Home Building Act 1989. The reforms to the Home Building Act comprise a new dispute resolution process for consumers and licensed builders/tradespeople; a financial soundness test for licensees and certain mandatory conditions for building contacts. The new dispute resolution process commenced on 1 July 2003. The other reforms are still to commence.

Disputes are now notified at one of the Fair Trading Centres that are located around the State. Depending on the nature of the dispute it may be referred to a building inspector. Where the inspector determines there are defects, incomplete work or damage as a result of the licence holder's work, a rectification order may be issued. Failure to comply with the order is a ground for taking disciplinary action. Where the dispute cannot be resolved through the intervention of the inspector the consumer is normally advised to lodge a building claim with the Consumer, Trader and Tenancy Tribunal.

The new dispute resolution process is intended to reduce the number of matters that have to be heard by the Tribunal and the number of potential insurance claims.

In May 2003 an Inquiry into the Home Warranty Insurance Scheme was announced. The Inquiry is chaired by Mr Richard Grellman. As part of the Inquiry's terms of reference it will consider whether the legislative framework governing home warranty insurance (including changes made to the scheme in 2002) is currently effective for consumers and industry.

The Inquiry’s interim report was provided on 30 June 2003 and can be accessed on www.nswwhi-inquiry.com. The Inquiry’s final report, with reform recommendations, is to be provided to the Governor by the end of September 2003.

Set out below are the recommendations of the Standing Committee on Law and Justice and the position as at August 2003. In a number of instances the issue raised by the Committee is being reviewed as part of the Inquiry into the Home Warranty Insurance Scheme being conducted by Richard Grellman.

**Recommendation 1**

The Committee recommends that the New South Wales Government should continue with the implementation of a data collection procedure for the home warranty insurance market. The Minister for Fair Trading should specify, as part of the Conditions for Approval of insurers, that they must supply the Government with detailed market data concerning home warranty insurance premiums, claims and payouts.
New reporting requirements for insurers have been in place since late 2002. These, among other things, require the submission of returns by insurers relating to policy sales, claims activity and premiums.

Draft revised Conditions of Approval were issued to the insurers for comment in July 2003. These include a Code of Practice for insurers. The new reporting requirements are continued in the revised Conditions of Approval.

Recommendation 2

The Committee recommends that the Minister for Fair Trading consider, as a matter of priority, the recommendations of the National Review of Home Builders Warranty Insurance and Consumer Protection, with a view to promoting the consumer protection aims of the New South Wales Home Warranty Insurance Scheme as well as a competitive and viable home warranty insurance market.

The recommendations of the National Review have been considered. A number of the recommendations have already been adopted. A Working Party of Officials of Consumer Affairs from the various States and Territories is considering and reporting on issues that can be researched/further developed to move towards areas of common or national consistency and improved effectiveness. The Working Party's response to the National Review was submitted to relevant Ministers in early 2003.

Recommendation 3

The Committee recommends that the Department of Fair Trading, in collaboration with insurers and industry associations, develop information for consumers clearly explaining the nature of home warranty insurance with particular emphasis on its last resort nature.

The Office of Fair Trading is developing a consumer information brochure that must be given by licensees to consumers when entering into a contract. This will explain the operation of insurance and the process for resolving disputes. Under the revised Conditions of Approval insurers will have to provide Plain English consumer information.

Recommendation 4

The Committee recommends that the Department of Fair Trading work with home building industry associations to develop information that clearly sets out the obligations of builders in relation to home warranty insurance and statutory warranties.

The Office of Fair Trading has consulted with the industry in relation to the new dispute resolution process that came into force on 1 July 2003 as well as the proposed consumer information brochure. The Office of Fair Trading has
also published a customer service guide for builders and other publications on these issues.

**Recommendation 5**

The Committee recommends that the Department of Fair Trading provide advice to the Swimming Pool & Spa Association of NSW Limited as to how the definition of 'structural defect' in section 57AC the *Home Building Regulation 1997* applies to all aspects of the construction of swimming pools and spas.

The Office of Fair Trading has written to the Swimming Pool & Spa Association (SPASA) about this issue.

However, it is the responsibility of the insurer to assess whether a defect is of a structural or non-structural kind based on the definition contained in the legislation.

**Recommendation 6**

The Committee also recommends that the particular characteristics of swimming pool and spa construction be incorporated into the proposed guideline document suggested in Recommendation 7.

The Office of Fair Trading in conjunction with the Department of Infrastructure, Planning and Natural Resources has developed a guide similar to the Victorian Guide to Standards and Tolerances. The Guide is now available to the public.

When the Guide was being developed it was circulated to industry associations, including SPASA for comment. SPASA did not submit any recommendations for change. It is intended that the Guide be updated from time to time to reflect any changes in the Building Code of Australia or other relevant standards.

**Recommendation 7**

The Committee recommends that the Department of Fair Trading develop a guide for use in New South Wales along the lines of the Victorian Guide to Standards and Tolerances. The Committee also recommends that the guide should identify which defects fall within the definition of structural defects and which fall into the residual category of non-structural defects.

See answer to Recommendation 6
Recommendation 8

The Committee recommends that the Minister for Fair Trading ensure that an appropriate regulatory framework is imposed on new alternative indemnity arrangements that it approves under s 102A of the Home Building Act 1989.

A number of guidelines were approved by the former Minister for Fair Trading in August 2002. Further conditions will be considered depending on the nature of any schemes lodged for approval. The need and requirements for alternative indemnity schemes will be re-examined in light of the recommendations from the Inquiry into the Home Warranty Insurance Scheme (the Grellman Inquiry).

Recommendation 9

The Committee recommends that the New South Wales Government consider examining the 20% limitation on liability for non-completion of work with a view to determining the impact of this reform on consumers.

The impact of this reform and the other changes introduced by the Amendment Act is being examined by the Grellman Inquiry.

Recommendation 10

The Committee further recommends that the New South Wales Government give consideration to amending the Home Building Regulation 1997 to provide that, instead of limiting liability resulting from non-completion of building work to 20% of the contract price, a contract of insurance may limit liability resulting for non-completion of building work to an amount that is ‘20% of the sum insured or 20% of the contract price, whichever is greater.’

The Grellman Inquiry is considering whether the existing legislative framework is effective for consumers and industry.

Recommendation 11

The Committee recommends that after the Home Building Amendment (Insurance) Act 2002 has been operational for six months, the Minister for Fair Trading should consider the impact that the reforms have had on dispute resolution resources with a view to meeting any additional demands on the Consumer Trader and Tenancy Tribunal and the Building Conciliation Service.

Following the passage of the Building Legislation Amendment (Quality of Construction) Act 2002 a new dispute resolution scheme has been established and commenced on 1 July 2003. The Building Conciliation Service has been wound up. The Office of Fair Trading will review the impact of the insurance reforms on the dispute resolution scheme and the operation of the Consumer, Trader and Tenancy Tribunal.
Recommendation 12

The Committee recommends that the New South Wales Government take the issues raised in relation to the experiences of builders in relation to the New South Wales Home Warranty Scheme, as set out in paragraphs 4.92-4.98 of this report into consideration as part of any future review of the scheme that it may undertake.

As part of the revised Conditions of Approval for insurers the issues of service delivery, transparency of financial criteria and insurer conduct are being addressed. These issues will be further reviewed in light of the recommendations of the Grellman Inquiry.

Recommendation 13

The Committee recommends that the Department of Fair Trading investigate allegations that some builders are working without obtaining insurance required by legislation and engaging in practices such as contract splitting to avoid insurance obligations.

These issues will be examined as part of the Office of Fair Trading’s compliance programs for the home building industry. Further, under the new dispute resolution process that started on 1 July 2003 building inspectors will investigate complaints against licensed contractors. If during an investigation a breach of the insurance provisions is detected it will be referred to the compliance area for necessary action.

Recommendation 14

The Committee recommends that the New South Wales Government examine the possibility of a supplementary catastrophic fund to consider claims from consumers who had received full payment of $200,000 from a home warranty insurance policy and still require additional funds to demolish/rectify or reinstate a building that was constructed for the purpose of being their principal residence.

The coverage to be provided under home warranty insurance will be examined by the Grellman Inquiry.

Recommendation 15

The Committee recommends that the New South Wales Government take the issues raised in relation to the experiences of consumers of the New South Wales Home Warranty Scheme, as set out in paragraphs 4.110-4.118 of this report, into consideration as part of any future review of the scheme that it may undertake.

The issues raised by the Building Action Review Group and other consumer advocates relating to the extent of cover; delays in claims handling; the
definition of “completion of building work” for the purpose of lodging claims; the right to make a claim where the builder has breached the contract and the administration and enforcement of the scheme will be reviewed in light of the recommendations of the Grellman Inquiry.

In relation to the quality of building work and dispute resolution, reforms were passed by Parliament in the Building Legislation Amendment (Quality of Construction) Act 2002. These reforms relate to certification, dispute resolution and contracts. The new dispute resolution system commenced on 1 July 2003. Certain mandatory conditions for contracts are expected to commence later in 2003.

**Recommendation 16**

The Committee recommends that the Minister for Fair Trading consider implementing a ‘Builder’s Choice Award’ in New South Wales, along the lines of that operating, in Alberta, Canada.

The Office of Fair Trading will be undertaking a feasibility study on the rating of builders.

John Della Bosca MLC