

**Submission
No 167**

**INQUIRY INTO REGULATION OF BUILDING
STANDARDS, BUILDING QUALITY AND BUILDING
DISPUTES**

Organisation: Society of Construction Law Australia

Date Received: 28 August 2019



Submission to the inquiry into the
regulation of building standards, building
quality and building disputes

Table of Contents

Executive Summary	3
Top Recommendations.....	3
Background: About The Society of Construction Law (Australia)	4
1 The role of private certification in protecting building standards	5
ISSUES	5
RECOMMENDATIONS	7
2 The adequacy of consumer protections for owners and purchasers of new apartments / dwellings, and limitations on building insurance and compensation schemes.....	9
ISSUES	9
RECOMMENDATIONS	11
3 The role of strata committees in responding to building defects discovered in common property	12
ISSUES	12
RECOMMENDATIONS	14
4 Case studies related to flammable cladding on NSW buildings and the defects discovered in Mascot Towers and the Opal Towers.....	16
ISSUES	16
RECOMMENDATIONS	18
References	20
Glossary	21
Summary table of key issues and recommendations	22

Executive Summary

The Society of Construction Law (Australia) (the **Society**) welcomes the NSW Legislative Council's Public Accountability Committee's Inquiry into the regulation of building standards, building quality and building disputes (the **Inquiry**). The Society is a national organisation of members, at all stages of their professional career, who share an interest in construction law. The Society promotes the education, study and research in the field of construction law and related subjects in Australia and overseas. The Society provides a forum for industry participants and thought leaders to connect and together initiate positive change in the construction industry for the benefit of the construction industry and public as a whole by influencing changes to legislation, policy and practice. It is for this reason that the Society make these submissions to the Inquiry.

The building industry is facing a crisis arising from the proliferation of serious defects in multi-dwelling residential buildings which is impacting on consumers. Structural defects identified in Sydney's Mascot and Opal towers as well as high-profile cladding concerns, have exposed the complications around liability and lack of consumer protection in the multi-owned residential sector. A recent Deakin University report by Nicole Johnston and Sacha Reid of Griffith University which analysed 212 building audit reports identified 3,227 building defects with an average 14 defects identified per building.¹ In New South Wales, the academics found that 97 per cent of buildings had at least one defect. The most common defects identified in the report were the type that often require invasive and costly remedial work.

This submission begins with our top recommendations to improve the outcomes for consumers of residential buildings through the certification and defect cost recovery processes. A response is then provided to the inquiry's Terms of Reference. In response to each of the Terms of Reference 1(a), 1(b), 1(c) and 1(d), we have provided some background information, set out issues faced by the construction industry as we see them, and our recommendations for change.

Top Recommendations

Issue:

- Lack of protection for owners from the cost of rectifying defects
- A culture of non-compliance in the building and construction industry

Recommendations:

- Extend the statutory warranty period to a minimum of 10 years for all defective building work
- Introduce a statutory warranty imposing a duty of care on builders to both new and subsequent apartment owners. In circumstances where the builder no longer exists, this statutory warranty imposes a duty of care on the developer
- Introduce reform to the HBC Scheme so that it applies to all residential buildings
- Establish a government defect fund such as by using a percentage of funds received by the government from stamp duty payable on high rise residential buildings
- Establish a government agency to manage the defect fund and work with owners corporations through the defect rectification process
- Reform the regulatory framework to streamline the powers and responsibilities of each of the regulatory bodies
- Change the requirements for all building professionals to have comprehensive professional indemnity insurance

¹ Deakin report analyses growing number of apartment building defects, Media release, 19 June 2019, <https://www.deakin.edu.au/about-deakin/media-releases/articles/deakin-report-analyses-growing-number-of-apartment-building-defects>.

Background: About The Society of Construction Law (Australia)

The Society is a national organisation of members, at all stages of their professional career, who share an interest in construction law. The Society was launched in May & June of 2009.

The Society encourages the active involvement of all of its members and discourse across the broad spectrum of issues relating to construction law, including matters of policy and legislation, "front end" issues, dispute avoidance, and all forms of dispute resolution.

The Society's vision is to:

- promote the education, study and research in the field of construction law and related subjects in Australia and overseas; and
- provide a forum for industry participants and thought leaders to connect and together initiate positive change in the construction industry for the benefit of the construction industry and public as a whole by influencing changes to legislation, policy and practice.

1 The role of private certification in protecting building standards

The role of private certification in protecting building standards, including:

- (i) conflicts of interest
- (ii) effectiveness of inspections
- (iii) accountability of private certifiers
- (iv) alternatives to private certifiers.

Unscrupulous and unregulated strata unit developers have caused significant economic and social damage. Developers have been known to conveniently disappear after the issue of an occupation certificate and in circumstances where developers of multi-storey apartments are not obliged to obtain home warranty insurance, any proposal to address the residential unit crisis should address these issues as well as put in place measures to prevent unscrupulous developers resurfacing under the guise of other corporate vehicles.

The broader construction industry, even under the current controls, is capable of quality and compliant construction. Multi-storey commercial buildings, shopping centres, hospitals and schools are generally not leaking, at risk of fire, or uninhabitable. Those who wish to, or by law are obliged to build correctly, are able to do so. Some reflection on this fact would be of benefit to the direction of reform. Clearly compliance can be achieved, leaving the question as to how it can be made to apply to residential unit developments.

The industry sector within which the problems primarily exist is residential, particularly high rise strata developments. The reforms have to focus on addressing the problems in that sector.

ISSUES

The following issues are relevant to certification.

Compliance with plans

All architectural and engineering plans including hydraulics, structural, fire engineering plans should be signed off and declared by a statutory declaration.

The concept of statutory declarations as to the compliance of plans, does however involve some serious misconceptions in that a declaration will probably only be effective for “deemed to satisfy solutions” (DTS) and, further that the Performance Requirements in the NCC are most often expressed in inspirational rather the specific terms.

For example Clause P2.1.1 in Vol 2 of the NCC, as to stability requires that the structure must “perform adequately” and Clause P2.2.2 “Waterproofing” requires that water not be allowed to penetrate. How effective in fact could a statutory declaration as to compliance with such standards be?

Plans could be plans be statutorily declared at the CC/CDC stages. At that stage the plans should be fully coordinated with each other and fully resolved. The limitations of the concept of statutory declarations as to the compliance of plans means that they are not particularly relevant to the ultimate issue of whether the work as-built complies. The NCC applies to the way buildings are built, not to the way they are designed.

Changes to plans and variations

When plans in respect of structural, hydraulics or fire engineering are changed they should be required to be submitted to the regulator. Cosmetic architectural changes need not be submitted to the regulator. Further if a change involves an alternative to a DTS solution the submission process will be difficult to implement.

Another option that could be workable if there are variations to plan is the conventional participation of building professionals during the construction stage as occurs in general commercial construction.

A statutory declaration could accompany variations to structural, hydraulics or fire engineering plans. In respect of variations to the structural design, the designer could certify that he/she has carried out all requisite design calculations to satisfy themselves that the design is fit for purpose, and that it complies with the DTS or alternative solution.

The Society can think of no credible obstacles that would prevent a person from submitting a statutory declaration for variations, except for the unjustified belief that a tangible benefit will follow. There would also be considerable complexity in the administration of the assessment of the compliance of the design of variations which are the subject of statutory declarations.

The modifications process in the hands of the developer / builders has been too simple to date and the goal should be to ensure that buildings are designed and constructed with due care and skill and the result is fit for purpose. Without a rigorous construction compliance, enforcement and approval process and the supply of requisite supporting documentation, this cannot be achieved.

Provision of plans and documents to the Building Commission

All documents need to be prepared in electronic amendable form. There should also be a requirement that the documents be updated upon completion (as-built). Delivery may be effected either via USB or electronic transfer.

The Society is of the view that it is important for building designers to demonstrate that the building and its elements have been designed with due care and skill. In the case of the structural elements of the building, the engineer should provide an outline of the methodology adopted by the designer to satisfy itself that the design is fit for purpose and complies with the relevant Standards identified in the DTS performance requirements.

Documentation of performance solutions

In most instances the process of documenting performance solutions and their compliance with the BCA will be complex and expensive. The verification of performance solutions which involve engineering analysis will be very complex, and for fire engineering design they will be difficult for any regulator to assess unless they have access to assessors with professional qualifications equivalent to the designers.

A performance solution report would be valuable as part of this process, however the capacity of a regulator to assess the adequacy of the solution and to verify compliance is very doubtful.

The concept of statutory declarations of compliance of plans as a means of verifying compliance with performance requirements seems to be at odds with how the performance requirements are expressed.

Declarations of compliance

The Society is of the view that to have a builder certify that the building that it has constructed complies with the plans and specifications would not be an effective way of ensuring compliance with the plans and specifications.

The Society considers that each of the building designers should be retained to inspect the building while it is being constructed to the extent necessary for them to be able to satisfy themselves that the building elements have been constructed in accordance with the approved plans and specifications.

The Society considers that a certifier who only makes critical stage inspections and primarily relies upon the documentary evidence produced by the various contractors and consultants is not equipped to make this assessment.

While the builders may have the initial role of “declaring final building work”, the Society is however strongly of the view that this declaration must be corroborated by the building designers. Note that in non-residential construction under the traditional methodology, which relies upon the continued involvement of building professionals during the course of construction, compliance is not difficult to achieve.

Registration of building professionals

The Society considers that, apart from the obvious necessity to have a national register of engineers, the current process of professional registration is satisfactory. The fact that there is no requirement that the builder of a multi-storey strata apartment building be licensed and insured needs to be addressed.

Architects, all engineers including hydraulics, fire safety, hydraulics should be in scope for registration. Consideration should also be given to setting rigorous requirements for the qualification for designing, and the performance of, waterproofing installations.

Professional indemnity insurance

Requirement for Professional indemnity insurance that covers the designer against claims made and notified in respect of a failure to exercise reasonable care and skill with such cover to extend to claims brought against the building designer under the Australian Consumer Law.

The cover should be commensurate with the value of the projects that the 'building designer' works on. As professional indemnity policies are claims made and notified, the 'building designer' should ensure that the value of their insurance is commensurate with the highest value of the projects that it has worked on in the preceding 10 years (adjusted to today's values).

Mandatory skills for 'building designers'

Mandatory skills for building designers' are the proven ability to design and carry out all requisite calculations, and to assess the compliance of all elements of the design with performance requirements.

The conventional historic approach to the registration of building professionals should be maintained.

Developer's /builder's duty of care

All building professionals owe a duty of care to those who may be affected by the performance by them of their profession. For all residential construction the principal duty of care should be owed by the original developer / builder to the purchaser and successors in title of the property.

The duty of care should be supported by compulsory major defects project insurance the premium for which will depend on the degree to which the developer / builder is prepared to satisfy the State regulatory bodies as to compliance.

The duty of care should be enforced by a statutory obligation upon the original developer /builder to ensure compliance. The contractual chain can deal with the extent to which the duty is satisfied.

Residential purchasers and future owners are not in a position to protect themselves from the risk of non-compliant construction. Initial owners of commercial property and government are able to ensure compliance. The same should apply to the initial "owners" of residential property.

RECOMMENDATIONS

Below is a list of recommendations provided by the Society.

1. Introduce a statutory requirement that all architectural and engineering plans including hydraulics, structural, fire engineering plans as well as plans for variations must be signed off and declared by a statutory declaration.
2. Introduce a statutory requirement that plans in respect of structural, hydraulics or fire engineering must be submitted to the regulator.
3. Introduce a statutory requirement that engineers must provide an outline of the methodology adopted by the designer to satisfy itself that the design for the structural elements of the building are fit for purpose and complies with the relevant Standards identified in the DTS performance requirements.
4. Introduce a requirement that the builder's declaration of the final building work must be corroborated by the building designers.
5. Introduce a national register of engineers.
6. Amend legislation to make clear that the principal duty of care is owed by the original developer / builder to the purchaser and successors in title of the property.

7. Introduce compulsory major defects project insurance the premium for which will depend on the degree to which the developer / builder is prepared to satisfy the State regulatory bodies as to compliance. As well as introducing a statutory obligation on the original developer /builder to ensure compliance.

2 The adequacy of consumer protections for owners and purchasers of new apartments / dwellings, and limitations on building insurance and compensation schemes

The adequacy of consumer protections for owners and purchasers of new apartments/dwellings, and limitations on building insurance and compensation schemes, including:

- (i) the extent of insurance coverage and limitations of existing statutory protections
- (ii) the effectiveness and integrity of insurance provisions under the Home Building Act 1989
- (iii) liability for defects in apartment buildings.

The *Home Building Act 1989* (NSW) (the **Act**) implies a number of warranties into contracts for all residential building work carried out in NSW. These warranties apply irrespective of whether they are included in a written contract. For works carried out under contracts entered into before 1 February 2012, a seven year warranty period applies to all defects. Whereas, for works carried out under contracts entered into after 1 February 2012, a six year warranty period applies for major defects and two years for any other defects. The time limits are calculated from completion of the works.²

Notably, the statutory warranty period in NSW is shorter than that in Victoria. In Victoria, the statutory warranty period within which to bring a claim for loss or damage arising out of defective building work is 10 years from the date of issue of the occupancy permit or, if no permit is issued, the date of issue of the certificate of final inspection of the relevant building work.³

In circumstances where the builder cannot be found, either because of bankruptcy/insolvency, disappearance or death, strata owners may be able to seek compensation and make a claim under the Home Building Compensation Fund Scheme (**HBC Scheme**). Relevantly, however, buildings with a rise of more than three rises are not covered by this scheme⁴

ISSUES

The following issues are relevant to the adequacy of consumer protections for owners and purchasers of new apartments and dwellings.

Statutory warranties and latent defects

Section 18B of the Act implies a number of statutory warranties by a builder into all residential building work contracts. For example, a warranty that the work will be done with due care and skill and in accordance with the plans and specifications set out in the contract.

Section 18E of the Act sets out provisions relevant to breach of a statutory warranty. Amongst other things, proceedings for breach of a statutory warranty must be commenced before the end of the warranty period for

² *Home Building Act 1989* (NSW) s 18E.

³ Section 134 of the *Building Act 1993* (Vic), provides that “*despite any thing to the contrary in the Limitation of Actions Act 1958 or in any other Act or law, a building action cannot be brought more than 10 years after the date of issue of the occupancy permit in respect of the building work...*”.

⁴ *Home Building Regulation 2014* (NSW), regs 56(1) and 56(7).

the breach. As discussed above, the warranty period is six years for a breach that results in a “major defect” and two years in any other case (unless the breach becomes apparent in the last six months of the warranty period – in that case, proceedings may be commenced within a further six months after the end of the warranty period). The warranty period starts on completion of the work to which it relates.

In the event of a latent “major defect”, it may well be the case that the warranty period has expired before the home-owner becomes aware of the defect. In that case, the home-owner may have no recourse against the builder for breach of the warranty.

This is particularly evident in the Sydney Mascot Towers case, where residents have been forced to evacuate the 132-unit development built 10 years ago due to defects. It is therefore clear that the statutory warranty periods as they currently stand do not adequately protect owners and purchasers of strata apartments.

The following issues are relevant to the adequacy of building insurance and compensation schemes.

The Home Building Compensation Fund Scheme

The HBC Scheme compensates home-owners if their builder is unable to complete building work or fix defects because of insolvency, death, disappearance or licence suspension. This means it operates on a “last resort” basis. If a builder simply refuses to repair defective work, the HBC Scheme will not assist. In that case, the home-owner’s only option is to sue the builder and incur the costs of doing so (assuming that they are within the warranty period identified above). The HBC Scheme also only provides a maximum cover per dwelling up to \$340,000, which may be inadequate in some cases.

Strata Building Bond and Inspections Scheme

The HBC Scheme provides cover in respect of residential apartment buildings of up to three rises only. For building work carried out on new residential apartment buildings of four or more rises, the Strata Building Bond and Inspections Scheme (**SBBI Scheme**) is now operational. From 1 January 2018, developers are required to lodge a building bond with NSW Fair Trading equal to 2% of the contract price. This bond can be used to pay for the costs of rectifying defective building work identified by a building inspector. The bond may be released to the developer after two years from the date of completion if no defects are identified.

Whilst the SBBI Scheme is still relatively new, a number of potential issues arise with respect to its application. Amongst other things, it is not clear that the two year period will encompass all defects which might emerge – for example, latent major structural defects.

It is also unclear whether the 2% bond is sufficient to combat the effects of structural defects in high-rise buildings. It is becoming increasingly clear that the costs of rectifying major defects, especially in larger strata buildings can quickly overtake the sums available in the bond, particularly if the issues occur throughout the building.

Compensation

No scheme provides “compensation” to home-owners in circumstances in which they or their tenant cannot reside in their new apartment/dwelling due to defects. This has been particularly pertinent in relation to Mascot Towers, Opal Tower and Zetland’s Garland Lofts, each of which have suffered serious defects forcing residents to vacate their homes. The inadequacy of building insurance and compensation schemes in these circumstances is clearly evident.

The following issues are relevant to liability for defects in apartment buildings.

Inability to locate the builder

The ultimate responsibility for defect rectification of common property and any issues with the management of the process lies with the owners corporation.⁵ If the defects arose during the statutory warranty period, then the usual remedy for strata owners to recover the cost of defect rectification is to sue the person responsible for the defect.

Under NSW tort law, negligence requires a person to prove there was a duty of care between themselves and the negligent party. However, it is not always clear with buildings who owes a duty of care to whom and it is even more difficult to determine who owes the duty of care to the final purchaser.

If the party responsible for the defect can be identified, it is often the case that they can no longer be found either because of bankruptcy/insolvency, disappearance, or death. In these circumstances, a claim through the HBC Scheme may be made, provided the builder/developer is not exempt from having to obtain insurance under this scheme. Therefore, as discussed above, strata owners of buildings that are more than three rises are in a very vulnerable position when it comes to recovering costs for defect rectification, as the builder is not required to obtain insurance under the HBC Scheme.

RECOMMENDATIONS

Below is a list of recommendations provided by the Society.

1. Introduce a statutory warranty for the benefit of both new and subsequent apartment owners which imposes a duty of care on the builder. In circumstances where the builder no longer exists, this statutory warranty would shift to the developer. The introduction of a statutory duty of care would make it clearer who could be sued.
2. Introduce reform to the HBC Scheme so that it applies to all residential buildings, including those that are more than three rises high and which are currently exempt from insurance pursuant to section 56(1) of the Act.
3. Extend the statutory warranty period in section 18E of the Act to, at a minimum, a period of 10 years for all defective building work (regardless of whether it is a major defect). This will also bring NSW legislation in line with Victorian legislation.

⁵ *Strata Schemes Management Act 2015* (NSW), s 9(3)(c) and s 106(1)

3 The role of strata committees in responding to building defects discovered in common property

The role of strata committees in responding to building defects discovered in common property, including the protections offered for all strata owners in disputes that impact on only a minority of strata owners.

A 2018 report commissioned by the Building Ministers Forum noted that the number of high-rise apartment (4 plus storeys) had tripled in less than a decade. In circumstances where the number of strata residents in NSW is increasing, the impact of defective buildings like the Mascot Towers, Opal Tower and Zetland's Garland Lofts will result in increased pressure on strata committees by other residents, on politicians, on government services and departments, as well as the court system.

Strata committees are often the first to take on the management of defects in residential buildings. The primary role of the strata committee is to act on behalf of the owners corporation in accordance with the Act and the Regulations. Strata committee members are elected representatives of the owners corporation who make many of the day-to-day decisions about the strata scheme's management. Strata committee members must act with due care and diligence and must disclose any conflict of interest at a meeting.⁶ The role of the strata committee typically includes managing the maintenance and repair of common property. However, the ultimate responsibility for defect rectification and any issues with the management of the process lies with the owners corporation.⁷ The Act requires an owners corporation to have mandatory insurance including for damage to the property for which the owners corporation could become liable.⁸

Protection offered to all strata owners in the face of defect rectification costs are those found in statute, primarily the requirement that builders rectify defects within the limitation period, and in contract, primarily the defects rectification period requirements which run for a specified number of months after the construction is complete.

The cost of defect rectification of common property is likely to be borne by all the owners of a building regardless of whether or not they are directly affected. This is the case unless:

- a) the defects arose during the defects liability period and were paid for by the builder;
- b) the HBC Scheme or SBBI Scheme apply, or
- c) the defects arose after the liability period and the owners' are able to recover some or all of their costs through a form of dispute resolution.

Even if the owners are successful in dispute resolution, this process exposes them to additional costs, some of which will not be recoverable, and if the owners lose they may be required to pay the other party's legal costs.

ISSUES

The following issues are relevant to the role of strata committees in responding to building defects discovered in common property.

Strata committees' skill set

Strata committee members may only have rudimentary knowledge of the building industry and limited experience managing the defect rectification process. The attribution of liability for defects in common

⁶ *Strata Schemes Management Act 2015 (NSW)*, s 37 and s 260

⁷ *Strata Schemes Management Act 2015 (NSW)*, s 9(3)(c) and s 106(1)

⁸ *Strata Schemes Management Act 2015 (NSW)*, s 164(1)(b)

property is often complicated as the design and construction of modern buildings involves a large number of people, each with different functions and responsibilities. The handling of high value or complex defects can impact on the outcomes for owners. For example, if the limitation period, which can be difficult to identify as it is determined by the occurrence of the defect, is allowed to expire the owners may lose avenues for cost recovery.

Impact on strata committees

Dealing with substantial defect rectification without industry knowledge or experience is stressful. This stress is heightened when the defect affects your property and is likely to impact you financially. Strata committee members are also likely to be living with other residents in the building who may openly comment on the committee's handling of the defect which may impact on the members' lives.

The following issues are relevant to protections offered for all strata owners in disputes that impact on only a minority of strata owners.

The availability of protections for strata owners

Defects involving the Charlestown's Landmark building has revealed the inequity and apparently long-standing nature of the problems involved with NSW apartment building regulations and law. Residents of the Landmark building have been levied thousands of dollars each to repair significant defects affecting common property. It is clear that the current system is failing to protect strata owners. This is particularly evident in circumstances where strata lot owners are required to pay special levies, vacate the premises or sell their home due to defects that could and should have been avoided. Further, the stress of being forced to bear the enormous cost of repairs for long-standing defective works can lead to terrible internal conflicts and divisions among building residents, particularly in circumstances where the defects do not affect all strata owners. It is clear that innocent strata owners should not have to put up with, and bear the cost of, builders/developers' poor workmanship.

There is also a temptation for strata owners to believe that it is in their own interests to keep issues relating to defects quiet and for settlements to be negotiated quickly before property values plummet. The conspiracy of silence is heightened further by the fear that whistle-blowers will be blamed for any reduction in property values.

Exemption from insurance under the Home Building Compensation Fund Scheme

Builders and developers of multi-storey buildings (defined as two or more separate dwellings which exceed three storeys in height) are exempt from having to obtain insurance under the HBC Scheme.⁹ There is no justification for this loss of protection and it is not in the public interest. It is evident that this exemption is outdated, as the number of residential high-rise developments has grown exponentially. Further, building defects, particularly in large high-rise developments, are a serious and growing problem. Home warranty insurance must be a mandatory requirement for all residential buildings regardless of height. This is vital to ensuring adequate consumer protection for strata owners of high-rise developments.

Strata Building Bond and Inspections Scheme

Recent reforms, which commenced on 1 January 2018, include a requirement on developers of a strata scheme to give the Secretary of the Department of Finance, Services and Innovation a building bond (being, 2%

⁹ *Home Building Regulation 2014* (NSW), regs 56(1) and 56(7).

of the contract price of the building work) before an occupation certificate is issued under the *Environmental Planning and Assessment Act 1979* (NSW).¹⁰ The building bond may be used by the owners corporation for, or in connection with, rectifying defective building work identified in the final building report or for costs related to the rectification and any excess amount must be repaid to the developer.¹¹ A claim on the building bond must be made within the later of two years after the relevant building work or 60 days after the final building report is issued.¹²

While this is a significant reform, it is uncertain whether the 2% defects bond is sufficient to combat the effects of structural defects in high-rise buildings. It is becoming increasingly clear that the costs of rectifying major defects, especially in larger strata buildings can quickly overtake the sums available in the bond, particularly if the issues are replicated throughout the building. Further, the time frame to identify latent serious building defects is likely to be insufficient. This means owners corporations can be exposed to further out of pocket expenses associated with rectification, and/or litigation.

Costs are likely to be borne by strata owners in many circumstances

In many cases however, it can take many years for defects to manifest themselves in high-rise buildings. This is particularly evident in the Sydney Mascot Towers case, where residents have been forced to evacuate the 132-unit development built 10 years ago due to defects.

The NSW State Government is currently offering an open-ended, low interest loan to the Mascot Towers owners corporation to allow it to pay for the evacuated residents' emergency accommodation. The finances for this loan will come from the interest accrued from rental bonds. The NSW State Government considers this to be a one-off loan. However, it is evident that it should not be a one-off assistance, given the considerable increase of new residential buildings in Australia plagued with defects.

As discussed above in section 2, in circumstances where the statutory warranty period has expired, and the HBC Scheme is not applicable, strata owners have little to no recourse against builders for the cost of defect rectification. In these circumstances, the costs are likely to be borne by strata owners. This is also likely to be the case in circumstances where the builder either cannot be located or no longer exists because it is bankrupt/insolvent.

RECOMMENDATIONS

Below is a list of recommendations provided by the Society.

1. The statutory warranty period be extended to a minimum of 10 years for all building defects.¹³
2. Introduce a statutory warranty for the benefit of both new and subsequent apartment owners which imposes a duty of care on the builder. In circumstances where the builder no longer exists, this statutory warranty would shift to the developer.

¹⁰ *Strata Schemes Management Act 2015* (NSW), s 207.

¹¹ *Strata Schemes Management Act 2015* (NSW), s 210.

¹² *Strata Schemes Management Act 2015* (NSW), s 209(3).

¹³ Victorian has for a 10 year warranty period. Section 134 of the *Building Act 1993* (Vic), provides that "despite any thing to the contrary in the *Limitation of Actions Act 1958* or in any other Act or law, a building action cannot be brought more than 10 years after the date of issue of the occupancy permit in respect of the building work...".

3. The Act should also be amended to specify that the management of substantial defect rectification over an amount set in the Regulations is not delegable to strata committees. Such defects should be managed by the body corporate with or without the assistance of a strata agent.
4. Amendments be made to the Act to place an obligation on body corporates to ensure that strata committee members have an understanding of the building's by-laws and the governing state legislation, the building's past committee and general meeting minutes, issues and financial position.
5. A NSW State Government defect fund should be established. This could be done by using a percentage of funds received by the government from stamp duty payable on high rise residential buildings. This fund would be accessible to strata owners for the rectification of defects in circumstances where:
 - a) the statutory warranty period had expired; and/or
 - b) the builder/developer no longer exists, is deceased or is unable to pay the costs due to bankruptcy or insolvency.
6. If a NSW State Government defect fund is not implemented, then an insurance based defect fund should be implemented to provide the funds for defect rectification. This fund could be created by owners corporations paying a levy as part of their compulsory building insurance.
7. A new NSW State Government agency should be established which manages the defect fund and works with owners corporations through the defect rectification process.
8. Reform the HBC Scheme so that it applies to all residential buildings, including those that are more than three storeys high.
9. Support a coordinated response from all State Governments in Australia to produce uniform legislation, including:
 - a) Uniform statutory warranties in each State and Territory;
 - b) A uniform statutory insurance scheme that covers both homes and apartment dwellings, and which operates on a first-resort basis;
 - c) Consistent national standards for building industry licencing and compliance of builders (including qualification, experience and financial holding requirements commensurate with the size of development projects they seek to undertake), including for other building practitioners such as designers, engineers and certifiers.

4 Case studies related to flammable cladding on NSW buildings and the defects discovered in Mascot Towers and the Opal Towers

The ‘flammable cladding crisis’ is a nation-wide issue (and indeed, it extends beyond Australia). Similarly, the Mascot Towers and Opal Towers incidents could signal a potentially much wider issue.

NSW has taken a number of steps to assess the extent of the cladding crisis, and to prevent combustible products being used in future. For example:

October 2016	Commencement of the <i>Environmental Planning and Assessment Amendment (Fire Safety and Building Certification) Regulation 2017</i> to strengthen fire safety certification requirements for new and existing buildings in NSW.
June 2017	Establishment of the Fire Safety and External Wall Cladding Taskforce to audit over 185,000 buildings and inspect 2,300 buildings across NSW and address related safety issues.
December 2017	The <i>Building Products (Safety) Act 2017</i> came into effect to prevent the use of unsafe building products.
August 2018	The NSW Fair Trading Commissioner issued a building product use ban to prohibit the use of aluminium composite panels (ACPs) with a core comprised of greater than 30% polyethylene core on certain types of buildings.

However, to date, the NSW Government has not:

- outlined any plans for rectifying existing buildings with combustible cladding;
- taken any steps to change the culture of non-compliance within the building industry which has led to the combustible cladding crisis and the latent defects in the Mascot Towers and Opal Towers;
- addressed the ‘tug of war’ with professional indemnity (**PI**) insurers which could result in many building professionals becoming unregistered and leaving the market as a result of skyrocketing insurance premiums.

ISSUES

The flammable cladding crisis and the increased discovery of latent defects in large residential towers in recent times highlight very similar systemic issues. In particular, they draw attention to systemic failures in:¹⁴

- **the building and construction process** – which, partially as a result of a culture of non-compliance in the building and construction industry, has resulted in a number of building products being used that do not comply with the standards set out in the National Construction Code (**NCC**); and
- **regulation** itself – including as a result of insufficient regulatory powers and a fragmented regulatory system.

Issues across the building and construction process

In past years, there has been an increasing awareness of a culture of non-compliance in the building industry across the country. This culture of non-compliance has been a significant contributing factor to the widespread use of non-compliant combustible cladding, and latent defects such as those in the Opal Towers and Mascot Towers.

¹⁴https://www.planning.vic.gov.au/_data/assets/pdf_file/0019/426034/DELWP0124_Victorian_Cladding_Taskforce_Final_Report_July_2019_v9.pdf, pg. 42.

The Shergold Weir Report identified that there is a high incidence of building products in the market that do not comply with the standards set out in the NCC. In part, this has arisen from a practice of product substitution. The practice of product substitution (where deliberately undertaken) reflects the culture of non-compliance, and has resulted in inferior and sometimes dangerous products being used.

As discussed below, the Society considers that reforms to the NSW regulatory framework may assist to change the culture of non-compliance through more effective enforcement powers. However, building industry bodies and building professionals have a significant role to play in changing the culture within the industry.

Issues in regulation

Limited regulatory powers

As discussed in section 3 above, at present, the immediate responsibility for the costs of rectifying non-compliant combustible cladding or latent defects typically falls to building owners. Facing the potentially significant costs of rectifying defects that were unknown at the time of purchase has, and will continue to, place many owners in a precarious and potentially unsustainable position.

The primary means currently available to owners to shift the financial burden of rectification works is to commence recovery proceedings against the builder and other responsible consultants and subcontractors. However, this option is not open to all owners (for example, owners who are time-barred from bringing claims, or who may not be in the financial position to commence proceedings). Further, there is no guarantee of success or satisfactory recovery. The Society considers that other means should be available to owners to hold building professionals to account.

Whilst Fair Trading NSW is authorised by the *Home Building Act 1989* to issue rectification orders for defective residential work, this mechanism does not provide a complete solution in all cases. The Society understands that in practice, rectification orders are typically only implemented after a decision is made by a Court or the NSW Civil and Administrative Tribunal. In many instances, this means that owners are forced to wait years for any action. In the meantime, occupants are left exposed to safety risks and owners are exposed to the costs of interim safety measures.

The Shergold Weir Report found that across Australia, authorities do not have the necessary powers to require rectification of defective works. The report recommended that regulators be given a broader suite of powers to monitor buildings and building work so that, if necessary, they can take strong compliance and enforcement action. Stronger compliance and enforcement powers will enable the relevant regulatory authority to compel the builders to rectify defects more promptly.

Fragmented regulatory framework

Unlike Victoria, NSW does not have a centralised body overseeing building regulation compliance. Rather, the regulatory system in NSW is somewhat fragmented – local councils, the Building Professionals Board, the Department of Planning and Environment and the Department of Fair Trading each have distinct regulatory functions.

As highlighted by the Shergold Weir Report, this results *“in a fragmented system of regulatory oversight which is prone to duplication, confusion, unclear lines of responsibility and a lack of information sharing.”*

The Society considers that reforms to the NSW building regulatory framework which consolidate the regulatory powers and responsibilities of local councils, the Building Professionals Board, the Department of Planning and Environment and the Department of Fair Trading, and give those powers and responsibilities to a centralised body will:

- streamline regulatory oversight responsibilities to ensure the culture of non-compliance in the building industry is systematically extinguished;
- increase regulatory efficiency, allowing rectification works to be undertaken more rapidly;

- improve the building and construction industry’s understanding of, and consequently compliance with, the relevant regulations; and
- instil greater confidence of the public and construction professionals in the NSW building regulatory system.

Insurance

The NSW government and professional indemnity (PI) insurers are currently in a stalemate: the government requires that building professionals hold PI insurance without any cladding-related exclusions. Meanwhile, PI insurers have responded to the cladding crisis by only renewing policies with cladding-related exclusions or alternatively, charging unaffordable insurance premiums and increasing excesses payable for each claim. This means that building professionals can only obtain the insurance needed to maintain their registration by paying unaffordable insurance premiums and excesses, or necessarily lose their registration.

If this stalemate continues it is likely to force an unprecedented number of building professionals out of the market – whether as a result of financial distress or deregistration. This could ultimately result in a collapse of the building and construction industry. It is clear that action needs to be taken, ideally by both the government and insurers.

The State of Victoria has already commenced the process to remove the requirement for certain building professionals to hold PI insurance without cladding-related exclusions. The Society considers this is a useful temporary solution to ensure the building and construction industry continues to operate. Separate issues may arise in the event that building professionals are sued in cladding-related claims and are uninsured for those claims. However, in the meantime, the Society considers that the Victorian solution is a necessary immediate step.

Rectifying existing buildings with combustible cladding

The NSW has gathered significant information and assessed the extent of the cladding problem in NSW through the Fire Safety and External Wall Cladding Taskforce audit. However, to date, it has not outlined any plans for rectifying existing buildings with combustible cladding.

The Andrews Labor Government in Victoria recently announced its intention to establish a program to tackle high-risk cladding, by introducing a \$600 million package to fix buildings with combustible cladding. It is intended that the grants will fund rectification works on hundreds of buildings found to have high-risk cladding, to make sure they are safe and compliant with all building regulations. The program will be overseen by a new agency, Cladding Safety Victoria, which will manage funding and work with affected owners’ corporations from start to finish. The Victorian Government will directly fund half of the rectification and will introduce changes to the building permit levy to raise the other \$300 million over the next five years. It has been suggested that as part of any funding agreement, the owners’ corporation accepting funding will agree to novate its right to pursue action against the responsible building professionals to the State. It is recommended that a similar system be introduced and implemented in NSW.

RECOMMENDATIONS

Below is a list of recommendations provided by the Society.

1. Address the culture of non-compliance within the building and construction industry by reforming the regulatory framework to streamline the powers and responsibilities of each of the regulatory bodies.
2. Broaden the powers of the relevant regulatory authorities to enable the regulators to ensure rectification works are undertaken rapidly by the responsible builder/parties.
3. Change the requirements for all building professionals to have comprehensive professional indemnity insurance.

4. Fund rectification works for high-risk buildings affected by combustible cladding and other significant latent defects under a system whereby the NSW government can step into the shoes of the relevant owners' corporation to seek to recover the rectification costs from responsible parties.

References

Deakin report analyses growing number of apartment building defects, Media release, 19 June 2019, <https://www.deakin.edu.au/about-deakin/media-releases/articles/deakin-report-analyses-growing-number-of-apartment-building-defects>

Glossary

ACPs	aluminium composite panels
Act	<i>Home Building Act 1989</i> (NSW)
HBC Scheme	Home Building Compensation Fund Scheme
DTS	deemed to satisfy solutions
Inquiry	NSW Legislative Council's Public Accountability Committee's Inquiry into the regulation of building standards, building quality and building disputes
NCC	National Construction Code
PI	Professional indemnity
Regulations	<i>Home Building Regulation 2014</i> (NSW)
SBBI Scheme	Strata Building Bond and Inspections Scheme
Society	Society of Construction Law Australia

Summary table of key issues & recommendations	
KEY ISSUES	SUMMARY OF RECOMMENDATIONS
Certification	
<p>Unscrupulous and unregulated strata unit developers have caused significant economic and social damage due to non-compliant construction.</p>	<ol style="list-style-type: none"> 1. Introduce a statutory requirement that all architectural and engineering plans including hydraulics, structural, fire engineering plans as well as plans for variations must be signed off and declared by a statutory declaration. 2. Introduce a statutory requirement that plans in respect of structural, hydraulics or fire engineering must be submitted to the regulator. 3. Introduce a statutory requirement that engineers must provide an outline of the methodology adopted by the designer to satisfy itself that the design for the structural elements of the building are fit for purpose and complies with the relevant Standards identified in the DTS performance requirements. 4. Introduce a requirement that the builder's declaration of the final building work must be corroborated by the building designers. 5. Introduce a national register of engineers. 6. Amend legislation to make clear that the principal duty of care is owed by the original developer / builder to the purchaser and successors in title of the property. 7. Introduce compulsory major defects project insurance, with the premium dependent on the degree to which the developer / builder is prepared to satisfy the State regulatory bodies as to compliance. As well as introducing a statutory obligation on the original developer /builder to ensure compliance.
Insurance	
<p>The short statutory warranty period.</p> <p>The HBC Scheme exemption for buildings over three rises.</p>	<ol style="list-style-type: none"> 8. Extend the statutory warranty period in the Act to, at a minimum, a period of 10 years for all defective building work (regardless of whether it is a major defect). 9. Introduce a statutory warranty for the benefit of both new and subsequent apartment owners which imposes a duty of care on the builder. In circumstances where the builder no longer exists, this statutory warranty would shift to the developer. 10. Introduce reform to the HBC Scheme so that it applies to all residential buildings, including those that are more than three rises high.

Summary table of key issues & recommendations	
KEY ISSUES	SUMMARY OF RECOMMENDATIONS
Strata committees' management of defects in common areas	
<p>Lack of protection for owners from the cost of rectifying defects in common areas.</p> <p>Strata committees' potential lack of knowledge and conflict of interest.</p>	<ol style="list-style-type: none"> 11. Extend the statutory warranty period in the Act to, at a minimum, a period of 10 years for all defective building work. 12. Introduce a statutory warranty for the benefit of both new and subsequent apartment owners which imposes a duty of care on the builder. In circumstances where the builder no longer exists, this statutory warranty would shift to the developer. 13. Amend the Act to specify that the management of substantial defect rectification over an amount set in the Regulations is not delegable to strata committees. 14. Amend the Act to place an obligation on body corporates to ensure that strata committee members have an understanding of the building's by-laws and the governing state legislation, the building's past committee and general meeting minutes, issues and financial position. 15. Establish a State Government defect fund such as using a percentage of funds received by the government from stamp duty payable on high rise residential buildings. 16. Establish a new State Government agency to manage the defect fund and work with owners corporations through the defect rectification process. 17. Reform the HBC Scheme so that it applies to all residential buildings. 18. Support a coordinated response from all State Governments in Australia to produce uniform legislation.
Cladding & other serious defects	
<p>A culture of non-compliance in the building and construction industry.</p> <p>Insufficient regulatory powers and a fragmented regulatory system.</p> <p>Conflict between the NSW government and PI insurers over the introduction of cladding-related exclusions.</p>	<ol style="list-style-type: none"> 19. Address the culture of non-compliance within the building and construction industry by reforming the regulatory framework to streamline the powers and responsibilities of each of the regulatory bodies. 20. Broaden the powers of the relevant regulatory authorities to enable the regulators to ensure rectification works are undertaken rapidly by the responsible builder/parties. 21. Change the requirements for all building professionals to have comprehensive professional indemnity insurance. 22. Fund rectification works for high-risk buildings affected by combustible cladding and other significant latent defects under a system whereby the NSW government can step into the shoes of the relevant owners' corporation to seek to recover the rectification costs from responsible parties.