

Submission

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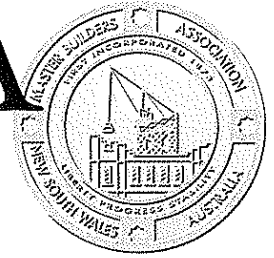
INQUIRY INTO THE OPERATIONS OF THE HOME BUILDING SERVICE

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Telephone:
Date Received: 9/11/2006

Subject:

Summary

MBA



8 November 2006

The Director
General Purpose Standing Committee No. 4
Parliament House
Macquarie Street
SYDNEY NSW 2000

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Dear Sir

**RE: MASTER BUILDERS ASSOCIATION OF NSW – SUBMISSION FOR
INQUIRY INTO THE OPERATIONS OF THE HOME BUILDING SERVICE**

Please find attached the Master Builders Association of NSW submission concerning the Inquiry into the Operations of the Home Building Service for your attention.

Should you wish to discuss this document, please do not hesitate to contact me on (02) 8586-3503.

Yours faithfully

Brian Seidler
Executive Director
MASTER BUILDERS ASSOCIATION OF NSW



MASTER BUILDERS ASSOCIATION OF NSW

SUBMISSION

INQUIRY INTO THE OPERATIONS OF THE HOME BUILDING SERVICE

NOVEMBER 2006

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Introduction

The New South Wales residential building industry is held up as having a major influence on both State and Federal economies, and as a major generator of revenue at a Local Government level. The New South Wales housing industry provides 133,000 jobs, produces approximately 43,000 homes per annum, with a worth of approximately \$6 billion, with a further \$4 billion provided by the home improvement sector. The importance of a vibrant residential sector on the three levels of government is often highlighted by governments and politicians.

Since 1992 there has been approximately eight (including the current inquiry) significant inquiries into licensing, insurance and the general operations and administration of the New South Wales residential sector. These inquiries were:

- The 1992 Dodd Inquiry into the Building Services Corporation
- The 1996 Review of Licensing in the Home Building Industry
- The 2002 National Review of Home Warranty Insurance and Consumer Protection
- The 2002 Joint Select Committee Inquiry on the Quality of Buildings
- The Standing Committee on Law and Justice, Review of the impact of the *Home Building Amendment (Insurance) Act 2002*
- The 2003 NSW Home Warranty Insurance Inquiry
- The 2005 Review of Licensing in the Home Building Industry
- The current inquiry, the Inquiry into the Home Building Service

As frequent as there have been inquiries into the industry, there has been the revolving list of Ministers responsible for Fair Trading and the subsequent licensing and administration of the residential sector:

- | | |
|----------------------|-----------------------------------|
| 1. Faye Lo Po' | 06/12/1995 – 01/12/1997 |
| 2. Brian Langton | 01/12/1997- 30/04/1989 |
| 3. Jeff Shaw | 30/04/1998 – 08/04/1999 |
| 4. John Watkins | 08/04/1999 – 21/11/2001 |
| 5. John Aquilina | 21/11/2001 – 02/04/2003 |
| 6. Reba Meagher | 02/04/2003 – 21/01/2005 |
| 7. John Hatzistergos | 01/02/2005 – 03/08/2005 |
| 8. Diane Beamer | 03/08/2005 – and current Minister |

Consequently, the industry has also been confronted with an endless stream of regulatory reform flowing from continual inquiry and ever changing Ministers.

The Terms of Reference of this inquiry provide no background as to what has initiated the inquiry.

Master Builders has therefore based our submission upon information found in the transcripts of the recent meeting of the General Purpose Standing Committee No 4 (Budget Estimate Committee).

It appears from these transcripts, that this inquiry is the result of lobbying by a consumer activist group - the Building Action Reform Group (BARG), and the failure by the Minister for Fair Trading to undertake a performance audit of the operation of the Home Building Service, pursuant to Section 145 of the *Home Building Act 1989*. It also appears that BARG has raised concerns regarding the adoption of the recommendation of the Campbell Inquiry for the establishment of a Home Building Advice and Advocacy Centre. Furthermore, there also appears to be grievances in relation to decisions on insurance claims under the administration of the Building Insurance Guarantee Corporation (BIG Corp).

The Home Building Service

The Campbell Inquiry recommended the establishment of a new authority independent of the Office of Fair Trading (OFT).

The establishment of the Home Building Service (HBS) under the administration of the OFT was the NSW Government's response to the Campbell Inquiry and we submit did not give the independence such a body requires.

Whilst Master Builders believes the structure of building regulation should be altered, the management and current operations of the Home Building Service (HBS), especially over the past twelve to eighteen months has been proactive, responsive and undertaken with a much clearer line of communication than that which previously existed.

What is of importance at this time is that the HBS has provided Master Builders with timely responses to issues that we have raised with senior HBS officers which has contributed to improved consultations and negotiations over industry issues and concerns.

An increased level of field activity and compliance work undertaken by HBS officers needs to be recognised as both good for administration and particularly good for improving industry performance with consequent increased consumer protection. The current compliance work of the HBS has resulted in substantial penalties, including custodial sentences, resulting from prosecutions launched by the HBS.

Master Builders has also had a representative on the Home Building Advisory Council (HBAC) and consequently has been privy to reports from the HBS on the implementation of reforms resulting from the Campbell and Grellman Inquiries. We have also been provided with a copy of the 2005 report by the Office of Fair Trading, on the Outcome of the Review of the Home Building Act 1989.

Whilst the Home Building Act needs to be rewritten so that it is easier to understand and as a means of simplifying things like work orders and dispute resolution, the HBS from our perspective is doing its work effectively.

The sheer size of the domestic construction industry means that in some instances problems will arise regarding work done, the licensing of people and the resolution of complaints.

As raised above, Master Builders is of the view that the establishment of the Home Building Service (HBS) is not a satisfactory response to the Campbell Inquiry, especially in regard to its recommendation for a new authority to be independent of the Office of Fair Trading. The current structure of the Office of Fair Trading (OFT) retains a direct link between the Commissioner for Fair Trading and the Home Building Service and consequently there is no clear separation in the operations of the HBS because of the clear link remaining with the Commissioner of Fair Trading.

Master Builders would prefer to move building regulation, dispute resolution, industry performance and consumer confidence forward by seeking the establishment of an Independent Building Commission (IBC).

Performance Audit

The absence of a performance audit is not an overly significant issue for Master Builders at this time as we are reasonably satisfied at the response to our enquiries and queries by the HBS.

Master Builders has had a representative on the Home Building Advisory Council (HBAC) and consequently, we have had reports from the HBS on the implementation of reforms resulting from the Campbell and Grellman Inquiries. We also had been provided with a copy of the 2005 report by the Office of Fair Trading, on the Outcome of the Review of the Home Building Act 1989. This report noted the insertion into the Act of the review provisions relating to the Home Building Compliance Commissions.

In July 2004, the HBAC was provided with agenda papers with an attachment containing an Operational Review of the Home Building Service. This Operational Review identified that consideration was being given to the combining both reviews required under section 145 of the Act (i.e. Home Building Act and Home Building Compliance Commission), with the intention of a report being submitted to Parliament in 2005.

At the time, Master Builders was reasonably receptive of this response, although it did not technically comply with the legislative requirement. Master Builders notes that there was no dissent in respect of this proposal from any representative on the HBAC.

Terms of Reference

a) The builder licensing system

The current builder licensing system and the administration of the industry in NSW remains a fragmented system despite the recommendations of Campbell. The majority of builders undertake activities in the normal course of their work which may require an additional licence, for example, bonded asbestos removal, use of explosive powered tools. These licenses are issued by the WorkCover Authority. Master Builders is of the view that such licenses could simply be an additional endorsement on an existing licence and better coordinated through a central licensing authority, thus minimising fragmentation through other agencies and limiting duplication. Furthermore, as result of the ICAC inquiry into fraudulent licensing scams involving both builder and WorkCover licenses, both agencies consequently were required to implement new anti-corruption measures, thus duplicating the anti-corruption processes across both agencies.

We respectfully submit, the current NSW licensing legislation requires urgent and significant review. It is our view that the HBS is frustrated by the fact that the description of residential building work under the *Home Building Act 1989*, in conjunction with the relevant provision requiring persons undertaking residential building work to be licensed, effectively captures an extremely wide scope of work and the persons performing such work. Recent attempts to rationalise the number of licence categories, as identified in the *Home Building Regulation 2004* is impossible due to the anomaly between the Act and the Regulation.

The Act also fails to define some critical terms, such as “construction”. Indeed, whilst it is called the *Home Building Act 1989*, it does not provide a definition of a “home”. Another critical feature is that the warranty period for building work differs, being 7 years, (subject to statutory warranties) for licensed builders and in Home Warranty Insurance contracts the period is two years for non-structural defects and six years structural defects.

Master Builders is of the view that the future licensing of the commercial sector is inevitable because all bordering jurisdictions require the licensing of commercial work. This is causing significant issues for NSW builders seeking to undertake commercial work in bordering States and the ACT, because mutual recognition will only account for domestic work due to NSW licensing only applying to residential building work.

It is our view that the commercial sector would be highly resistant to any attempt to have its licensing regime overseen by the Office of Fair Trading.

Master Builders raised these issues in our submissions to the Review of Licensing in the Home Building Industry and we trust that the subsequent report will have considered the issues as raised above. Consequently, we consider this inquiry premature, in that the terms of inquiry relating to the licensing system and related activities would benefit with the findings and recommendations of the Moss Report.

b) The Home Warranty Insurance Scheme

The privatisation of consumer protection insurance in NSW has had a devastating impact on the NSW residential building industry.

The consumer has lost considerable ground with the introduction of the privatised HWI scheme. Other than for insurers, it is difficult to identify who has benefited from the introduction of a privatised insurance scheme in NSW.

Following a period of significant upheaval in the industry, from early 2005, the scheme has settled to a situation whereby the majority of builders wishing to access insurance can now do so. There still remain, however, certain trade sectors and swimming pool builders who continue to have some difficulty in accessing HWI.

This increased accessibility does not mean the industry likes or accepts the scheme. The legacy of the industry upheaval caused by the privatised scheme, the demeaning process of builders “begging” to get HWI, will remain with many in the industry for a long time.

The amendment of the scheme in July 2002, which changed the scheme from a “first resort” scheme, to a “last resort” scheme, whereby a claim can only be made if the builder is insolvent, deceased, or has disappeared, has substantially reduced the level of protection for consumers. However, Master Builders does not support any notion of a return to circumstances of the previous “first resort” scheme, whereby a client could terminate the contract and make a claim on the scheme.

The performance of the scheme is heavily reliant upon the approved insurers responding to their reporting obligations, pursuant to the Conditions of Approval to which the insurers subscribe in providing the home warranty insurance product. Previous government inquiries (i.e. Allen, Grellman inquiries) into Home Warranty Insurance were hampered and frustrated by the lack of data on the operations and performance of the scheme. This was despite obligations on the Director General of Fair Trading to ensure compliance with reporting obligations under the previous Conditions of Approval which were referenced in the *Home Building Act 1989*. With the introduction in September 2004 of new reporting requirements under Market Practice Guidelines, industry now awaits the publication of data, in relation to the performance of the current scheme. This new data should provide an analysis of the level of premiums charged in relation to the number of claims made and identify the number of builders who have accessed the scheme.

Whilst the HBS has responsibility for the administration and oversight of the HWI scheme, as an agency of the OFT, it appears that critical decisions regarding aspects of the current and former “first resort” scheme reside with the Department of Commerce and the Minister for Commerce.

The Allen inquiry recommended the establishment of an insurance ombudsman to review builders’ complaints in relation to the scheme. The proposal would have provided independence on issues such as the Dexta Corporation and the withholding of bank guarantees.

The Home Warranty Scheme Board was established in response to recommendations of the Grellman Inquiry. Members of the Scheme Board are appointed by the Minister and include a representative from the Office of Fair Trading. The Grellman Inquiry also recommended the establishment of an industry and consumer advisory council – the Home Building Advisory Council (HBAC), which would report to the Scheme Board.

Whilst the Scheme Board has been meeting, there has been little, if any, public disclosure of matters before the Scheme Board, nor its decisions or goals.

Master Builders has a number of issues relating to the current operations of the current HWI scheme, but has been waiting for the re-structuring of the HBAC to pursue these matters.

Issues include:

- Builder access to all approved insurers; and
- Identifying why there is a variation in premiums between NSW and Victoria, noting the schemes were supposed to be aligned.

Access to HWI insurance has improved with seven approved insurers now in the market. Whilst it may be suggested that there is a satisfactory level of competition the question remains whether in reality there is true competition. Builders being blocked from registering with all insurers in the market is not consistent with “free movement” in this specific market. This barrier prevents builders from capitalising on any competition in premiums offered by

the seven insurers, effectively denying the client or consumer of the benefits of competitive premiums.

Indeed, a builder is required to cancel their eligibility with the current insurer, should they wish to gain eligibility with a new insurer. Not only does this cause difficulties and increase administration for the builder, it also denies the builder a contingency should an insurer choose to withdraw from the scheme. The previous withdrawal of insurers caused significant hardship to many builders. The proposition of further withdrawals from the current scheme cannot be ignored due to the significant downturn in residential activity in NSW and the competition for market share amongst the approved insurers.

As a statutory product, builders should be able to compare premiums and access insurance in a similar manner to CPT Green slips, whereby an online facility compares Green slip premiums on offer by all of the approved insurers.

The change from a scheme of “first resort” to a scheme of “last resort”, from July 2002, effectively aligned the schemes in NSW and Victoria. Amendments to legislation in NSW, resulting from the Campbell and Grellman inquiries (e.g. introduction of CPD, scrutinizing the influence of associates) strengthened licensing requirements for NSW builders, relative to their colleagues in Victoria, so literally, NSW should be a “safer” market.

However, despite the so-called alignment of the schemes and additional legislative reforms, NSW builders and their clients have continued to pay substantially higher premiums (\$700 -

\$800 on a \$150,000 contract) than Victorian builders. Without access to specific and objective claims details, this discrepancy can not be readily understood.

c) The resolution of complaints

The transcript of the Budget Estimates Committee hearing identifies that the Building Action Reform Group (BARG) has raised issues relating to the time to process complaints and, as understood, the outcomes of representations made to the HBS about building matters.

The transcript identifies that approximately ten matters or aggrieved constituents are presently on BARG's "must attend to" list.

Substantial evidence was provided to the Campbell Inquiry by BARG in which similar concerns were raised.

Master Builders is not in a position to comment on the circumstances or validity of BARG specific grievances. Without being dismissive, this number is small in comparison to the volume of residential work undertaken in NSW.

Whilst the NSW government has introduced Security of Payments (SOP) legislation for the construction industry in NSW, its use is restricted to business to business transactions. One critical party has been excluded from the process, that being the owner occupier.

The lobbying by consumers, in particular BARG, or through earlier Government policy decisions has achieved some significant changes in order to strengthen or support the position of the consumer.

Changes to the consumer builder relationship include:

- The removal of arbitration as a mandatory dispute resolution process for residential contracts.
- Promotion of the CTTT as the primary body to determine building matters.
- The removal of contract created caveat provisions from residential contracts.
- The introduction of a 5 day cooling-off period for contracts
- The requirement for a Consumer Guide to be provided when residential contracts are entered.
- The establishment of the web-based Public Register
- New provisions allowing the Commissioner to examine the relationship and character of “close associates” of licensees and the employment by licensees for disqualified or suspended persons.
- The introduction of mandatory, critical stage inspections.
- The owner or client to nominate the Principal Certifying Authority.

An early dispute resolution service was introduced in July 2003. The process is triggered by the homeowner lodging a complaint with the Office of Fair Trading. This can then lead to the intervention by a Home Building Service inspector who will meet with the homeowner and contractor on-site in an attempt to assist the parties to resolve the dispute.

Early intervention in disputes is critical. Situations where differences of opinion are “muddying the water” would clearly benefit from that being done. The sooner both parties recognise that their concerns are being addressed the more likely it is that the problem can be eliminated.

The Home Building Service in conjunction with the Consumer Tenancy and Trader Tribunal (CTTT) advise that the introduction of the early dispute resolution service has reduced the number of matters referred to the CTTT by 32%. Approximately 80% of matters referred to inspectors are resolved without the need for orders against the builder to be made.

Whilst Master Builders, in principal supports the early intervention process, the current process is structured towards the client or consumer, and in doing so, does not fully capitalise on the potential for the dispute resolution process to resolve disputes.

The current early dispute process cannot be triggered by the builder. Matters of dispute, including payment issues raised by the builder are referred as a building claim to the CTTT. The fact that the builder cannot trigger the early dispute resolution process does not lend itself to overcoming the perception of bias that the system is slanted towards the consumer. Further to this, where there is intervention by a HBS inspector, the inspector can make rectification orders against the builder, but cannot make orders against the consumer. The inspector can order the builder to complete certain work, but cannot order the client to pay for such work. This clearly does not provide or project a balanced approach.

Master Builders had initiated discussions on this issue with the former Director General of Fair Trading through the HBAC, but to no avail. It is instances such as this that continues to impose a perception of bias against the industry.

A further issue Master Builders has regarding the early intervention process is that reports compiled by the HBS inspector are not required to be considered by the CTTT member, should the early dispute process not succeed, and the matter is lodged with the Tribunal. The Tribunal member has the discretion to consider the report or disregard it.

This ability to disregard the HBS inspector's report, whom it has to be assumed has suitable technical skills and experience to appraise the matters at issue, an accepted level of independence and has actually visited the site, is seen as a significant flaw in the process and a waste of resources.

Master Builders has assumed that in all cases, where the matter proceeded to the Tribunal, then a report by the inspector would also be referred. Master Builders has learnt that this is not always the case.

It would appear from the transcripts of the Budget Estimate Hearing, that BARG appears to have considerable grievance with the current dispute process. Such grievances have not been raised by BARG's representative on the HBAC.

The resolution of disputes, the early dispute process and indeed a presentation by the CTTT have all come before the HBAC as issues for review, comment and advice to the Scheme Board. If BARG has issues of such importance as to require this Committee to hold this inquiry, then the question must be put why haven't these issues been raised with the HBAC?

The raising of such issues at a forum such as the HBAC, would allow balanced discussion amongst the industry, consumer and insurance representatives on the Council, with a subsequent record of discussions available directly to the Minister.

d) The exercise of disciplinary powers

The level of prosecutions over the past twelve to eighteen months and the publicity attached to such matters, verifies that the HBS is out there doing what it is required to do.

There has been a significant increase in field compliance operations since the establishment of the HBS. Whilst Master Builders has been provided with preliminary advice regarding some operations, we only become aware of other operation following calls or inquiries from members advising that inspectors are active in the field.

These operations and other investigations have resulted in substantial penalties, including custodial sentences for repeat offenders. Master Builders has posted the press releases of these prosecutions on our website as a warning, but more importantly to indicate to members that the regulator has been active in responding to the industry's request to be active against unlicensed contractors.

An area of improvement identified by Master Builders is for greater compliance action to be taken against licensed trade contractors where these contractors have clearly been identified as being the cause of a defect or have significantly contributed to defective or incomplete work. We are most concerned that findings can be made against the principal contractor, without the relevant party who physically did the work being at the site investigation meeting and as appropriate being held accountable.

A view that the principle contractor is entirely responsible for the work of their contractors is a simplistic and an incomplete approach. The NSW construction industry is structured on a sub-contract system, whereby the trade contractors perform the majority of actual “hands-on” building work. This provides many efficiencies to the consumer in many forms.

The head contractor is liable for the work but clearly does not in many cases carry it out without engaging trade contractors. They are licensed to do their work, so if the work is defective and action is taken concerning the work, both the head contractor and the trade contractor should be held accountable – on a proportionate basis.

An attitude that the principal contractor should be more discerning in the choice of contractors and ensure adequate supervision, whilst easy to apply in a textbook world, does not readily or comfortably sit with the realities of supply and demand, skills shortages and the cyclical nature of building work.

Indeed, the majority of residential builders tend to have a pool of good subcontractors and retain them year after year. Establishing a pool of good subcontractors is the principal “insurance” builders have. They cannot purchase insurance to cover against claims and losses caused by subcontractors. Builders remain personally liable for the work or projects, a fact that is not realised or appreciated by those immediately outside of the industry.

In periods of high activity and with recognition of serious skills shortages in the industry, builders can have great difficulty about the choice of subcontractor, due to the compounding pressures of obligations under the Act and from the client, especially as to quality and time.

The builder is also confronted with other legislation in relation to aspects such as workers compensation and taxation. Overseeing and directing a so-called “contractor” may deem that person a “worker”. A builder who engages the same contractor, year after year, job by job, due to the fact they provide quality work could fall foul of various taxation provisions.

From an efficiency perspective, the definition of who is and who is not a worker/employee as opposed to an independent contractor needs to be made clear, functional and able to be readily applied by those who actually work in the industry.

e) The enforcement of relevant legislative and regulatory provisions

Master Builders repeats the comments at item (d) above.

f) The establishment of a Home Building Advice and Advocacy Centre

The recommendation for the Consumer Advocacy Centre is founded upon the premise that consumers are disadvantaged and should be on an equal footing with builders in access to advice and advocacy services.

There appears a perception that builders have ready access to information, advice and advocacy services. The reality is that such services to builders and trade contractors are generally provided by industry organisations, of which only some 20% of the current licence holders are financial members.

The majority of the industry does not have access to critical advice and information and in relevant circumstances pay commercial fees for advice and advocacy services. Licensees generally receive insufficient information regarding industry changes, including advice on regulatory reforms, and no doubt other issues affecting their work.

The proposed Home Building Advice and Advocacy Centre was a recommendation (recommendation 3) of the Campbell Inquiry, which recommended that it be independent of government, funded from the proposed Home Building Compliance Commission, however, the Centre could charge on a fee-for-service basis, for specific legal or advocacy work.

The recommendation of the Campbell Inquiry is interpreted as two specific functions, firstly, the establishment of an independent, Home Building Compliance Commission and secondly, the establishment of the Home Building Advice and Advocacy Centre, independent of

government and funded by the Commission. The industry did not get its independent Commission, nor did the consumers Advocacy Centre come to fruition. However, despite a surplus in revenue from licensing fees going into consolidated revenue, as identified by Campbell and disclosed in subsequent Budget Estimate Committee transcripts, licensees in NSW had imposed a 21.5% levy on licenses to establish the Home Building Service.

It is suggested the builders would not be receptive to a proposal to now establish the Consumer Advice and Advocacy Centre, funded from licensing fees or levies paid by builders, whilst at the same time, continuing to be administered by the government's consumer protection agency.

Many licensees see themselves as the ones being disadvantaged by the tactics regularly used by some consumers and consumer activists. Instances of consumers taking occupation and withholding payments continue to be an issue for industry. The continual expose of building projects, sensationalised through television programs cast an ongoing stigma over the industry and do not provide a balanced view of the industry, nor the thousands of successful building projects and satisfied customers.

No public body provides a sufficient nor a balanced presentation of the dilemma faced by builders who have suffered from recalcitrant clients.

The establishment of an Independent Building Commission would immediately remove the conflict between the central charter of Fair Trading, being that of consumer protection and the conflicting role assigned to it of administering the residential building sector.

This separation would leave the Office of Fair Trading to focus upon providing consumer advice and protection, without having to defend perceptions of bias in administering licensing and the building industry.

Consequently, there would be no need to establish an Independent Consumer Advocacy Service, because of the single focus by the Office of Fair Trading on consumer protection.

An Independent Building Commission could take the activities of the HBS out of the political sphere and allow it to improve on what is being done without the distractions and conflicts caused by being a sub sector of a Government department.

South Australia is the only other State or Territory where the Department of “Consumer Affairs” regulates builders and administer licensees.