**REPORT OF PROCEEDINGS BEFORE**

# STANDING COMMITTEE ON LAW AND JUSTICE

## INQUIRY INTO HOME BUILDING (INSURANCE) AMENDMENT ACT 2002

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**At Sydney on Thursday 11 July 2002**

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**The Committee met at 10.00 a.m.**

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**PRESENT**

The Hon. Ron Dyer (Chair)

The Hon. John Ryan

**JOHN LANCE SCHMIDT,** Deputy Director-General, Cabinet Office, Level 39, 1 Farrer Place, Sydney, affirmed

**PETER EDWARD SMITH,** Public Servant, Level 12, 234 Sussex Street, Sydney,

**LYN FAY BAKER,** Public Servant, 234 Sussex Street, Sydney, and

**CHRISTOPHER JAMES AIRD,** Public Servant, Level 20, 227 Elizabeth Street, Sydney, sworn and examined:

**CHAIR:** Mr Schmidt, in what capacity are you appearing before the Committee?

**Mr SCHMIDT:** I am representing my former role as Assistant Director-General of the Department of Fair Trading.

**CHAIR:** Did you receive a summons issued under my hand in accordance with the provisions of the Parliamentary Evidence Act?

**Mr SCHMIDT:** I did.

**CHAIR:** Are you conversant with the terms of reference of this inquiry?

**Mr SCHMIDT:** I am.

**CHAIR:** Could you briefly outline your qualifications and experience as they are relevant to the terms of reference of this inquiry?

**Mr SCHMIDT:** Until the end of last week I was Assistant Director-General, Policy and Strategy, of the Department of Fair Trading. That area of the department is responsible for developing legislation and implementing the Government's policy in relation to matters falling within that department, and in this case, the Home Building Act.

**CHAIR:** The Department of Fair Trading has made a written submission to this inquiry. Are you happy to have that included as part of your affirmed evidence?

**Mr SCHMIDT:** I am.

**CHAIR:** Mr Smith, in what capacity are you appearing before the Committee?

**Mr SMITH:** I am the Director of the Home Building Division, which is responsible for the administration of the Home Building Act provisions as they relate to licensing and to the closed government insurance scheme.

**CHAIR:** Did you receive a summons issued under my hand in accordance with the provisions of the Parliamentary Evidence Act?

**Mr SMITH:** I did.

**CHAIR:** Are you conversant with the terms of reference of this inquiry?

**Mr SMITH:** Yes, I am.

**CHAIR:** Could you briefly outline your qualifications and experience as they are relevant to the terms of reference of this inquiry?

**Mr SMITH:** As Director of the Home Building Division I have experience in the administration of licensing, the closed government insurance scheme and the general disputes that arise with home building insurance.

**CHAIR:** Are you willing to have the department's written submission included as part of your sworn evidence?

**Mr SMITH:** Yes, I am.

**CHAIR:** Ms Baker, in what capacity are you appearing before the Committee?

**Ms BAKER:** In my capacity as Assistant Director-General, Property and Licensing, of the Department of Fair Trading.

**CHAIR:** Did you receive a summons issued under my hand in accordance with the provisions of the Parliamentary Evidence Act?

**Ms BAKER:** Yes, I did.

**CHAIR:** Are you conversant with the terms of reference of this inquiry?

**Ms BAKER:** I am.

**CHAIR:** Could you briefly outline your qualifications and experience as they are relevant to the terms of reference of this inquiry?

**Ms BAKER:** In my role as Assistant Director-General, Property and Licensing, the Home Building Division falls into my area of responsibility. So for the past three years I have had responsibility for home building, including licensing, the closed insurance scheme and the private insurance scheme.

**CHAIR:** Are you willing to have the department's written submission included as part of your sworn evidence?

**Ms BAKER:** Yes.

**CHAIR:** Mr Aird, in what capacity are you appearing before the Committee?

**Mr AIRD:** As Manager, Legislation Branch, within the Policy Division of the department.

**CHAIR:** Did you receive a summons issued under my hand in accordance with the provisions of the Parliamentary Evidence Act?

**Mr AIRD:** Yes, I did.

**CHAIR:** Are you conversant with the terms of reference of this inquiry?

**Mr AIRD:** Yes.

**CHAIR:** Could you briefly outline your qualifications and experience as they are relevant to the terms of reference of this inquiry?

**Mr AIRD:** As Manager of the Legislation Branch I was involved in assisting Parliamentary Counsel in developing the legislation.

**CHAIR:** I take it that you are happy to have the written submission of the department included as part of your sworn evidence?

**Mr AIRD:** Yes, I am.

**CHAIR:** If any of you should consider at any stage during your evidence that, in the public interest, certain evidence or documents you may wish to present should be heard or seen only by the Committee, the Committee will be willing to accede to your request. However, I should add that the

House has the right to override our decision in that regard, if it so chooses. Mr Schmidt, I invite you to make a brief opening oral statement to the Committee.

**Mr SCHMIDT:** I could go back a considerable period and give you the history of the former Building Services Corporation [BSC] and the establishment of the new arrangements whereby private insurance is provided in this market. However, I will confine my opening comments really to the events which led to the environment in which the legislation ultimately appeared in its current form. We have some material which we could table later—material which is based on documents that were provided in another place for the Joint Select Committee on the Quality of Buildings, which gives the history and background to the operation of building, licensing and insurance in New South Wales.

As you may be aware, the change to private insurance took place in 1997. The former government scheme closed in May 1997. Insurance was provided through a number of private insurers. The arrangements are as follows. Normally insurers are approved by the Government to provide this form of insurance. Those insurers then offset some of their risk through the reinsurance market. In fact, it is a similar arrangement to the arrangement that operated in New South Wales when the government scheme was operating. The Government offsets its risk by reinsurance and this operates to this day in Queensland with a government scheme there.

The players in the private sector changed over time. Some reinsurers came and left and some of the insurers changed identity. For example, at one point FAI, which had been a separate entity, merged with the HIH group. The market was reasonably stable during this period until events began to unfold last year. The first major shock to the system came with the collapse of HIH. HIH had a significant share of the market in New South Wales. Remember that it was HIH now combined with FAI. The effects of the demise of that company were many. There was great upheaval for builders. Builders who had previously dealt with HIH suddenly found that they had to find insurance elsewhere if they were to be able to continue to do their work.

For jobs that were in place there was even a question mark as to the status of work that builders could do. You are required to have insurance in place to undertake relevant residential building work. The Government took some immediate measures to try to stabilise the market at that stage. It established a rescue vehicle—the Builders Insurance Guarantee Corporation—which stands behind all existing HIH and FAI policies. That had a number of positive impacts. It enabled those builders who were building with those policies to continue to do work and, obviously, it gave consumers protection. There was somebody to stand behind those policies.

For builders, though, there was a considerable period of upheaval. Having settled down the consumer side, once builders finished those jobs where they had HIH-FAI policies, they had to find replacement policies. The two major players in the market who were left were Dexta, whose insurer is Allianz, and HIAS, whose insurer is Royal and Sun Alliance. They were not geared to take up that massive slab of the market and found it very difficult. The Government intervened again to assist. It provided some financial resources to both insurers and also staff from New South Wales to try to assist with getting builders reassessed under the new regimes of those particular insurers. The same problems were experienced in Victoria and other parts of Australia.

After some difficulties it appeared that things were beginning to settle down. The market was stabilising, although some builders were still tied up in the queue to have their insurance replaced. Unfortunately, we then had the events of September 11—which are well known to people. Even though they were overseas events and home warranty insurance is a small product in the insurance field, it was not immune to the impacts. The impacts first manifested themselves in New South Wales in December last year when one of the insurers, the Dexta-Allianz arrangement, was negotiating to replace or reinstate its reinsurance arrangements. What normally happens is that the insurers lock in a panel of reinsurers for a time and those panels come up for review periodically.

Dexta-Allianz had reinsurance with an entity, Swiss Re, which is one of the largest reinsurers in the world and one of the longest-serving reinsurers in the world home warranty market. It announced that it was leaving the market worldwide. Dexta-Allianz was negotiating with a French company to fill the gap left by the impending departure of Swiss Re and that company expressed great concern about the operation of the New South Wales market: the parameters within which the insurance was provided and the scope of the scheme. Discussions took place and a reinsurance

arrangement was put in place to enable Dexta-Allianz to continue. Those arrangements continued from December to April this year.

Shortly thereafter the Government had approaches from both the French reinsurer, SCOR, and the other major insurer in the market, Royal and Sun Alliance, which indicated clearly to the Government that, if it was to continue in this particular field, it was looking for significant reforms to the operation of the market. It wanted the introduction of a distinction between structural and non-structural defects; it wanted the Government to remove the requirement for high-rise insurance; it wanted the Government to move to a last resort scheme based on existing models in South Australia and Western Australia; and it raised some other issues. Basically, the company put a log of claims to the Government.

New South Wales and Victoria decided that those issues should be addressed on a joint basis by the respective State governments so intensive negotiations took place to try to nut out an arrangement for the insurance to go forward. It should be noted that this was an area of insurance where some players—Swiss Re is one example—had made a decision based on overseas events and on the history of their involvement in this market across the world, not just in Australia. To put it bluntly, they could find a better place to put their capital rather than in the home warranty market. The insurers were in a difficult position in that it was not as though they were speaking with one voice and saying to government or anybody else, "If you give us these parameters, we can stay in the market on that basis." They must also satisfy their overseas backers that the arrangements will be satisfactory.

One example of how difficult that can be is that although ultimately an arrangement was entered into, and the governments' policy settings in New South Wales and Victoria would have addressed most of the issues that the insurers and reinsurers had raised and put on the table, the French reinsurer, SCOR, on 1 April decided that it would not stay in the market at all. This created great difficulties for the Dexta-Allianz arrangement in that it simply could not operate unless it had the necessary reinsurance in place. Another aspect of the Government's rescue package—although it is not reflected in this legislation—was that the New South Wales and Victorian governments agreed to act as a reinsurer for the Dexta-Allianz insurance products in order to stabilise the market. Those arrangements were recently extended to 31 December.

In relation to high-rise, despite the other reforms being acceptable to the players, the Royal and Sun and the Dexta-Allianz entities could not find reinsurers who would be willing to take on the high-rise risk. So in New South Wales the Government has maintained 100 per cent coverage of the high-rise cover, which those entities are writing. In Victoria they have taken a different approach: they have taken away the mandatory requirement for high-rise cover for consumers in that State and are implementing a catastrophe fund to provide a level of cover. That is the context in which this legislation came forward.

**CHAIR:** Thank you. The submissions that the Committee has received fall into a number of groupings. There are submissions from your department; the insurers; the Insurance Council of Australia; builders and building organisations, such as the Master Builders Association and the Housing Industry Association; and consumers to a minor extent—although they have, perhaps surprisingly, been somewhat slow to respond to our invitation to make submissions. My questions largely arise from concerns that have been raised in some of those submissions.

I will begin historically. Several submissions, especially those from small builders, appear to lament the demise of the Building Services Corporation [BSC] and the scheme that existed at that time. I realise that the issue has a long history and that the Building Services Corporation was preceded by the Builders Licensing Board. I do not want you to give an exhaustive, blow-by-blow account of the history of the whole matter but could you identify briefly for the Committee the factors that essentially led to the replacement of the Building Services Corporation?

**Mr SCHMIDT:** I will pass that question to Chris Aird, who is one of the longest-serving officers of the department and who has an extensive knowledge of the history of the former BSC and related developments.

**Mr AIRD:** I suppose the initial move to a private scheme started in 1993 when the Dodd report was released. In 1991 a royal commission was established in New South Wales to look into

various matters in the broader building industry. It did not focus on residential building or the BSC. However, a number of complaints about the BSC and residential building work were made to the royal commission, which then undertook some investigations. When the royal commissioner handed down his report he said that he did not have time to conduct a lengthy investigation of the Building Services Corporation or the residential industry and recommended to the Government that there be an inquiry into the BSC.

The Government appointed a commissioner—Peter Dodd—to conduct an inquiry into the Building Services Corporation in 1993. He handed down a report that included the finding that there was no reason why there should be a monopoly government scheme. Based on that finding, the then BSC undertook feasibility studies and research with the insurers about the establishment of a private scheme.

Work on that took place between 1993 and 1995. I was not personally involved in that and I am a bit vague and about that area. The BSC appointed a consultant to work within the organisation to liaise with the insurers and it established a working group of insurance bodies, the Cabinet Office and Treasury. The working group developed a model for the insurance scheme. When the Labor Government came to power the BSC continued the process of developing that private scheme. In 1995 Cabinet approved the movement towards the private scheme and the legislation came into force in 1996 because there was a bit of the delay before it was passed and it commenced in May 1997.

At that time I assume the national competition policy would have been in the minds of the Government. I suppose that, coupled with the general dissatisfaction with the BSC at that time and the recommendation to move away from a monopoly insurer, would have been the driving force towards it.

**CHAIR:** A number of submissions to this inquiry from builders expressed frustration and dissatisfaction about what they termed as the ongoing difficulty in obtaining home warranty insurance. I refer to small builders and young builders and what they say are long waits for applications for insurance to be approved. Do you have any view on that?

**Mr SCHMIDT:** It has been a fact of the market that there have been significant delays and difficulties for builders in giving insurance. It is interesting to go back before the HIH collapse and track it forward to see how it developed. The HIH influence cannot be understated on this market, and we see more and more examples of distortion of the insurance market that that corporation seems to have brought to bear in the Australian scheme.

**CHAIR:** Is that because HIH dominated this area of insurance?

**Mr SCHMIDT:** It dominated by being a very large player and significantly undercutting the market. Yesterday the *Financial Review* reported APRA as saying that insurance across Australia, and I do not know whether they were referring to building as well, has been significantly underpriced. HIH significantly undercut the market and went in for market share with an aggressive policy. That was reflected in its administrative arrangements. When the Government moved the scheme into private hands one expectation was that although the Government would remain as a regulator in licensing builders and would check on qualifications, behaviour and other relevant factors, the insurers, with their particular interests and expertise, would be better placed to do financial assessments.

A key component of licensing or insurance, be it government or private, is the financial wherewithal of the builder. We know only too well with business it is possible to structure affairs through $2 companies and walk away and leave things in the lurch. The insurers have a vested interest, obviously they are the ones to be picking up the tab, to make sure that there are sufficient assets in the building entity. HIH did not do rigorous assessments. Anecdotally we hear of people turning up, quoting the size of a job, a figure being given for the premium, then paying it and off they go.

Having said that, towards the end of the operation of HIH we began to receive representations from builders who were unhappy because HIH seemed to be changing its role and lifting its game, it was starting to take an active role in assessing the wherewithal of builders. However, builders who had

been dealing with that company had been lulled into a false sense of security, because they had not been subject to that scrutiny. The other insurers were somewhat tougher. With the absence of HIH, not only was there a large group of builders that had to move to a completely different insurer, with whom they had not dealt before, and go through the administrative processes, but that insurer had to put in place arrangements to try to handle the flood of work.

In addition some builders had never been properly financially assessed by an insurer. So, naturally enough, they turn up at another insurer and that insurer wants to see their statement of account and profit and loss. The builders were not used to that sort of scrutiny. With the impact of the flood of builders trying to get insurance, the more difficult ones dropped to the bottom of the pile. They were not followed up and there were terrible delays. The department put a couple of officers into the Melbourne offices of the two remaining insurers to find out what was going on with the backlog of cases.

In the majority of cases where there was a communication breakdown the insurer had requested further information in support of an application and the builder had not responded. That was partly because the builder did not understand what they were being asked because they had never gone through that scrutiny before. Unfortunately this had a compounding effect. Builders were suffering from that and trying to get insurance and builders who were dissatisfied with the scheme were now undergoing a greater level of scrutiny than they were accustomed to. Backlogs developed, and people were caught in the mix.

To this day that is still a problem with some builders in getting communication. We have been speaking to the insurers to try to get them to lift their game. One recent development was that Royal and Sun committed more resources to the arrangements and recently opened a second string of brokers with whom builders can deal. Hopefully that second stream will help builders ease their way through the system. They are also doing other things to help improve communication. I am not defending the insurers, although I can understand the demands put on them. However they did not respond particularly well and builders experienced difficulties.

A legitimate complaint of builders is that insurers have been secretive about their financial criteria. The difficulty is that it is all very well to say to a builder, "Yes, you must be subject to financial scrutiny before you can get insurance" and then say, "We are not going to tell you what our parameters are. Just put in an application and if we want more information we will get back to you until you get it right." All insurers have admitted that that must change and have committed themselves to making that financial criteria transparently available so that people can get their applications in a proper state when they put them in.

**CHAIR:** You are suggesting that in due course the insurers will disclose the criteria?

**Mr SCHMIDT:** Yes, they have recognised the communication failings and have given us various undertakings that they will improve it.

**CHAIR:** Another theme of the builders' submissions is dissatisfaction with the common requirement by insurers that deeds of indemnity or bank guarantees be provided. Could you comment on that?

**Mr SCHMIDT:** Yes, we have different figures from different insurers as to the degree of financial security required. In recent times there have been changes in practice. Basically it is about capitalisation. The insurer will want to see either a dollar value of capital in the company or, for whatever reasons such as tax, the builder does not want to put up assets in a particular building entity, but assets must be available should a claim be paid out. That is understandable on the insurer's part because the bulk of dollars paid out by insurers is because they or their entities become bankrupt or insolvent. Under the old New South Wales Government's scheme and under the current Queensland Government scheme it has always be a requirement that there be some financial adequacy test for builders.

When we speak to builders we hear a strong dialogue amongst builders about the reasonableness of those requirements. I have sat in on discussions where builders have had strong views and said that it is unreasonable, that they should be able to build and that their record should be

all the guarantee that is needed. However, if for some reason or circumstances beyond their control they get into financial difficulty that is no comfort to the insurer or consumer. Other builders are very adamant the other way and say it is not unreasonable. They say that they have gone to the trouble of building up their industry and putting their assets on the line and they expect there to be a level playing field.

That should be reflected in some capital requirements. We are aware of very few bank guarantees that are demanded. A bank guarantee means that someone is putting aside some capital that is available. Obviously the person giving that guarantee has got the wherewithal to provide it. For whatever reason they decide not to put that money into the business itself, but decide to keep their capital with a financial institution and give a guarantee against those funds. The more prevalent security is a deed of indemnity. They seem to be losing favour with the insurers. We received varying feedback from insurers as to how widespread a deed of indemnity is used by builders. Certainly with corporate structures they seem to have been reasonably prevalent.

A deed of indemnity is a means of getting that extra capital into the business to enable the builders to get insurance. The capitalisation requirements vary from company to company. The smallest new insurer, Reward, has a very clear policy of a 20 per cent capitalisation requirement. If the builder has 20 per cent of capital to turn over in the business, Reward does not need any other security. Other insurers have different requirements, depending on the particular structure. If the builder cannot put up the capital, one means of getting across the line is a deed of indemnity. In recent times Royal and Sun Alliance announced that except in very limited circumstances it will no longer require deeds of indemnity.

Every year the insurer reassesses the builders and unless there is a major change in turnover, in which case they might bring the assessment forward, those who have given indemnities in the past will have them returned if they are not in the limited category builders who still require them. On the other hand the Dexta group has made it very clear that it does not intend to change its policy. There is a bit of differentiation in the market. We understand the problem, but there is a basis for it.

**CHAIR:** Some builders have suggested that subcontractors should also be required to obtain insurance. What is your view on that?

**Mr SCHMIDT:** I find that a very interesting proposition. What seems to be underlying that argument is that in some way builders should not be responsible for tradesmen. To put it baldly, they seem to be saying that if a consumer were to engage builder X, and something goes wrong and builder X knows that the brickie did it wrong, the consumer would have to take action against the brickie and therefore the brickie should have insurance. I have never seen a builder advertising their services and saying to a consumer, "Yes, I am happy to do the job, but by the way, if something goes wrong I may not be to blame because I cannot be responsible for my subcontractors. If the subcontractor is at fault you will have to claim against the subcontractor."

The point of contact in the contract is the builder and the consumer. The consumer is the novice and the builder is the expert. The consumer relies on the builder's expertise in choosing materials, work practices and the tradesmen. That is my personal observation. And I see some difficulties with this.

**CHAIR:** Is there any likelihood of reduced insurance premiums as a result of the new or present scheme?

**Mr SCHMIDT:** There have been mixed comments on the impact of these reforms on insurance premiums, just as there has been in the wider field about government reforms in other areas of insurance. The comments seem to range between "It will stabilise the market and constrain future premium increases", to an insurer signalling that "Premiums might drop up to 20 per cent in the next two years."

**CHAIR:** Could you identify what you see as the likely benefits of the new or present scheme for the industry and consumers.

**Mr SCHMIDT:** The insurance industry is providing a framework through which it will form an assessment as to profitability. Certainly Royal and Sun Alliance has committed considerable new resources to expand its operations following the reforms. The NRMA has been quoted in the media as saying that it is seriously looking at that market. I have had discussions with someone from the NRMA who reinforced that. From the insurance perspective, the hope is that the parameters have been set for a market which would offer a profitable area for them in which to operate.

These reforms do go some way to addressing some of their concerns. One of the concerns we have often had expressed by builders is that prior to a move to last resort when an insurance claim could be made when a contract was still on foot, they felt they had lost some of the relationship with the consumers in that it was theoretically possible for a consumer to walk away from a contract, lodge a claim with an insurer who might then pay it out, yet the builder not be given adequate opportunity to respond to that claim. That area has now been resolved by the clarity of the move to last resort.

For builders it should also significantly alter the risk profiles that are used by insurers in basing their assessment criteria and their premiums, so we expect to see improvements there. For the consumers the scheme has been maintained; there is insurance in place. One of the options obviously when the whole thing began to suffer extreme stresses and strains in the past year or so was to remove the mandatory nature of the requirement. New South Wales has not followed the Victorian approach and the approach of a couple of the other States as well to take high-rise out of insurance requirements. There is insurance in place for consumers. The parameters of that insurance have changed but the product is still available in the market place.

**Ms BAKER:** In respect of builders, consumers and insurers certainty would be the word that I would use. Prior to these insurance blips that have happened in the past year, builders have raised with us on a number of occasions things like "How can we guarantee paint work for seven years? It is ridiculous." So some of the reforms are addressing things that builders have raised with us over a period of time. Some of the reforms will make it more certain for builders to know what is covered and when a consumer can claim against defective work. It also provides for us to enhance the responsibility that builders take for their work because it is last resort, the builder is responsible to rectify the work, and that is the best thing that can happen for consumers rather than going through a claims process.

In terms of consumers, again it is a system. We prod one part of the system and we anticipate some good things will happen like reduced premiums over a period of time and also a better service delivery if the reforms cause the kind of competition that we anticipate, and additional insurers may come in. So better service. Prior to the insurance issues in 2001, the biggest issues raised with us by consumers were about claims problems. I anticipate that the insurers will need to lift their game in that area when competition ultimately arises.

**Mr SCHMIDT:** One further comment, people fail to remember when looking at this issue, is that it is not like turning on and off a tap. Some people were pushing very strongly when the problems of earlier this year began to arise, "Why doesn't the Government just reintroduce a government scheme?" That is not something you can do. You cannot say one minute that there is a government scheme and private insurers close their doors and walk away. How could the Government get into the market place immediately to enable the builders to build? Some builders have called for a moratorium from the insurance requirements until some of the past problems settle down. What does that mean for consumers? Can government say to consumers they should just deal with any builder and if there is a problem, maybe down the track we might able to provide some sort of cover because we have not got those arrangements in place?

What does it mean for good builders? People also tend to forget that the majority of builders kept building. We have had a boom in New South Wales. There have been difficulties—no-one will deny that—but the majority of builders and consumers have been able to get residential building work done. Those ones who have been doing the right thing and standing behind their work and putting their money on the line, what would they have done if there had been a moratorium or the scheme had been swept away with nothing to replace it? There will always be people who are unhappy with aspects of the legislation. We will never be able to have a scheme which satisfies all players. The Government has been able to introduce some stability into the market to see how things sort themselves out. We cannot predict this time next year that there will not be another event overseas or

in Australia which completely unsettles the market. At the moment we have locked in arrangements under a framework which provides insurance to builders and consumers.

**CHAIR:** Would the department regard it as a positive development if there were new entrants to the ranks of the insurers to provide added competition?

**Mr SCHMIDT:** Absolutely. I had discussions the week before last with a particular broker who was talking about a small change with the suggestion of new players coming into the market or new products being made available through that brokerage and that the standard of service delivery that they had experienced from insurers with whom they were dealing was remarkably improving. I have no doubt that competition will have very positive impacts.

**CHAIR:** I assume you agree that dispute resolution is an important component of the new scheme. It may be somewhat early for you to comment but is there any indication of the success of the Building Conciliation Service and the Consumer, Trader and Tenancy Tribunal? If you are able to comment on that, are there any plans in place for reviewing the success of those structures?

**Mr SCHMIDT:** That leads on to a comment made by Ms Baker earlier that 18 months or two years ago the major source of complaint about the scheme was really how claims were being handled by insurers in dispute resolution. It was leading out of that that a raft of reforms were introduced last year by the Government and commenced on 1 January in one significant area, the establishment of the Building Conciliation Service through the tribunal. It was the Fair Trading Tribunal and now it is the Consumer, Trader and Tenancy Tribunal. From information which has been given by the tribunal—I refer to the testimony and great deal of material given to the Joint Select Committee on the Quality of Buildings by the Chairperson, Sally Chopping—it would appear that the scheme is quite successful. What is an interesting facet of that is that some figures I saw which dealt with the operation of that service earlier this year showed that the biggest group of claims were, in fact, under $5,000 that that service was handling. The significance is that $5,000 is where the old insurance threshold used to be, so already that scheme was directed towards helping those people who for a start did not have insurance but had a dispute. The alternative dispute resolution system for claims of less than $5,000 the majority of matters were being resolved through mediation.

It must be remembered that people at that end of the market in the building industry tend to be the mums and dads. They are not the ones who have the sophisticated financial structures who want to go broke and can walk away from their responsibilities. Those people tend to be the ones who want to keep trading and their reputation is their collateral. If a mechanism can be devised to enable people to settle their disputes they may be able to be resolved. The figures from the tribunal would suggest that that is the case. Certainly, there have been other changes. The Building Conciliation Service looks at the whole range of claims, and it is interesting that most of them are smaller amounts. But most home warranty claims are not large sums of money but there are some very large ones occasionally. Certainly we believe that the system seems to be making inroads in providing another source of dispute resolution but the tribunal would probably be better placed to talk in more detail about that.

**CHAIR:** What is an average amount in dispute?

**Mr SCHMIDT:** From my recollection approximately two-thirds would be under $25,000 and one-third might be under $10,000. The bulk of the claims were not large sums of money.

**CHAIR:** I put to you a brief extract from the submission of the Master Builders Association to the committee:

> There is no guarantee that existing insurers still will not withdraw. What is guaranteed by the Act is that insurers' exposure has been substantially reduced.

What do you say about that?

**Mr SCHMIDT:** There is absolutely no doubt that there is no way you can force an insurer to stay in the market but be it a government or private scheme the same problem will arise. As I have said earlier, the old government scheme in New South Wales and the current government scheme in Queensland is in the majority underpinned by private reinsurance. I understand that the reinsurance arrangements in Queensland were negotiated for a further three years in July of last year—before

September 11—and even then they had difficulties getting the reinsurers in the private market to come to the table and they had to change their premium structure and agree to some other changes to keep them in the market. The answer is, be it a government or private scheme, there is no guarantee you will have the financial underpinning for that system. But that is the nature of business and that is true of any insurance product or a whole range of services in the community.

In relation to insurers' exposure being substantially reduced, certainly part of the basis that the insurers were coming to us was that they felt in light of the losses they had suffered to date, something had to be done to limit their exposure. One of their areas was not actually the claims paid but the administration of the claims. They said of the scheme as it was then operating that they were spending vast sums of money just dealing with the legal and administrative sides of matters. Yes, we believe that insurers' risks should have been reduced by these changes which is why we are looking forward to ultimately changes in premium and the profiles that they use to assess builders' risks.

**CHAIR:** Am I correct in believing, so far as the model of the scheme is concerned, that New South Wales and Victoria have followed the same path and there is a similarity with that model in South Australia and Western Australia as well?

**Mr SCHMIDT:** Yes, in relation to the New South Wales and the Victorian schemes part of the agreement between governments was to try to harmonise those schemes as much as possible. The major area of difference at the moment is high-rise where we have continued the requirement: they have not. The time limits and the range of cover vary from jurisdiction to jurisdiction but the majority of States now have similar time limits—six years is the general period for cover. The scope of works vary from jurisdiction to jurisdiction. You may be aware of the work of Professor Percy Allen who has been engaged to do an inquiry on behalf of the Ministerial Council on Consumers Affairs. Part of the reason why he was engaged was to look at the Australian market and the various schemes and to see if there were ways to harmonise them to try to create a national market. New South Wales and Victoria are obviously the largest markets so anything that we can do will have a major influence on the other jurisdictions. But one of the aims would seem to be to try to harmonise the scheme completely.

**CHAIR:** Professor Allen has indicated that he is willing to brief the committee on his inquiry later. Is it correct from what you say that the Queensland scheme is different: that it is a one-off within Australia?

**Mr SCHMIDT:** It is different and it is same. It is an insurance scheme but it is run by a government arrangement but it is a government arrangement underpinned by the private market through reinsurance. We hear various comments about the operation of the Queensland scheme. They have had the benefit of having a continuous operation for a period of years. One of the difficulties we face in comparing schemes is that the schemes in all jurisdictions have chopped and changed over time so even statistically it is very hard to get an apples and apples comparison. But the Queensland scheme, it must be remembered, has some deficiencies, perhaps some people could say, in that it does not cover high-rise. So consumers of high-rise buildings in Queensland do not have the protection of the scheme. It has a time limit of 6½ years which is slightly longer on paper compared with New South Wales and Victoria, but it is 6½ years from the date of the contract and we are from the date of completion.

In fact the New South Wales and Victorian schemes probably on a temporal basis are now more generous than the Queensland scheme. The Queensland scheme draws the distinction between structural and non-structural defects. The Queensland scheme has areas of cover. One-third of its claims deal with matters which seem to be a particular problem in Queensland which do not appear to be a problem in other jurisdictions which relates to subsidence. Again, not only is it difficult to compare within a jurisdiction like New South Wales, the scheme as it was a few months ago with as it was 1997, it is difficult to compare Queensland and New South Wales or Victoria because within those schemes there are very major differences between them.

**The Hon. JOHN RYAN:** I was going to wait until the end and ask you a series of questions, some of which will cover similar ground to Mr Dyer, but, as you are aware, I am a member of the other committee that is looking at this matter and we received a two or three-hour briefing from the Queensland Building Services Authority. They quite frankly said to us that their underwriting

expenses are less, that quite a number of builders said that one of the aspects of their scheme that they were very happy with was that the fact that they publish builders' capital requirements and there were a couple of other advantages in the Queensland scheme that I thought we certainly miss: One of the particular advantages I would like to explore with you relates to what they call a category of claim which they say is termination of the contract, in which New South Wales is deficient, as is every other State deficient in that regard. So if the builder loses their licence or clearly engages in behaviour which has to be regarded as outrageous—that does happen from time to time—I do not know what happens to the consumer in New South Wales but in Queensland they are able to put a case to the insurer and make an insurance claim..

They say that they offer all of these benefits with a much less premium exposure and you have said that part of the reason is they are able to negotiate before September 11 but, notwithstanding that—with the exception of the six and a half years—the product that they offer in Queensland is similar to what is now available in the other States, the structural and non-structural defects are now part of the New South Wales and Victoria schemes. How rigorously was the Queensland scheme investigated as an option for New South Wales?

**Mr SCHMIDT:** Can I take up a couple of points in the lead up to my answer? First off, as far as the transparency financial criteria, as I said earlier, we agree, and the insurers here have agreed, that that must be made transparent. So hopefully it would be in accord with their approach. The cost of the underwriting—I would be interested to see what the cost of their underwriting would be if they had to renegotiate in the current market.

**The Hon. JOHN RYAN:** When you say you would be interested, I imagine you were the person in New South Wales who had the most responsibility for investigating all of the available options. If you are going to say "I would be interested to see" one imagines that you had not investigated the matter.

**Mr SCHMIDT:** No. The answer to that is obviously if their reinsurance came up for negotiation now they would sit down with their reinsurers who would have commercial discussions with them based on their experience. That is not the sort of information that the reinsurers are going to volunteer to us in New South Wales.

**The Hon. JOHN RYAN:** But the Queensland scheme would volunteer to you what it cost them for reinsurance and they were confident they were paying a great deal less. One of the reasons why they say they pay a great deal less is that they negotiate on behalf of the whole market, they do not have a series of front end sellers and other commissions which are involved in the New South Wales scheme where usually you go to an insurance broker who is selling it on behalf of Royal and Sun Alliance, who is selling it then on behalf of another underwriter; by the time you have all of these different agencies taking their cut they say that the cost of the product is much less because you are dealing with one player who writes the whole scheme and they additionally have the advantage, I suppose, that as the licensee of builders they are able to give certain guarantees as to the quality of the building work.

**Mr SCHMIDT:** Back to that point though about finding out the basis on which they have financially entered into arrangements with the reinsurers, I would suspect that they are constrained by commercial in-confidence just as we are about some of our financial dealings. The point is we are not comparing apples with apples when you compare the two schemes and it is not a government scheme where you cover 100 percent of the market. So the dynamics would be different. The point you were leading to was the determination cover?

**The Hon. JOHN RYAN:** Yes. One of the points is they have a termination cover. What is going to be the position of a consumer who has a long and lengthy dispute with a builder who winds up unlicensed, may have their assets hidden in all sorts of places which are going to be difficult to discover but they do not cease to exist; it might have been a lengthy dispute to get them to that point already. Why should there not be a position where because the insurer is usually in an infinitely better position to chase the builder than an individual consumer, we at least modify the scheme as it is currently written in New South Wales where there is a position under certain circumstances for the contract to be terminated either because of the misbehaviour of the builder or they become unlicensed,

they no longer satisfy the requirements in New South Wales to be a licensed builder. Why shouldn't that at least trigger an insurance claim?

**Mr SCHMIDT:** The parameters of the policies as issued in New South Wales are as has been set by the Government. That is the framework that we operate under.

**Mr AIRD:** Legislation currently provides that you are covered for termination of contract but it is a last resort scheme. So that cover will only apply where you cannot recover against the builder because of the death, disappearance or insolvency of the builder.

**The Hon. JOHN RYAN:** I would put to you that the group of people who have been the least consulted in this arrangement, that have made the most amount of sacrifices in this are consumers. Builders may ultimately get some advantage from the fact that their capital requirements will be published; there might be some competition—we will explore all those matters later in my questioning to you—but what the consumer in New South Wales has had to deal with is first of all the rate of $200,000, for example, as the cap of the largest claim, which was understood to be a starting point for the scheme for the future. There was an expectation that that amount would in fact be increased over time to deal with inflation. To give you one aspect of how that is going to have a significant impact: if a claim that runs over six years is made in the fifth or six year, clearly by the time inflation eats into the capacity for the consumer to make a claim, that alone might mean that the claim is negligible. It is a last resort scheme, so it covers legal costs. I can certainly take you and show you a few building sites where $200,000 would be a minuscule amount of the funds required.

Have you done any sort of estimation independently of insurers as to what the exposure to consumers is going to be for what I would call catastrophic claims? Normally when we review insurers in New South Wales we have tended to take the view that the group of people that we most need to look after are the top end of the scheme, the people who are going to be the most catastrophically affected. What we have done in this scheme is in fact reverse that around. The people who are catastrophically impacted are left high and dry, I put to you, under the scheme that is available now. If I find a major structural defect in my residential home in five years time after I have written insurance perhaps next year when there has been at least three percent inflation from where we are now—so we are talking about seven years inflation on $200,000 and I have spent $180,000 to build a house in the first place–I am going to be hundreds of thousands of dollars out of pocket by the time I finish chasing the builder and amassing legal expenses, aren't I?

**Mr SCHMIDT:** There are a number of issues that arise out of those observations. One of the interesting areas of feedback we have had as part of discussions in the context of these reforms and earlier, and having in mind too the number of claims which are greater than $200,000, you are talking about a small cohort—that is not minimising the suffering of those people—

**The Hon. JOHN RYAN:** Can I express one small irritation I have with the whole submission that you have made this morning, Mr. Schmidt? You have used qualitative terms like "the vast bulk", "approximately", and those sorts of things, but there has not been a single graph, table, chart, anything that tells us that we can have any confidence in those things. They are value assessments that you might have made with the knowledge of some facts but as yet in your written submission and in the submission that you have made so far orally, there is not a table or a chart or anything that we can rely on that would indicate those judgments are correct. Are we able to at least have some data that might justify some of those value judgments?

**Mr SCHMIDT:** I will come back to that in a second. The point I was going to make though was that in discussions in the context of the reforms, we have had representations from builders and even some consumers who are saying that for large projects—the ones which you are alluding to—"We do not see why we should be required to have insurance. We are big and bold enough ourselves at this end of the market to deal with a problem if it arises and we want to be able to build without having to have insurance in place". Now there are not many people who have said that but the point I am alluding to there is you have to draw a line somewhere in the provision of cover. You are correct in saying that the $200,000 is the minimum that is required to be provided cover. I am not sure what the expectation was but I anticipate the expectation at the time was that you would be able to get insurance for larger amounts for specific projects.

**The Hon. JOHN RYAN:** No, the understanding was when we introduced some reforms that you referred to earlier, the expectation given to me from Minister Watkins was that over a period of time $200,000 would be something which by regulation would be able to grow with the rate of inflation. We now have a scheme which looks like it is going to stick at $200,000 until such time as the insurers decide otherwise.

**Mr SCHMIDT:** One of the dynamics there is obviously trying to bring the schemes in harmony across Australia so that there is a uniform market. New South Wales has now been matched by Victoria, it has raised its level. But even under the old government scheme when I think there was a $100,000 limit, there were cases which fell outside the dollar value. If you raised it by inflation there would still be cases that fall outside the dollar value of the cover available.

**The Hon. JOHN RYAN:** That does not address my point. What proportion of consumers are going to be paying for an insurance policy which is going to be a minuscule proportion of the amount they insure for and what are we going to do for catastrophic claims? You know and I know that we could take you to Paul Vogel's place where they invited a builder in to do a renovation. After a very long tedious performance the home was left open, in fact it could be said that that was an incomplete building, so it might not even get the whole $200,000. So it was left open to the elements. The entire house—not just the bit that was renovated—the entire house was destroyed by the effluxion of time and weather. You are aware of the fact that there was an enormous amount of legal costs involved in just getting to where they were able to make a claim and in the end they were rescued by the fall of HIH because the Government took over and simply made out a $200,000 cheque. So that is what brought that one even to the point of having a claim made. Now you know and I know that $200,000 has not even come dangerously close to meeting Mr Vogel's losses.

**Mr SCHMIDT:** Through the Chair, I am in a difficult position here because I do not want to talk about an individual case. Mr Ryan is making very firm statements about the adequacy of payments made to a particular person. I would be uncomfortable in responding to that. I would like a bit of guidance here.

**The Hon. JOHN RYAN:** I will give you the guidance. You do not have to deal with Mr Vogel. It is perfectly obvious there are plenty of building claims that will be more than $200,000 and the losses incurred by the consumer will be catastrophic simply because, particularly with the last resort scheme, it is possible to half complete a building to the frame stage while the frame sits out in the elements and rots and in fact other building work becomes almost unusable over the affliction of time you are limited to 20 per cent. So in other words, what the consumer has already paid for might well have been built adequately but because they are limited to 20 per cent of the total costs, because what has been built has been left out in the elements and gets destroyed or vandalised, whatever, then clearly there are going to be a large number of people, because of the way the scheme is now structured, who are going to suffer catastrophic loss. Do we know how many of those people are involved and what are we proposing to do for them?

**Mr SMITH:** Certainly, Mr Ryan, I take your point that the closed BSC scheme had completion costs capped at $25,000 on a $100,000 maximum. So the same scenario existed in that scheme where people fell outside it.

**The Hon. JOHN RYAN:** The sins of the past do not justify continuing it into the future, just as the Dodd report made a number of recommendations and that was one of the things which the Dodd report said, that the amounts offered were inadequate. So it is not fair to simply say the scheme was bad therefore this represents something of a minor improvement. None of you have said to me yet, by virtue of whatever study you have done, how many catastrophic claims you estimate we are going to have that are going to be well outside the $200,000 amount of cover and what is going to happen to those people? That is a fair question to ask because previously although the scheme was not in place the scheme was expected to grow over time; there was an expectation of heavier regulation of insurers. So some of those things were going to be addressed. At the moment there is still the position that if I get two-thirds of the way through a building and it is not at lock-up stage, for example, a lot of what I have already paid for becomes ruined; I am going to have a lengthy and difficult legal process to recover those costs; I have got $200,000 in the pot and that $200,000 not only has to cover me for the costs of getting to that point but if I choose to complete the home and sell it to someone else they

effectively have no other insurance available on that home because I will have claimed the full amount already. So what are we doing for people who are in that position?

**Mr SCHMIDT:** There are a number of answers to that question. The practical answer is that the scheme as endorsed by the Government and negotiated at the moment has the $200,000 figure and that is the basis on which the insurers have said they are willing to provide cover. That is a statement of fact. The claims before the Building Conciliation Service, some figures I have from back at March this year—and unfortunately the breakdown I have here is the figures over $25,000, so it would be useful to have some feedback from the tribunal as to its experience—only 9 per cent of claims in that period were over $25,000. Those that were over $200,000, you will not be happy with the answer but I would assume it would be much less, but it would be interesting to ask the tribunal for the breakup.

**The Hon. JOHN RYAN:** You seem to be telling me that you had not done that study before we legislated?

**Mr SCHMIDT:** A number of factors had to be balanced in arriving at the scheme. The factors were harmonisation with other jurisdictions, in particular with Victoria, and a product that would be viable in the marketplace and would be provided by the insurers. There will always be matters that fall outside the scope of any determined scheme. The factors you are alluding to now are some of those factors. You can increase it by inflation or put in place some other arrangements but unless you have a system in place where the private insurance market is willing—which it is not—to have unlimited cover for individual residential building projects or the Government is willing to do the same, and at the moment the Government's policy parameters are not to do that, people will always fall outside the extremes. Having said that, I revert to my earlier comment that there are some builders and consumers at that higher level, because we are talking about the highest level of construction work, suffering that degree of loss who have indicated that they do not want to have insurance in place and have asked to be given the opportunity to opt out of the insurance arrangements.

**The Hon. JOHN RYAN:** They would be large contract corporations, corporate builders.

**Mr SCHMIDT:** No, I am talking about consumers as well.

**The Hon. JOHN RYAN:** I doubt it.

**CHAIR:** Before this matter gets lost, the Hon. John Ryan asked the question some time ago and it bore on the extent to which, if at all, the department has prepared or has available graphs or charts or similar material reflecting its experience under the existing legislation. I do not know what your answer is, but possibly the fact might be that the scheme has been on foot for a short period and you do not have the long history to demonstrate anyway. But, could I have your response regarding that matter?

**Mr SCHMIDT:** One of the biggest problems we have faced in this market in Australia, not only in New South Wales, has been the lack of hard data. There is no doubt about that. There are reporting requirements under the conditions of approval that insurers operate under. We have material that I think we have given to the other Committee and we can equally make available to this Committee, but I will be the first to say that when you look at that information the questions that have been asked in the past and the answers that have been given have not been particularly helpful, and this has been an issue for prospective insurers wanting to come into the market. Not only are there question marks over the scope of information that we have asked for in New South Wales. In Victoria I do not think they have reporting requirements, and the reporting requirements vary from State to State. It is very hard, if not impossible, to get a good statistical basis for analysing this market. I understand this was a problem that the Motor Accidents Authority had with third party insurance some years ago, and it implemented major reforms to the reporting requirements to get that statistical data and it has now been on foot because it has been going for a few years.

One of the things we have been working on, we have engaged Trowbridge Consulting to look at our reporting requirements, and they have prepared a draft format which is much more intensive and much more are data deep than we have asked for to date. We can certainly make that available and that is out for consultation at the moment. Yes, there have been great deficiencies in the data

available, and unfortunately with the changes to the scheme transfer of the data as far as its relevance from the old scheme to the new scheme, there are limitations on what that data can be used for.

**The Hon. JOHN RYAN:** Just to finish the point about data, I am not sure whether the information you provided to the quality of buildings committee is based on what the insurers have recently provided to you or whether it is based on what they previously provided to you under their old reporting requirements.

**Mr SCHMIDT:** The new reporting requirements have not come into force yet.

**The Hon. JOHN RYAN:** I know that, but there were some previous reporting requirements. Occasionally I used to ask the odd question to have them published, because apparently there was no requirement to have them published. To be fair, I think we should publish or you should make available to this Committee the previous figures that were supplied to you by the insurance industry and then perhaps the details they have given you of the new ones. I would be grateful if you would do that. I think there is likely to be a discrepancy between the two. That is a matter that should be published, that the insurers have not been telling you the truth or giving you inadequate information for the past five years or so, and have since come to you and said, "Sorry, the details we gave you were inadequate. It is a new scheme."

I can remember on a couple of occasions when I asked for data with regard to the scheme it looked on the face of it reasonably profitable. If you roughly multiplied the number of premiums by the average premium and took away the number of claims, it did not look too bad. Obviously they have done what I am not surprised occurred, one of the players has died, HIH, and everybody wants to blame them because they are no longer available to speak up for themselves. Some of that is true, some of their complaints with regard to HIH are legitimate, I accept, but nevertheless it is easy to blame the one player who is no longer able to speak for itself. I think is fair that Royal and Sun Alliance, previously trading as Homeowners Warranty should have the details that it gave to the Government before, so we are at able to clearly say, "This is what you were telling us was the state of the scheme prior to that; this is what you are telling us is the state of the scheme now." Are you able to give us both sets of data?

**Mr SCHMIDT:** There is a publicly available compilation of figures, which we have given in the past. Again, I do not think it is particularly helpful to answer some of the questions, as you know from your own experience, Mr Ryan. I have a concern about introducing on a public basis the reports they have previously given to the Government. They are commercial in confidence. This is no different from the experience of the Motor Accidents Authority. People are happy for compiled data to be made available but they do not want their own individual details. If we make it available on an in-camera basis for the Committee, I do not think it will necessarily answer the questions you are raising.

**The Hon. JOHN RYAN:** I remember putting on the parliamentary record, and you had no difficulty in answering the question then, the number of policies held by each individual insurer, the number of—

**Mr SCHMIDT:** That is in that table, yes. You can have that table.

**The Hon. JOHN RYAN:** I have been trying to look for the previous answers, and I am not sure whether I asked them as questions on notice or in estimates committees.

**Mr SCHMIDT:** We will give you that. There is a one-page document or a couple of pages which have that summary.

**The Hon. JOHN RYAN:** As I say, it is true that the insurers say it is all changed? Recently the insurers basically said to the Government that the situation is far more catastrophic than we were led to believe. A Committee like this would not be doing its job if it did not publish both sets of data—this is what they said it was; this is what they say it is now. So, can you give us both?

**CHAIR:** Is it possible to give us data that does not breach the commercial in confidence criteria?

**Mr SCHMIDT:** We will give you the information we have in that format and we will see what your response is to that information, but to pick up Mr Ryan's point, the data we have asked for did not go to profitability, so it will not enable you to draw that conclusion.

**The Hon. JOHN RYAN:** No, it will not, but it will become apparent that they were not reporting the level of claims that they are reporting in submissions to this Committee, for example.

**CHAIR:** May I clarify one matter. The Hon. John Ryan in his recent question refers to HIH and suggested that there is perhaps a tendency to put the blame in their basket, namely HIH's. I did ask you a question before about the insurers and I have formed the impression that HIH was a dominant player in the then market. Are you able to quantify that in percentage terms?

**Ms BAKER:** I think we used to talk about HIH being about 60 per cent of the market.

**The Hon. JOHN RYAN:** I must say, I do not recall that.

**Mr SCHMIDT:** It was 60 per cent of Newcastle and 40 per cent in the rest of New South Wales.

**Mr SMITH:** I think it was 60:40 statewide.

**The Hon. JOHN RYAN:** The most common was HIW, not HIH. I do not think it would reach even 40 per cent, myself. I thought it was much more in the order of about 20 per cent. I would be happy to see the figures.

**CHAIR:** It was a large player, then?

**Mr SCHMIDT:** Yes, absolutely.

**The Hon. JOHN RYAN:** Dominant might be overstating it?

**Mr SCHMIDT:** The influence of them in undercutting and lowering financial standards, there is a legacy that is still being felt today.

**The Hon. JOHN RYAN:** That is an allegation that current insurers make. I do not know to what extent that has been vindicated. If you are able to vindicate that, I would be interested, but that is the allegation they make.

**Mr SCHMIDT:** I will try to add some more information. It is important know that that issue has been raised. The Master Builders Association had a relationship with HIH, just as the Housing Industry Association has a relationship with the Royal and Sun Alliance group. Even when HIH was on foot, towards the end of its existence we started getting representations from the Master Builders Association, complaining that HIH was changing its approach and raising its financial assessments and getting tougher on builders. There certainly was a perception, even amongst the building industry itself, that HIH was a softer touch, as it were. It was easier to get insurance, its criteria were much less stringent than the other insurers.

**The Hon. JOHN RYAN:** If I may go back to the point we were making before we took a diversion, what estimation have you made of how much of the market is not going to be covered by the $200,000 limit on claims? I would have thought that the negotiations or discussions you had with insurers and the meetings that happened in Victoria you would have done some homework to make sure that you were at least on a level basis to be able to say, "These are your problems, but these are ours." One of the problems you would have researched is when you set a limit of $200,000, this is the amount of the market that will not be covered.

**Mr SCHMIDT:** The answer to that is very simple. When we went to negotiate with the insurers the issue of changing our level was not something that we were looking at. We were proceeding on the basis of maintaining the $200,000, and nothing eventuated to change that perception. Therefore, we did not do an analysis along the lines you have outlined, because we had no intentions in those negotiations, in those discussions, of changing that limit.

**The Hon. JOHN RYAN:** So you have come back and they made an offer—particularly, one of the most important ones was the limit of 20 per cent for incomplete work. What calculations have you made as to whether that will cover the market or not?

**Mr SCHMIDT:** We had the experience of Victorians, who we were negotiating with, and the operation of the scheme down there. We also had the experience of the old government scheme. Under the old government scheme there was a cap as well. Completion under that was limited not to a percentage but to a dollar value. I think the dollar value was $25,000, so it was far tougher. The completion cap at the moment is up to $200,000 if it is 20 per cent of the cost of the contract. I do not have figures that give you a breakdown of what scale of claims are paid based on those figures, et cetera.

**The Hon. JOHN RYAN:** Is that because you do not have them here or they have not been calculated?

**Mr SCHMIDT:** No, we were basing those discussions on harmonisation and the experience of the government scheme, but I do not have data that does a detailed analysis of that. I know one of the arguments is to what extent actuarial work was done with some of these reforms, and you must remember that these negotiations took place in an environment where the scheme was on the verge of collapse. It involved the highest levels government in two jurisdictions and the major insurers. We were trying to find a broad framework in which a scheme could continue to operate and a product be made available. Part of the intention, as I outlined earlier, was to maintain the market for all those concerned with those changed parameters and give us time to do more assessments over time. This is one of the reasons why this new reporting requirement has been introduced. I suspect on some of the issues that people now, with hindsight, might like to have had more time and opportunity to delve into there would not be the statistical basis to form those conclusions anyway.

**The Hon. JOHN RYAN:** Again I ask has it been calculated as to what amount of the market is not going to be covered by the $200,000 cap?

**Mr SCHMIDT:** No.

**CHAIR:** You did indicate in response to earlier questioning, if I recall correctly, that the incidence of higher-level claims under dispute appear to be fairly low?

**Mr SCHMIDT:** Yes. The difficulty you face in trying to find that from insurers is that they have the limit of policy, so people would only be claiming up to the $200,000 under their scheme. The data source you might go to for that and which would be reliable in New South Wales would be the tribunal. They do keep figures, as I understand it, and we have some figures. Unfortunately, the cut of figures I have here breaks into four segments from less than $5,000 to the highest category of being over $25,000, and the figures before the Building Conciliation Service at the end of March were showing that only 9 per cent of matters were over $25,000. They may be able, through their database, to do a much more refined split for amounts moving up. I do not have those figures.

**The Hon. JOHN RYAN:** But that is only for amounts now as they are claimed. It takes no account, for example, of the ravages of inflation or what might happen over the length of the dispute. It does not take into account legal costs, does it? They are added on at the end, are they not?

**Mr SCHMIDT:** Unless you have a scheme that has an open-ended cheque, as it were, no upper limit, there will always be those catastrophic claims that go over any limit you set.

**The Hon. JOHN RYAN:** Yes, that is understood. One of the reasonable assessments to make of any scheme is how many will go over that.

**Mr SCHMIDT:** The discussions that took place at that time were not to change the New South Wales limit.

**The Hon. JOHN RYAN:** And it is not unreasonable that an agency like the Department of Fair Trading should have some idea as to how many of the consumers its represents will be uncovered by the value of the scheme. I appear to be the only person in the world who has asked the question.

**Mr SCHMIDT:** Part of the basis for our engaging an appropriate firm to develop detailed reporting requirements was to get that sort of data for the future. We admit that there are limitations, and insurers are suffering exactly the same problem. There is a paucity of good, hard data that can be analysed on a statistical basis in this area of the market. For example, APRA keeps detailed statistics, but home warranty insurance is a small component of the overall insurance market, and it does not keep detailed statistics. One of the things that we will do is try to get it to get more involved in requiring reports from insurers. Unfortunately, there is a paucity of hard data.

**The Hon. JOHN RYAN:** With regard to the reporting requirements of insurers, I remember when we put through the previous amendments to the Home Building Act I was told that arrangements were in hand to increase the level of reporting by insurers. What is the current level of reporting by insurers under the current scheme? Exactly when can we expect to see it change?

**Mr SCHMIDT:** You are absolutely right. Part of the reforms that were put in that legislation last year were to mirror some of the reporting requirements or the administrative arrangements that the Motor Accidents Authority uses, and those provisions were taken from that legislation. They have not yet commenced because we are developing the reporting framework. The development of the framework has been delayed by some of the other upheavals in the market. Earlier in the year we did not know whether we were going to have a market. We have not stopped work on those, but they have been delayed. We are hoping to get those in place as soon as possible.

**The Hon. JOHN RYAN:** What does "as soon as possible" mean?

**Mr SCHMIDT:** It is a matter for the Minister and the Government to determine when those provisions will commence. We are doing the work now to enable that to happen.

**The Hon. JOHN RYAN:** Has that been part of your negotiations with the insurance industry, that they would expect and will agree to that?

**Mr SCHMIDT:** Yes. The insurers would welcome hard statistical data. You must remember too, that it is not just the insurers. As I said at the outset, one of the difficulties in this market is that you have the insurers at the front end and you have this raft of changing reinsurers in the background. One of the difficulties the insurers have faced is that when they have gone offshore to renegotiate or try to get a new insurer to the market or the table they have said the same things that you are asking now: Where is the hard statistical data to enable us to make a decision about the viability of the scheme?

**The Hon. JOHN RYAN:** What are we able to offer people who will be catastrophically affected by the failure of a home builder? What if you decided to cancel the licence of a home builder? What assistance are you able to offer the consumer in chasing the builder, given that this is now a last resort scheme? Previously, at least you could go to the insurer and say, "I have lost my builder" and the insurer would pay out. What assistance will the Department of Fair Trading be able to give consumers when you have cancelled the licence of their builder, which means that the builder cannot go back and complete the work? It might take ages to discover where his assets are. The house will continue open. The consumers will be unable to move into it. The dispute will continue at length. Are you planning to offer any assistance to consumers who are caught like that?

**Mr AIRD:** One of the reforms passed last year was to allow the director-general to make orders for completion of works in this situation. The intention is that where a project builder might be disqualified from holding a licence the department can enter into discussions with the insurer. Our main concern is the other customers of the builder. The director-general has the capacity to appoint a person to supervise that work, which could also include the builders themselves under the supervision of the department or the insurer. The legislation provides some flexibility to cover that situation.

**CHAIR:** I take it that such an event has not happened?

**Mr AIRD:** No, we have not had a situation like that yet.

**The Hon. JOHN RYAN:** It happens all the time! Homeowners do not want the builder to come back to their home because of the outrageous way in which the builder has behaved. Truckloads of constituents have complained to me that they do not want the builder back.

**CHAIR:** My reference is to the underlying principle of the builder's licence being taken away by the department.

**Mr AIRD:** The situation I was talking about is where a builder's licence might be cancelled because of conduct in respect of one or two jobs, but the builder might have 10 other jobs going and those customers may not be dissatisfied with the builder. Our concerns would be to ensure that all the work can be completed.

**The Hon. JOHN RYAN:** What about the customer who is dissatisfied with the builder?

**Mr AIRD:** Obviously, there is a process for that, such as making a claim.

**Mr SCHMIDT:** It is an interesting point you raised. When disputes arise between builders and consumers, right is not always on one side. Certainly, there are occasions when there is a breakdown in relationship between the builder and the consumer, and the builder is willing and able to go back on site and fix the job but the consumer, for whatever reason, does not want that. We are not really the people to make that judgment, that that arrangement should not continue on the contractual basis. That is why we have the Building Conciliation Service and the tribunal. At that point that is a civil dispute between parties. Sure, it is a building dispute but it is in the same nature as many other civil disputes where a similar issue arises between a consumer and service provider.

**The Hon. JOHN RYAN:** Not quite. If I have a renovation going on in my home that has already taken 18 months to complete, and I had an obnoxious builder who was not prepared to complete a home, I have to continue to allow that person access to my family home. That is not quite the same as buying a motor car or those sorts of things. There are legitimate circumstances where removing the builder from the site is a perfectly reasonable thing to do.

**Mr SCHMIDT:** One of the orders available to the tribunal in those circumstances, quite reasonably, is that a third party builder be engaged to complete the work at the expense of the original builder.

**CHAIR:** Is there still a statutory power to remove a licence from an unsatisfactory builder who has demonstrated non-compliance over a substantial period?

**Mr SCHMIDT:** Yes, and that was one of the major raft of the reforms last year, again which the insurers were calling for as well.

**The Hon. JOHN RYAN:** It might be reasonable for the CTTT to do that, but at the moment there is no legal basis to do it. The CTTT cannot take into consideration that the builder's behaviour has been outrageous. Sometimes it tends to make money orders. I understand that the CTTT is waiting for us to create new regulations in the Home Building Act to set out situations in which it would be reasonable to say that the builder should not come onto the premises any more, and the circumstances in which it would be appropriate to terminate the building contract.

**Mr SCHMIDT:** I think that they are slightly different things. The issue you were talking about lastly was trying to clarify for the purposes of the insurance policy when it would be reasonable or unreasonable for the consumer to refuse the builder back on site. Let us put that aside and go back to the dispute in the tribunal. I am a bit cautious because I am not in the tribunal, but I believe it has very broad order-making powers and I believe one of the powers it would have is that arrangements be put in place to engage another builder to complete the work.

**The Hon. JOHN RYAN:** When we asked Ms Chopping about the same thing on the other Committee, she said, "We just make money orders." Sometimes, money orders are hopelessly inadequate to get another builder. Previously, because the insurance scheme was first resort, it was

necessary to decide when it was appropriate to terminate the contract. For exactly this reason, in Queensland there are numerous occasions when consumers are in the position of falling between, what they describe as, two stools. There was an opportunity for the Queensland insurer to say, "This has gone on far enough. We are paying the claim and we are chasing the builder." Unfortunately, that is not available in New South Wales. I am trying to explore ways and means of ensuring that we do not have the category of consumers who will, clearly, fall between two stools. Apparently, we will leave them to fight through a very expensive procedure in the local courts, the CTTT and, possibly, the Supreme Court. I wonder whether there is not some means to provide for a reasonable termination of the contract that might well trigger an insurance claim, one that insurers, themselves, might be willing to enter into if they were asked. Surely an area of harmonising insurance schemes would be to create something in New South Wales that was analogous to the scheme Queensland.

**Mr SCHMIDT:** My personal hope is that when the Percy Allen report is delivered it will have support. My knowledge, from the reception he has received to date from States and Territories and the difficulties that have been experienced, is that there will be a will to introduce harmonisation in the scheme across the board. The very point you made is one that could be addressed as part of that. Absolutely, as part of harmonisation and trying to find a national framework that tries to cover all the gaps that factor should be looked at.

**CHAIR:** It is not beyond the realms of possibility that Queensland could be part of the harmonisation to which you refer?

**Mr SCHMIDT:** Queensland has a service-delivery mechanism through a government corporation, but the product does not have to be wildly different. Other jurisdictions could pick up the Queensland model. For example, they might pick up cover of high rise. It does not matter how you deliver it as far as that is concerned—be it a government scheme or a private scheme, the product is determined by the Government in each jurisdiction.

**The Hon. JOHN RYAN:** I sincerely hope that the Department of Fair Trading in New South Wales might advocate for the harmonisation of a scheme that benefits consumers. To date very few things in this package look like they improve the lot of consumers. With regard to premiums, there has been virtually no movement. You have said there might be some movement within two years. Given that we now have a scheme that is pretty much the same as South Australia, why should not the premiums very quickly become similar?

**Mr SCHMIDT:** That is an interesting question, and one, I am sure, that you will raise with the insurers when they appear.

**The Hon. JOHN RYAN:** I certainly will. But as advocates and regulators of insurers, why would you not ask it?

**Mr SCHMIDT:** Bear in mind that when people talk about premiums and compare them from jurisdiction to jurisdiction they have to look at other factors. For example, the Royal and Sun premiums structure is a five-tier one. They look at builders and they slot them, based on their risk criteria, into five categories. You could be a category one builder and have a very low premium. You could be a category five, an extreme-risk builder, and your premium could be five or six times higher than a category one. If you average out the premiums and compare them from jurisdiction to jurisdiction you will get significant disparities. If you look at the individual best risk builders, the biggest turnover builders with the best assets, there is a difference but the disparity may not be as great. In the middle of last year Queensland had to bring its premiums up to the New South Wales level before all these other shocks and things worked their way through the system.

Premiums have changed from jurisdiction to jurisdiction under very different factors, but there is a wide scale of premiums available to builders in New South Wales depending on which insurer they are with and the risk profile they satisfy. One of the other factors that does not always come through is that, for example, the Dexta-Allianz product has an arrangement with builders so that they can limit their exposure. That does not seem to get much airing. They have a subrogation limit policy where, for an extra premium, a builder can be exposed to a maximum of $50,000 in respect of a particular job. Even within the framework of the product, builders can pay different premiums to get a different degree of cover, but the consumer still get the $200,000, under the policy itself.

**The Hon. JOHN RYAN:** What happens if the builder is not able to pay the full amount?

**Mr SCHMIDT:** The insurer pays.

**Ms BAKER:** The insurer picks it up.

**The Hon. JOHN RYAN:** Any way?

**Mr SCHMIDT:** Yes.

**Ms BAKER:** It is consumer protected.

**Mr SCHMIDT:** I do not know what the right terminology would be.

**Mr AIRD:** Subrogation limit.

**The Hon. JOHN RYAN:** You have said, "We believe that insurers will disclose requirements on builders and they have given various undertaking." Could we have that a little bit firmer than "we believe" and "various undertakings"? What undertakings have been given, and in what timeframe will they be able to deliver them?

**Ms BAKER:** I know you will say that this is non-specific, but I understand that the agent for Royal and Sun, HIA Insurance Services which is one of the significant providers, is only weeks away from issuing an interactive builder kit that we understand to be a bit like a mortgage ready reckoner that banks use into which you can plug your details. If you are builder you can plug in your capitalisation and have some idea of what your premiums are likely to be. They say they are within weeks of launching that. Royal and Son now has two providers, HIAIS, and this new shopfront that involves 50 or so brokers. They also have just started up and intend to make clear their eligibility requirements.

It is fair to say that Dexta has been somewhat diverted by other issues recently, but we have had a commitment fromtheir managing director. I spoke to one of their senior managers as recently as last week. They have given a clear commitment that they will make their requirements transparent. They understand fully that this is something that we, as a government, expect of them. At the moment we are a significant underwriter or reinsurer of their product. That leverage seems to be having some impact on their response to that issue.

**The Hon. JOHN RYAN:** I will read part of the submission from the Master Builders Association. With regard to the business of "other insurers" it states:

> At a home warranty meeting organised by the Leader of the Opposition and the shadow Minister for Fair Trading on 16 April 2002, representatives of Royal and Sun Alliance told the meeting that the passing of the reform package was likely to have the immediate affect of attracting reinsurers into the market. It was implied that insurers are —

and I remember this expression being used—

> waiting in the wings to enter the market as soon as the reforms have been passed.

I do not know whether that same rhetoric was used by Royal and Sun Alliance when it was dealing with the Government or whether it was used at any of the other meetings that you have had. Were you given any assurance that insurers were waiting in the wings to come into the market or just waiting for reforms to be passed? Are insurers waiting in the wings? When are we likely to see additional insurers enter the market?

**Mr SCHMIDT:** It was not put as strongly as "insurers waiting in the wings". In regard to your question about who is interested at the moment, we know—and it has been publicly stated—that the NRMA is seriously looking at the market. Not only reinsurers were thinking of withdrawing from the market completely. Royal and Sun Alliance made it very plain that it would stay in the market until the end of this calendar year and it would then have left if the reforms had not gone through.

Now that the reforms have gone through it is expanding that network, as Ms Baker just outlined, with the second tier of brokers through which it is providing cover.

We keep hearing comments from people like the Master Builders Association that they are out there themselves. They have approached government and they are going to be given some funding to try to do some work to further develop an industry-based scheme. They have engaged off-shore people to make inquiries in North America to try to find insurance partners. As I understand it, they are still doing that. They have not given up on that score. So there are people out there talking. The trouble is, to be quite blunt about it, other than the NRMA, there are not people flagging in the street that they are seriously thinking of entering the market.

**The Hon. JOHN RYAN:** One of the other things that the new scheme introduced was the difference between structural defect and non-structural defect. With the exception of what is outlined in section 57AC of the new Home Building (Insurance) Amendment Act, what arrangements are in place to decide what will fall into the categories of structural and non-structural defects?

**Mr SCHMIDT:** That is a matter of interpretation. At the moment, putting structural defects aside, the legislation draws a distinction between residential work and non-residential work that has to be covered by the policy. Occasionally disputes will arise as to whether a particular project—

**The Hon. JOHN RYAN:** Occasionally? I think they will occur fairly frequently.

**Mr SCHMIDT:** There was a distinction between structural and non-structural under the old government scheme. There is to this day in Queensland. So I am not denying that there will be occasions when people argue the toss, but it is a matter of definition in the circumstances of an individual contract.

**The Hon. JOHN RYAN:** With the exception of what is in the Act, who will make the decision as to what falls inside or outside those categories?

**Mr SCHMIDT:** Obviously it is a term of the contract. It is a matter of insurance. If a dispute arises the appropriate place to determine that would be the CTTT or a court. The Government is not out there as some massive arbiter who comes in over the top of a consumer, builder or insurer and says, "In our wisdom this is where the line should be drawn."

**The Hon. JOHN RYAN:** If you are a consumer who had something on the edge you would have an expensive dispute. It should be remembered that there is a $200,000 limit on litigation. Why would the Government not be trying to get insurers to define in some sorts of terms what will be structural and what will be non-structural?

**CHAIR:** Before you respond to that, I state for the record that section 57AC of the legislation appears to contain an extended definition of the meaning of "structural defect". It is in four or five parts. So I suppose, as with any statute, it is a matter of administration and interpretation as to what the statutory definition means in practical terms.

**Mr SCHMIDT:** This is an outcomes-based definition, so you apply it to the circumstances and draw a conclusion as to how it operates in a particular set of circumstances. What is the alternative? The alternative might be to try to draft some comprehensive list of every factual circumstance. First, it would be enormous and, second, despite your best endeavours, there would always be cases, no matter where you ended your list, where there is a dispute or grey area about a particular circumstance.

**The Hon. JOHN RYAN:** Surely it would be helpful for industry generally, given that we are trying to provide a quick dispute resolution service? It is not impossible to have a reasonably extensive list that includes issues such as the slab, the framework, windows and so on. A statement of tolerances exists in Victoria. It is not a comprehensive list, but at least it gives people going into a dispute some idea about where they will come out. People might want to challenge things outside that area. If we are to be reasonable surely the insurance industry and the Government should make an effort to try to define these things in lay terms so that consumers know whether it is worthwhile going to the CTTT to pursue claims relating to whether a window leaks, whether a front door needs to be

replaced or whether steps have been provided by a builder to make a building accessible by a wheelchair.

Those claims might fall into the category of something that is likely to result in a building or part of a building not being able to be used. In my view there should at least be some industry standards. I would be stunned if the insurance industry was not prepared to be at least co-operative in providing some sort of list that consumers could understand. Clearly, there is miles of room for litigation.

**Ms BAKER:** You referred earlier to the Victorian booklet on standards and tolerances. At a meeting of consumers, builders and insurers just two weeks ago, that came up as a major issue for all groups. New South Wales agreed to get hold of it, have a look at it and determine whether it will be useful for us. But all groups were interested in a document like that. We will make every attempt to introduce something like that in New South Wales.

**CHAIR:** I am somewhat troubled about the matter to which the Hon. John Ryan was referring. Let us suppose, for argument's sake, that someone has a leaking window. It seems to me that in the statutory definitions it would be a matter of fact, in a given situation, whether or not it falls within the definition of a structural defect. For example, an element of the definition is "prevents or is likely to prevent the continued practical use of a building or any part of the building". Whether a leaking window, to give that example, has that outcome, I suppose depends on where the window is—whether it is an upper floor window or a lower floor window—and what room it is in.

**The Hon. JOHN RYAN:** And whether or not it is leaking three years after the house is built. I accept that in other areas of law it would be reasonable to allow the courts to sort these things out. But it should be remembered that everybody is limited to $200,000. A lot of claims have been put in by insurers. It is not unreasonable to have some guidance for consumers. I know dozens of consumers who have gone to the Fair Trading Tribunal with legitimate expectations of what they might come out with. They discovered, only through extensive litigation, that the statutory warranties provided in the Home Building Act do not cover their complaints.

The tribunal subsequently discovers that they are cosmetic problems, not something which affects the proper use of the home. Sometimes they end up with an award for damages, but not sufficient to defeat the legal costs of the building. It will be necessary for the insurance industry to provide some sort of guidance to consumers and builders. Ultimately the insurance industry will be pretty much the arbiter of these sorts of things. There should be some sort of industry standard as to what is reasonable before litigation is commenced.

**Mr SCHMIDT:** Ms Baker has already referred to the fact that agreement has been reached in relation to tolerances. I have no doubt that the issue could be included in those discussions. We will see what we can come up with.

**The Hon. JOHN RYAN:** I think that the meeting to which you referred is called a roundtable. What was the purpose of that meeting? Who attended it? What do you expect to be the outcome of that meeting?

**Ms BAKER:** The purpose of the meeting was to have all three major groups involved in the home building system in New South Wales—that is, builders, insurers and consumers—meet together and try to work through and identify further issues for reform. Really, it was a brainstorming exercise, if you like. The Minister might then consider those further issues in the home building area. In other words, whilst we implemented home building reforms in 2001, we implemented some insurance reforms earlier this year. We have not really stopped. We are aware that people are raising other issues with us. We usually hear insurers' concerns individually from them. We hear consumers' concerns when we meet with consumers, and we hear builders' concerns.

So it was decided that the three groups would meet together to identify further areas for reform. In relation to the outcomes, no document has yet been issued, but there were a series of ideas for further consideration and implementation. They ranged across all areas. They proved, I guess, that the system always needs to be looked at as a whole because the issues that people raised with us were about licensing, dispute resolution, insurance, contracts, standard of work and other agencies such as

planning and re-certification. We have actually logged all those ideas and we will be thinking about how to proceed with them. The Minister, as a result of the roundtable, has established a smaller consultative group with consumer representatives, builder representatives and insurer representatives, to advise him on the future implementation of those ideas.

**The Hon. JOHN RYAN:** What issues were discussed with regard to insurance that might be relevant to this Committee's deliberations?

**Ms BAKER:** Very few issues were raised about insurance. The ones that were raised I think we have already addressed this morning. The primary issues for insurance were transparency of criteria for builders and delays in processing. I did not bring those documents with me. There were only two or three insurance issues.

**The Hon. JOHN RYAN:** Did consumers raise the issues that they wanted you to deal with?

**Ms BAKER:** From my recollection, not with regard to insurance.

**The Hon. JOHN RYAN:** If they did, it would be useful for the Committee to know what was in the pipeline. Are there any further opportunities to refine the scheme? Given that it has been said that most of the arrangements that were made were done under emergency circumstances, will there be additional opportunities to refine the scheme? If so, when and how?

**Mr SCHMIDT:** As you would be aware, it seems that in almost every session a home building amendment bill is introduced. I have already referred to the work of Professor Allen. I hope that that will be a major catalyst for ongoing reform, regardless of what happens at a national level. It is very clear that the Government will continue to examine the operation of this scheme to see whether it can be further improved and enhanced. So the work has not stopped at all.

**The Hon. JOHN RYAN:** Notwithstanding your belief that the reforms that were passed through the House last year improved licensing, the insurance industry believes that there is a need for speed and more rigour with regard to the licensing issue. For example, New South Wales had the highest non-completions. The insurance industry believed that that was, in part, first resort.

It also said that there were other components involved in New South Wales litigation. The Royal and Sun Alliance submission lists lower standards of work as discussed in the Allen review and poorer quality control mechanisms—it particularly highlights inspections with regard to New South Wales but I am not exactly sure what it means by that. Have you identified any areas where the licensing scheme, the inspection scheme and your resources will be available? Clearly strong, rigorous enforcement by the Department of Fair Trading will be absolutely vital to ensuring that builders take proper responsibility.

**Mr SCHMIDT:** There has been extensive discussion about this area in the Joint Select Committee on the Quality of Buildings. The tenor of those discussions was that the reforms introduced last year have commenced on a rolling basis—the disciplinary processes and so on. Consideration is always given to whether we need to enhance them further. That is always an option. Certainly it is now putting in place, implementing and using those powers and I think some information was tabled to that Committee about prosecutions and so on. Those figures give an indication of how the powers can be used—regardless of whether these reforms have taken place.

Let us put this in a philosophical context. The philosophy of governments across Australia and throughout the Western world has changed in the past five to 10 years from the approach some years ago when it was felt that, if more information were given to consumers and traders, they would be able to balance their rights and determine their own courses of action. I think that attitude may be changing. It has become apparent and accepted on all sides of government that a strong regulatory regime underpins something like the home building industry. These reforms were put in place partly to ensure that the Government has a full raft of powers available to it, and it will revisit those powers if it feels that it needs to build upon them.

**The Hon. JOHN RYAN:** I think additional resources will be necessary. Previously the insurance industry did something to make builders return and look at their work. If consumers cannot

make builders go back and negotiate, the only place they can go is the CTTT—which does not have many more resources now than it used to. Some intervention will be necessary. People will complain to you that they have asked a builder to come back but there is no-one now to compel the builder to come back other than the CTTT, which will need at least the resources that replace that aspect of the scheme. Is there something in place to ensure that that will happen?

**Mr SCHMIDT:** The resources were enhanced. Part of last year's reforms was the 10 per cent levy on licence fees, which kicked in on 1 January. Part of that money is earmarked for the CTTT so that we can fund the building conciliation service to engage the independent mediators and experts to go on site and sort things out. To address your last point about how to get builders to do the work that they are ordered to do, the licensing regime has been linked with the tribunal order regime. If an order is not complied with and licensees wants to keep their licence, the department has the capacity to tell the licensees that, if they do not do the right thing and satisfy an order made by an independent judicial body, there will be a question mark over why they should keep their licence. As part of those reforms that area was given additional resources and placed in the compliance area of the department where they not only have access to the existing investigators with building backgrounds but the entire compliance area, if necessary, can be brought in for sweeps and other programs if intensive work is required in a particular area. Measures have been taken to try to raise the capacity to deal with those things.

**The Hon. JOHN RYAN:** One area of compliance raised in some of the submissions is that some builders have said that in some parts of New South Wales—particularly rural New South Wales—there is a black market operating in which people are doing building work without insurance. We have found from other inquiries that the most likely outcome for a builder who does not have a certificate of insurance attached to the contract of his insurance is that he will get a warning letter from the Department of Fair Trading. That would almost suggest that the builder is allowed the first offence penalty free. That would if not encourage then not discourage a black market from operating. What sort of rigour will you use to ensure that builders seek and get insurance? If a black market is operating—as builders have stated to this Committee—what are you doing to ensure that it does not continue?

**Mr SCHMIDT:** There are a couple of issues involved. First, even under the regime prior to 1 July some consumers would enter into arrangements with builders who did not have insurance—that is not to exonerate the builders in any way, shape or form. One of last year's reforms was to bring the disciplinary process in house because, as we outlined previously, the difficulty was that discipline had to go through the tribunal. It was an incredibly judicial process and it could take years to resolve a particular matter. It was not a good use of resources and was not very efficient and effective. I am not from the compliance area and thus not in a position to talk about the details of how we are implementing those powers in relation to uninsured work. However, that matter was canvassed previously and we can certainly answer further questions about it.

**Ms BAKER:** In respect of compliance activities, we have commenced a series of regional blitzes on unlicensed work. We issued 49 penalty notices during a recent blitz. We visit building sites and identify anyone who is working unlicensed. We have started a series of regional blitzes involving those sorts of aspects.

**Mr SCHMIDT:** Thank you for inviting us to appear before the Committee today. I will table a folder containing information that gives some background of the history of the scheme and inquiries.

**Document tabled.**

**CHAIR:** Thank you for your submission and for submitting to our interrogation this morning. It is ordered that the transcript of today's hearing and the tabled material be published.

**(The Committee adjourned at 12.06 p.m.)**