Submission

No 20

INQUIRY INTO THE OPERATIONS OF THE HOME BUILDING SERVICE

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Subject:

Summary

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The Hon Jenny Gardiner MLC
Committee Chair
General Purpose Standing Committee No.4
Parliament House
Macquarie Street
SYDNEY NSW 2000

Dear Ms Gardiner

Inquiry into the operations of the Home Building Service

Thank you for the invitation to make a submission to the Inquiry.

The Terms of Reference of the Inquiry have been addressed by the Society's Property Law Committee. The Committee is comprised of senior practitioners and property law experts. Due to time constraints the Council of the Law Society has not had the opportunity to consider the issues raised by the Terms of Reference. The comments that appear below are those of the Committee alone.

The Committee's comments relate only to those issues that are within its areas of expertise.

Members of the Law Society are most frequently involved with the operation of the Act when advising vendors, purchasers and incoming mortgagees about the requirements on sale of properties on which residential building work has been done. Other areas in which members of the Society are occasionally involved are in advising consumers about the terms of proposed building contracts (although anecdotal evidence suggests that relatively few consumers will as a matter of course seek legal advice about the content of a proposed contract), or in representing clients in litigated building disputes. This submission will focus most closely on these areas.

References in this submission to sections and clauses refer to the *Home Building Act 1989* and the Home Building Regulation 2004 respectively, unless indicated to the contrary.

a) THE BUILDER LICENSING SYSTEM

The Committee supports the licensing regime as fulfilling an important consumer protection function.

The Committee recognises benefit in co-operation with various regulatory bodies in other jurisdictions to harmonise the licensing regimes in various States.

b) THE HOME WARRANTY INSURANCE SCHEME

This regime is the area which has the greatest impact on the Society's members.

It is also an area which gives rise to frequent complaints by members and their clients.

The main broad areas of concern, namely complexity, inconsistencies, frequency of change, "gaps" in coverage are set out in more detail below.

Specific areas relating to complexity

1. Some key concepts undefined (e.g. "person who does building work otherwise than under a contract" – see section 96), or defined for limited purposes only (e.g. when building work is "completed" is defined for the purposes of coverage under a policy of insurance in clause 61, but not for, for example, delimiting obligations on sale in sections 95, 96 and 96A), or in a convoluted and sometimes self-referencing manner (e.g. to determine who is an owner-builder, regard must be had to sections 3, 29 and 90).

2. The provisions detailing the obligations of some vendors on sale (sections 95, 96, 96A) are poorly drafted. For instance, each of the sections gives a right to a purchaser to rescind for a breach of certain obligations imposed by the section at any time "before the completion of the contract" (sections 95(4), 96(3A) and 96A (3)). In each case the right is lost if the vendor serves a certificate of insurance "before completion of the contract" (sections 95(4A), 96(3B) and 96A (3A)). The conceptual difficulty is that if the right to rescind is exercised the contract is never in fact "completed" (as that term is understood in the conveyancing sense) and so on one view a contract validly rescinded under the first provision could be revived if the vendor followed the steps set out in the second provision. Furthermore, the drafting of section 95 probably contains an incorrect cross-reference. As the section stands, one can cure a lack of insurance as at the date of making of the contract for sale (a breach of section 95(1)) by providing a copy of a certificate evidencing insurance, provided the certificate had been obtained prior to the date of making of the contract for sale (section 95(4A)). It is probable that the rescission provision in section 95(4) was intended to refer to the right of rescission arising on a contravention of section 95(2) rather than for breach of subsections (1) or (2A).

3. Where work is done over a lengthy period of time (particularly where performed by an owner-builder or a person who is doing work otherwise than under a contract) it is unclear whether the work constitutes a number of separate instances of building work or should be aggregated – of relevance to determine whether the work reaches the thresholds referred to in Part 6.

4. The Part 6 thresholds have been increased by regulation from $5000 to $12,000. It would be helpful if in due course that increase was incorporated into the Act.

Specific areas relating to inconsistency

1. The treatment of owner-builders under the Act is different from, and more onerous than, the provisions relating to developers and persons who do building work otherwise than under contract. For instance, the developer and person who does building work otherwise than under contract must on sale provide a brochure from the OFT (sections 96(2B), 96A (1A)). A breach attracts a maximum penalty of 40 penalty units. The corresponding obligation for an owner-builder is to attach a "conspicuous note" to the contract (section 95(2A)). A breach attracts a maximum penalty of 1000 penalty units and grounds a right of rescission in the purchaser.

2. To take a further example, the definition of owner-builder is limited to someone who obtains an owner-builder permit – one consequence of this is that someone who has obtained a permit is subject to stricter obligations on sale than someone who has done the work without obtaining a permit at all.

Frequency of change

The Act has had 32 "historical versions" in force since July 2000. The current and former Regulation has had the same number of historical versions in force since July 2001 – to take one specific example, the 1997 Regulation had substantive differences between the versions current on 30 December 2003, 31 December 2003 and 1 January 2004. The majority of amendments went beyond mere technical or mechanical changes to the home warranty insurance regime. Additionally, amending statutes frequently have had several different commencement dates (the history of the *Home Building Legislation Amendment Act* 2001 is particularly instructive).

Gaps in coverage

1. *Coverage of multi-storey buildings*

   The Committee considered the most telling gap in the operation of the domestic building regime is the removal of the insurance requirement for multi-storey buildings with effect from 31 December 2003 (clause 74). The Committee is of the view that owners of residential high-rise lots are arguably in greater need of protection under an insurance scheme than owners of, for instance, free-standing dwellings. One reason for this is that the involvement of a strata owners corporation which is the owner of some, but not all, parts of the building work means that claims involving strata buildings will involve more parties, and frequently be more complex and expensive, than claims involving free-standing dwellings. Another difficulty is that while the High Court has held that the builder of a house owes a duty of care to a subsequent owner of the house, and therefore may be liable in negligence to that subsequent owner (*Bryan v Maloney* (1995) 128 ALR 163), the Court has held that the principle does not extend to circumstances where the building work is a warehouse and factory complex (*Woolcock Street Investments Pty Ltd* v *CDG Pty Ltd* [2004] HCA 16). The latter decision strongly suggests that tort law may not protect the subsequent owner of a residential strata lot. The following extract from the joint judgment of Gleeson CJ, Gummow, Hayne and Heydon JJ squarely raises the issue (at [17], emphasis added):

> ... [I]t may be doubted that the decision in *Bryan v Maloney* should be understood as depending upon drawing a bright line between cases concerning the construction of dwellings and cases concerning the construction of other buildings. If it were to be understood as attempting to draw such a line, it would turn out to be far from bright, straight, clearly defined, or even clearly definable. As has been pointed out subsequently, some buildings are used for mixed purposes: shop and dwelling; dwelling and commercial art gallery; general practitioner's surgery and residence. **Some high-rise apartment blocks are built in ways not very different from high-rise office towers. The original owner of a high-rise apartment block may be a large commercial enterprise.** The list of difficulties in distinguishing between dwellings and other buildings could be extended.

Unhappily the question of whether a subsequent owner of a residential strata apartment has a claim against the builder independent of any statutory protection may ultimately require resolution in subsequent litigation, presumably to be finally determined by the High Court. The uncertainty in the meantime creates enormous practical difficulties for all stakeholders, especially consumers.

The Committee appreciates that the decision to exclude multi-storey buildings was triggered by a reluctance of the home warranty insurers to continue to underwrite such projects. However, the Committee also observed that section 102A contemplates the possibility of alternative home building indemnity schemes or arrangements, and was strongly of the view that the interests of consumers would be well served by the creation of such a scheme to protect owners in residential multi-storey buildings. Such schemes could include provision for a retention sum or bank guarantee to be held by the owners corporation for a specified period.

2. *The Onerati Principle*

On 4 November 2005 the Law Society wrote to the Commissioner for Fair Trading expressing its concern about the unsatisfactory state of the law following the decision of Master Harrison (as she then was) in *Honeywood* v *Munnings* [2005] NSWSC 515. The principle was further explored in the Court of Appeal (*Honeywood as executrix of the estate of the late Neville Honeywood* v *Munnings & Anor* [2006] NSWCA 215). The Committee was pleased to note the recent introduction of the Home Building Amendment (Statutory Warranties) Bill 2006 which will hopefully clarify the law on whether the *Onerati* principle is of continuing relevance. One area of concern with the Bill was the potential retrospective operation of the amendment.

3. *The comatose builder*

In the same submission the Law Society referred to the decision of *Chapman* v *Taylor & Or; Vero Insurance Ltd* v *Taylor* & Ors [2004] NSWCA 456. Unlike the *Honeywood* decision, the Committee is not aware of any attempt to resolve the issue raised by *Chapman*. The following extract from the November 2005 correspondence encapsulates the issue:

> "In this matter, proceedings in the CTTT were instituted by a claim by Mr and Mrs Taylor for damages from Mr Chapman, a builder, for breaches of a building contract, and for indemnity from Vero under an insurance policy issued pursuant to the HBA.

After work under the contract had commenced, Mr Chapman was injured and remained in a coma as a result of his injuries for a period of approximately five weeks. He was unable to undertake or supervise the work under the contract for a period of about five months.

The Court of Appeal held that the contract had been frustrated as a result of Mr Chapman's injuries.

Hodgson JA at paragraph 40 of his judgement (with which Tobias JA and Beazley JA agreed) stated:

> '40 However, the HBA makes specific provision in section 99(1) (a) for insurance against non-completion due only to the death, disappearance and insolvency of the builder, but omits that provision where non-completion is due to supervening incapacity of the builder. **The facts of this case suggest that this is an anomalous omission in the legislation.** There is some tension between a proposition that the builder is absolved by frustration from further performance of the contract, yet remains liable under the warranty if the building is not complete. On the whole, I think the Court must recognise an inadequacy in the provisions of the HBA in this respect, rather than hold that the statutory warranties can still in effect require completion by the builder when the contract is put to an end by frustration.' [emphasis added]

The Society agrees that section 99(1) of the HBA should be amended to provide for insurance to cover cases of non-completion due to supervening incapacity of the builder."

PARAGRAPHS (C) AND (D)

The Committee does not wish to comment on paragraphs (c) and (d) of the Terms of Reference as these relate to issues outside its areas of expertise.

(e) THE ENFORCEMENT OF RELEVANT LEGISLATIVE AND REGULATORY PROVISIONS

The Committee commented earlier on the frequency of change to the legislative and regulatory provisions. As noted, the majority of amendments have gone beyond mere technical or mechanical changes to the home warranty insurance regime. This has resulted in difficulties in advising on enforcement matters.

(f) THE ESTABLISHMENT OF A HOME BUILDING ADVICE AND ADVOCACY CENTRE

The Committee supports the separation of the regulatory role and consumer protection advocacy.

A major concern, under earlier schemes was the criticism levelled at the former Building Services Corporation and Builders Licensing Board for attempting to carry out the roles of "judge jury and executioner". Their roles as a regulator of industry could be perceived as inconsistent with the consumer protection function and the role as source of funds for the insurance scheme. The Committee believes this holds true today.

While the Committee sees no difficulty with Office of Fair Trading providing information about the operation of the Act, the role of consumer protection advocacy should be carried out by independent advocates.

CONCLUSION

The Society notes that its delegates will have the opportunity to address the Parliamentary Committee directly in relation to these issues at the hearings to be held on 20 November 2006.

The Society takes this opportunity to express its appreciation to the Parliamentary Committee for the opportunity to address the issues raised by the Inquiry both through this submission and at the hearing

Yours faithfully

June McPhie
President