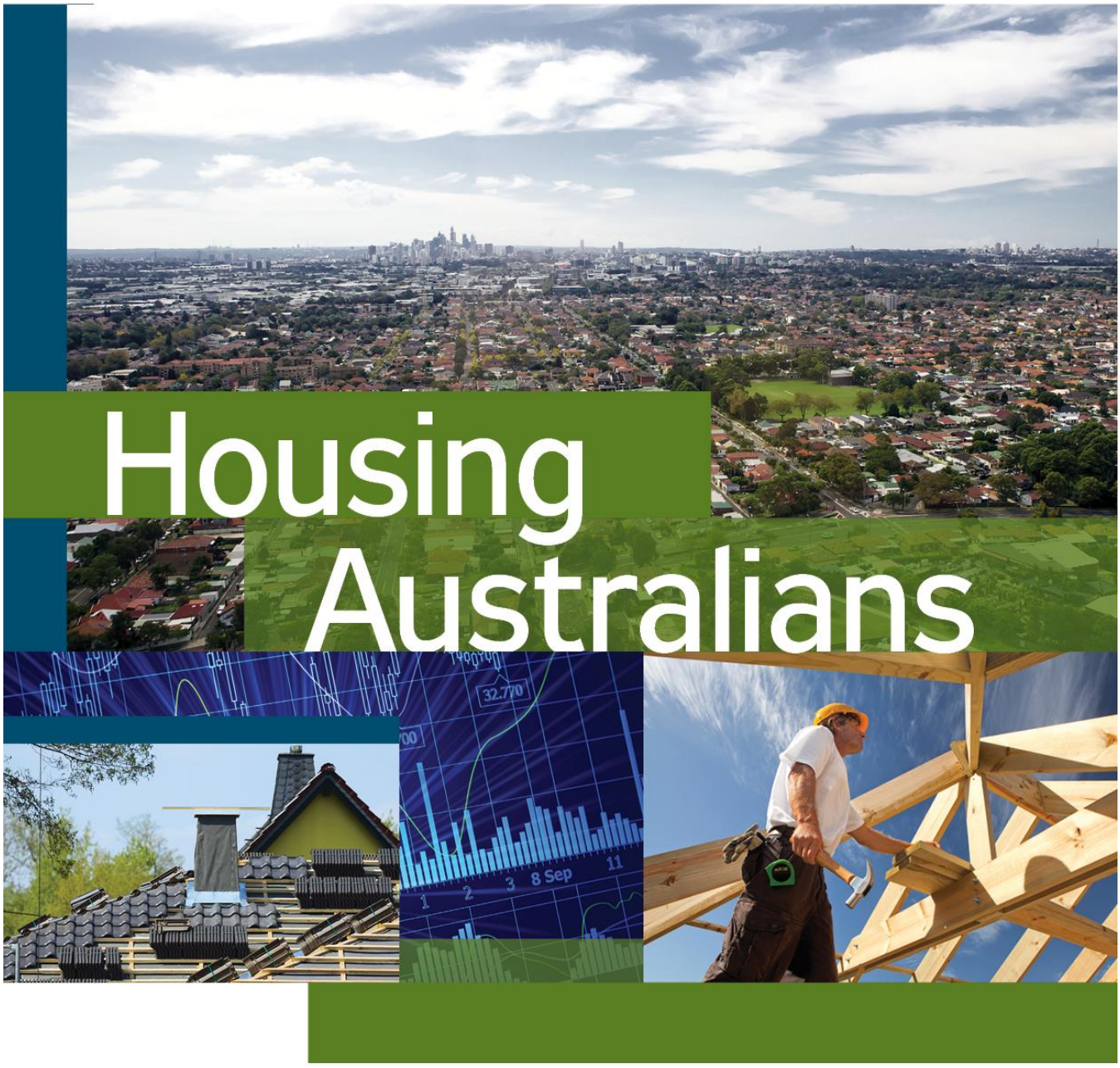
HOUSING INDUSTRY ASSOCIATION

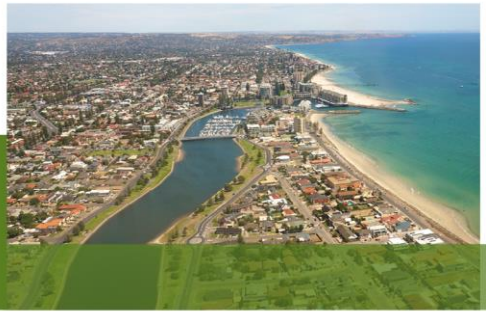


Submission to the
IPART

Review of the Efficiency and Effectiveness of the NSW Home Building Compensation Fund

16 October 2020

HOUSING INDUSTRY ASSOCIATION



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Housing Industry Association contacts:

David Bare
Executive Director - NSW
Housing Industry Association
4 Byfield St,
NORTH RYDE
Phone: 02 9978 3333
Email: d.bare@hia.com.au

ABOUT THE HOUSING INDUSTRY ASSOCIATION

The Housing Industry Association (HIA) is Australia's only national industry association representing the interests of the residential building industry.

As the voice of the residential building industry, HIA represents a membership of 60,000 across Australia. Our members are involved in delivering more than 170,000 new homes each year through the construction of new housing estates, detached homes, low & medium-density housing developments, apartment buildings and completing renovations on Australia's 9 million existing homes.

HIA members comprise a diverse mix of companies, including volume builders delivering thousands of new homes a year through to small and medium home builders delivering one or more custom built homes a year. From sole traders to multi-nationals, HIA members construct over 85 per cent of the nation's new building stock.

The residential building industry is one of Australia's most dynamic, innovative and efficient service industries and is a key driver of the Australian economy. The residential building industry has a wide reach into the manufacturing, supply and retail sectors.

Contributing over $100 billion per annum and accounting for 5.8 per cent of Gross Domestic Product, the residential building industry employs over one million people, representing tens of thousands of small businesses and over 200,000 sub-contractors reliant on the industry for their livelihood.

HIA exists to service the businesses it represents, lobby for the best possible business environment for the building industry and to encourage a responsible and quality driven, affordable residential building development industry. HIA's mission is to:

> *"promote policies and provide services which enhance our members' business practices, products and profitability, consistent with the highest standards of professional and commercial conduct."*

HIA develops and advocates policy on behalf of members to further advance new home building and renovating, enabling members to provide affordable and appropriate housing to the growing Australian population. New policy is generated through a grassroots process that starts with local and regional committees before progressing to the National Policy Congress by which time it has passed through almost 1,000 sets of hands.

Policy development is supported by an ongoing process of collecting and analysing data, forecasting, and providing industry data and insights for members, the general public and on a contract basis.

The association operates offices in 22 centres around the nation providing a wide range of advocacy, business support services and products for members, including legal, technical, planning, workplace health and safety and business compliance advice, along with training services, contracts and stationary, industry awards for excellence, and member only discounts on goods and services.

1. EXECUTIVE SUMMARY

Following the release of an Issues Paper in April 2020 the Independent Pricing and Regulatory Tribunal (IPART) released its draft report into the Review of the Effectiveness and Efficiency of the NSW Home Building Compensation Fund (Draft Report).

HIA provides these submissions in response to the Draft Report.

The Draft Report sets out a number of draft findings and recommendations across the following six areas including:

- The effectiveness of the Home Building Compensation Fund (HBCF) to protect homeowners.
- The costs and efficiency of the HBCF.
- The regulatory barriers and framework that applies to private warranty insurance providers looking to enter the scheme.
- The operation of icare.
- The builder eligibility process.

The Draft Report highlights well-known problems with the NSW HBCF including the costly nature of the scheme and the need for transparency regarding the operation of icare and the builder eligibility process. While not underserving of attention and further improvements can be made these are matters that have been a source of constant frustration, ones that HIA has raised for many years and have already been the target of a range of reforms.

Of most concern is that the observations and recommendations regarding the lack of private sector entrants into the NSW HBCF market fail to capture the true barriers to entry. The Draft Report points to the regulatory requirements for non-insurers i.e. Fidelity Funds as the critical barrier to entry to private providers entering the market, asserting that non-insurers should be allowed to offer products that are not required to comply with APRA standards. This completely overlooks the much more simple and obvious conclusion that a scheme that has run for many years at significant losses thereby making it a very unattractive proposition for a private sector, profit-seeking business. To suggest that somehow this loss making record can be overcome by exposing home buyers to providers of lesser financial standing than an APRA approved insurer is preposterous.

The focus on and lauding of the Queensland first resort style model of home warranty insurance reflects serious misunderstanding of the detail of the Queensland operation and its financial structure.

The financial arrangements for the Queensland insurance, licensing and dispute resolution schemes are conflated to the point that it is risky to be drawing conclusion about the efficacy of its warranty provision based on its published accounts. The Queensland approach also not only inappropriately uses insurance as a dispute resolution tool but also has embedded in it a lack of natural justice that has adverse impacts on the residential building industry by, for example, encouraging regulator directed dispute resolution in the very first instance.

Any moves towards this model in NSW would require a dramatic shift in the regulatory framework and there is no guarantee such a move would result in better outcomes. A first resort style model would also only act as a further disincentive for private sector entrants.

HIA recommends that IPART consider the following as critical elements of a viable and sustainable HBCF in the long term:

- **Insurance under the HBCF is a safety net**

  Insurance under the HBCF is considered a key plank of the consumer protection framework in NSW acting as a safety net for homeowners whose builder dies, disappears, becomes insolvent or has their licence cancelled for failure to comply with an order from the NSW Civil and Administrative Tribunal (NCAT) or a court order. It is not and should not be used as a dispute resolution system. The operation of the scheme through its underwriting standards already functions as a quasi-regulatory device to limit a builder's ability to trade.

- **The private sector must be encouraged to enter the market**

  Overwhelmingly various reports and inquiries have recommended that warranty insurance schemes be run by the private sector. Competitive pressure is the best way of delivering the most cost-effective outcome for the home buying public.

  The move by the NSW Government in 2010 to take over underwriting the scheme was a significant development and probably reflected the disruption to financial markets stemming from the GFC rather than any underlying inability of the private sector to operate an effective warranty scheme. However, moves between private and public operation are far from novel, for example, the privately underwritten Domestic Building Insurance Scheme was introduced in Victoria in May 1996, replacing the previous government scheme administered by the Housing Guarantee Fund.

  Private providers, industry, Government and consumers must also have confidence that those private sector entrants are appropriately regulated to ensure they can fulfil their statutory role. To that end, all of those seeking to enter the market should comply with the APRA prudential requirements. This would provide clarity, certainty, a level playing field and reduce duplication.

- **The current design of the product must be reformed**

  Linking the basis of a claim over the defect 'tail' period (currently 6 years) to a breach of statutory warranty under the NSW *Home Building Act 1989* (HBA) is a significant contributor to the difficulties with the insurance. The high frequency of claims over that tail period caused by the nebulous nature of this trigger has been a continuing source of uncertainty for whoever underwrites the scheme including both government and the private insurer market.

  HIA is aware that linking the claims trigger to a clearer definition of a defect and providing certainty for a shorter period of defects cover will encourage the participation of private insurers in the market and negate the need for Government involvement.

  While the ability to offer split product cover was a first step, the minimum cover requirements for each limb of $340,000 coupled with these structural issues have discouraged any consideration of

entry by private providers who are prepared to provide warranty cover across the entire home building spectrum from renovations through to low rise apartments.

2. THE FIRST RESORT MODEL

While not forming part of a draft recommendation or finding, it is clear that IPART views the Queensland model and first resort insurance as an attractive alternative to the current arrangements in NSW.

HIA would oppose any moves to a first resort arrangement. The Queensland scheme is costly, inherently unfair and not in the best interests of consumer, the residential building industry or the NSW Government.

Many have been critical of the first resort style insurance model.

The 1993 Inquiry into the NSW Building Services Corporation (the Dodd Inquiry) was highly critical of the current Queensland 'one-stop-shop' approach noting that such a system was rife with perceptions of bias and commenting that:

> *"I believe there is an inherent conflict in combining the key function so industry regulation and consumer advice, dispute resolution and insurance. I also note that the management and administration of such disparate functions necessitates different structures and skills"*[1]

HIA members do not want a return to that type of scheme.

The Percy Allen review went as far as calling the model of first resort a *"cruel hoax* that resulted in *homebuyers having false expectations about their insurance rights"*[2]. This remains apposite with the Queensland Building and Construction Commission (QBCC) having the most complaints lodged against it with the Queensland Ombudsman out of all Queensland statutory bodies for 2019-2020.[3]

To categorise the Queensland scheme as 'first resort' is not entirely correct. A genuine 'first resort' insurance scheme requires that the insurer pay out on all claims and pursue builders through the courts, but without the power for the insurer to suspend or revoke builder licences, it is simply not sustainable. It gives 'an inspector or responsible body' (presumably Fair Trading) power to make decisions about rights that should be made by an impartial court or tribunal after a fair hearing. Administrative decisions to remove a business's livelihood on the basis of an unresolved building dispute triggering an unchallengeable insurance claim treads very close to an inadequate separation of powers.

Insurers experienced loss ratios in excess of 300% under previous first resort schemes in NSW. Under the previous first resort scheme homeowners were able to claim against an insurer if there was a breach of statutory warranty, regardless as to whether the builder was still in business or even

[1] 1993 pg. 46
[2] 2002 pg.26
[3] Queensland Ombudsman 2019-2020 Annual report, see Appendix B, table 4, 'Complaints about statutory authorities, (page 34) https://www.ombudsman.qld.gov.au/about-us/corporate-documents/annual-report

prepared to fix the alleged defect. The insurance cover was activated usually by a termination of the building contract.

However, under this approach insurers frequently became entangled in contractual disputes between homeowners and the builders. This feature of the first resort scheme presented a significant disincentive for insurers to enter into the schemes and added substantially to the premiums paid by the homeowners. In the first resort schemes, legal costs represented in excess of 15% of the total claims bill.

Just as in 'last resort' States, the QBCC, and ultimately the courts, require builders to comply with their legal obligations to complete building work as contracted and rectify any defects, and where this does not occur because a builder dies, goes into liquidation or disappears, the QBCC insurance policy is triggered.

However, unlike other States, where a builder refuses to rectify work that the QBCC considers is defective, the QBCC will complete the work and pursue the builder for the cost often before any review of whether or not the work is actually defective is conducted. This is facilitated by the QBCC also being the licensing authority, with power to suspend or cancel the builder's licence for non-compliance. In addition, all directors of building companies are personally liable under the QBCC Act to pay for insurance debts, costs of doing work and fines, as an incident of licensing. [4]

The first resort nature of the QBCC insurance scheme positively encourages disputes to be sent to the regulator.

It is not uncommon for contractors to first discover that their client even has an issue only when notified by the regulator. There have also been occasions where the QBCC will be taking action against a contractor even though the contractor and their client are in Queensland Civil and Administrative Tribunal (QCAT) at the same time in dispute on the same issue. A common example is unpaid money. A builder will be pursuing the owner for unpaid money under the building contract through QCAT. The owner will then separately make a defective works complaint against the builder. The builder is forced to go through the defective works process, a punishment in itself, despite the matter being before the QCAT.

QBCC insurance covers work done by any licensed contractor irrespective of whether a premium was paid for the work – this reinforces the message among consumers that the QBCC is the centre of the building universe and that they will fix anything. Further, a QBCC decision to accept an insurance claim cannot be reviewed by an affected contractor (via internal review or through QCAT) however a QBCC decision to disallow a claim can be reviewed by a homeowner (via internal review or through QCAT).[5] This means there is little scrutiny over QBCC decisions in accepting and paying out insurance claims. A contractor may apply to the Supreme Court to review a QBCC decision to accept an insurance claim however this is costly.

[4] QBCC Act s71
[5] QBCC Act s86(h)

The QBCC combines the roles of insurer and licenser of builders. HIA considers that this process also involves a conflict of interest, not to say obvious moral hazard; any work the QBCC can force a builder to do is work that it will never have to pay out on one of its insurance policies.

This conflict of interest is further exacerbated since it is in the interests of its insurance arm for a potentially insolvent builder to attempt to trade out of their financial difficulties rather than go into liquidation and trigger insurance liability, while it is the duty of the licencing arm (and in the best interests of current and future home buyers) to suspend a potentially insolvent builder's licence immediately. This conflict of interest may result in the builder's eventual collapse being more costly, and involving more consumers, than would otherwise have been the case. Indeed the QBCC's predecessor, the Building Service Authority, found itself allowing home owners to contract with businesses **after** the QBCC had determined in-house that the business did not meet its own financial standards and was expecting to have to meet significant warranty claims. The business was allowed to continue taking on these new clients in the expectation of limiting the ultimate extent of insolvency claims for incomplete and defective work.

QBCC's role as a combined regulator and monopoly insurer prevents competition on price, but it also has other undesirable aspects, including an inclination to use its administrative powers to increase its insurance income. For example, a roofing contractor doing repair work valued at more than $3,300 on the roof of a strata title property is required by the QBCC to take out a separate insurance policy for every unit in the property. As there is a minimum premium payable for each policy, and there may be 20 or 30 units under the one roof, the cost of the compulsory domestic building insurance may be many times the value of the building work done. This is a blatant case of misuse of statutory power for revenue-raising purposes.

There are also significant issues of natural justice.

Under current QBCC dispute resolution processes, inspectors issue contractors formal directions to rectify, after conducting a telephone "mediation" and a short site visit. Often this can occur without even first giving the contractor a written request to rectify the allegedly defective work.

Initial correspondence from QBCC to contractors is somewhat draconian and includes a thorough description of all the consequences of what will occur if they do not fix the (allegedly) defective items. This is the case despite such correspondence being sent before any real investigation has been completed by the regulator.

Many disputes involve matters of interpretation of codes, standards and accepted practices, rather than black and white rules. There are very real circumstances where a contractor genuinely believes that work is not defective. Not surprisingly, builders are frequently critical of QBCC opinion-based decisions that their work is defective and must be rectified. Further, non-compliance with a direction to rectify can have serious implications for a licence holder including fines, demerit points, reputational issues (directions are noted on the licence holder's publically available record) and the possible suspension or even termination of their licence. Such claims then generally proceed to be handled through the warranty insurance scheme. Rectification work by builders under the insurance scheme inherently costs more than what the original builder would complete such work for: however the

original contractor is liable for money paid out of the insurance scheme and is also noted on the licensee's publically available record.

Where the builder disputes the QBCC assessment, the matter will be resolved by QCAT, but in the meantime the consumer is relieved from having to pursue the builder and the work in dispute is rectified at no further cost to the consumer.

For example, the following court cases (from QCAT through to the Supreme Court) illustrate a situation where QBCC accepted and paid-out three defect works insurance claims, totalling over $400,000, despite never providing the individual they intended to pursue with an opportunity to attend to those defects. From a builder, or former builder's perspective, to one day receive a notice of liability for hundreds of thousands of dollars despite not being provided an opportunity to address the issue before an insurance claim is made is simply unjust.[6] In a similar case the QBCC paid out over $100,000 despite the insurance claim being made over two years out of time and again, no notice being provided to the builder regarding the rectification work. The Supreme Court overturned the QBCC's decision.[7]

HIA is aware of numerous other instances where contractors have received, with no prior notice, letters of demand from the QBCC demanding significant amounts of money for insurance claims accepted and paid out of the insurance scheme. Unfortunately, many contractors are not in a financial position to take the matter to the Supreme Court.

It will be seen that the essential difference between the Queensland and NSW schemes is not in the insurance aspect at all, but in the licensing authority's effectively unfettered power to act unilaterally to enforce builder action in relation to allegedly defective work. In NSW, an equivalent position was obtained after 2009 with the introduction of the fourth trigger for insurance claims being that the builder has their licence suspended due to non-compliance with a money order from NCAT or a court.

There are a number of other difficulties with the Queensland system. As the examples above demonstrate builders find that on the issue of whether or not work is defective, the QBCC is accuser, judge, jury and executioner. While this is of course advantageous for the individual consumer complainant, from an industry perspective, builders in Queensland need to make some allowance for the cost of redoing work that is not actually defective, since the expense to the builder of disputing a QBCC opinion on workmanship are in many cases prohibitive.

Also, the overall high degree of regulation in Queensland has associated administration costs for both Government and business, which is a hidden cost ultimately borne by home buyers (as the QBCC is required to be self-funding). This is illustrated by the growth within the QBCC bureaucracy. As at 30 June 2017, the QBCC employed 402 FTE[8] since then and, as at 30 June 2020, the QBCC employed 529 FTE.[9]

[6] Crocker v Queensland Building and Construction Commission [2017] QCAT 304; Queensland Building and Construction Commission v Crocker [2018] QCATA 194; Lee Anthony Crocker v Queensland Building and Construction Commission [2020] QSC 24
[7] Kline Industries International Pty Ltd v Queensland Building and Construction Commission [2020] QSC 243
[8] https://www.qbcc.qld.gov.au/sites/default/files/QBCC_Annual_Report_2016-2017.pdf page 61
[9] https://www.qbcc.qld.gov.au/sites/default/files/QBCC_Annual_Report_2019-2020.pdf page 30

The inevitable consequence of such a system is that this bureaucracy is subsidised by insurance and licensing costs.

The all-encompassing nature of the QBCC places an additional cost burden on the Queensland industry (which must eventually be paid for by Queensland home owners) which is not incurred in NSW, where only courts determine whether building work is defective.

The QBCC, while providing insurance cover to all who are licensed, does not cull out poor and failed builders through refusal of insurance. Rather, this culling is (in theory, at least) done through builder licensing, which is also operated by QBCC. This system does not prevent the bad builder from building but seeks to fix the problem after the bad building work has been done and the consumer adversely affected. As an illustrative example, for a job costing $5,000 a builder with a history of defective work will pay (on behalf of the consumer) the same insurance premium as a builder with a clean record of never having any defects. Obviously, the risk to the insurance scheme would be different for each builder given their prior history.

For the reasons set out above, HIA considers that the only material difference between Queensland's so-called 'first resort' and NSW's so-called 'last resort' scheme lies in dispute handing, and that improvements in dispute resolution, separate from the insurance regime, in the NSW scheme will lead to a more effective outcome than adopting the Queensland model.

Another significant issue with the first resort scheme was the claims frequency. Homeowners were effectively using the insurance to bypass their builder. This resulted in very high claims frequency, as in Queensland today. The emphasis should be on correcting the dispute resolution process and continuing to provide a last resort safety net with the fourth trigger as mentioned above.

The claims experience is also influenced by the claims trigger. In Queensland, the definition of a structural defect for the purposes of an insurance claim is much narrower and arguably clearer than that under the NSW system. To illustrate Schedule 6 of the QBCC Regulations provides that:

> *structural defect, for primary insurable work, means:*
>
> *a) if the work is for a residence or related roofed building:*
>
> *i. a defect in the work that causes or contributes to deflection or movement of the footing or slab of the residence or building so the residence or building no longer complies with the building assessment provisions under the Building Act 1975; or*
>
> *ii. the work does not comply with a performance requirement under the Building Code of Australia, part B1 or part 2.1 for the residence or building; or*
>
> *iii. a defect in the work that causes the residence or building to be uninhabitable or not reasonably accessible; or*
>
> *b) if the work is for a swimming pool—a defect in the work that allows water to escape through the shell of the swimming pool; or*
>
> *c) if the work is on or for a residence, related roofed building or swimming pool—a defect in the work that adversely affects the health or safety of persons who occupy or use the residence, building or swimming pool; or*

d) *if the work is on or for a residence or related roofed building—a defect in the work that allows water penetration of the residence or building.*

In NSW a breach of the statutory warranties under section 18B of the HBA provides the basis for an insurance claim:

a) *a warranty that the work will be done with due care and skill and in accordance with the plans and specifications set out in the contract,*
b) *a warranty that all materials supplied by the holder or person will be good and suitable for the purpose for which they are used and that, unless otherwise stated in the contract, those materials will be new,*
c) *a warranty that the work will be done in accordance with, and will comply with, this or any other law,*
d) *a warranty that the work will be done with due diligence and within the time stipulated in the contract, or if no time is stipulated, within a reasonable time,*
e) *a warranty that, if the work consists of the construction of a dwelling, the making of alterations or additions to a dwelling or the repairing, renovation, decoration or protective treatment of a dwelling, the work will result, to the extent of the work conducted, in a dwelling that is reasonably fit for occupation as a dwelling,*
f) *a warranty that the work and any materials used in doing the work will be reasonably fit for the specified purpose or result, if the person for whom the work is done expressly makes known to the holder of the contractor licence or person required to hold a contractor licence, or another person with express or apparent authority to enter into or vary contractual arrangements on behalf of the holder or person, the particular purpose for which the work is required or the result that the owner desires the work to achieve, so as to show that the owner relies on the holder's or person's skill and judgment.*

The difference has obvious impacts on costs.

The Queensland approach insulates the insurance scheme from payouts by either strongly incentivising builders to rectify works, whether or not such work is rightly one for the builder to fix, or, if the builder refuses to fix pursuing the individual for those costs. This is why the costs of the scheme seem lower and premiums less than elsewhere and it would be superficial to conclude that the scheme is more inexpensive than a last resort system. Any return to a licencing-plus-insurance type operation, along the lines of the QBCC, would be very expensive to set up and fund, both initially and on an ongoing basis.

3. EFFECTIVENESS OF THE SCHEME IN PROTECTING HOMEOWNERS

The Draft Report would appear to be based on the mistaken view that the NSW HBCF has a role to play in dispute resolution and in encouraging better building practices. This is not the purpose of insurance under the HBCF.

If there are concerns regarding the effectiveness of the current dispute resolution processes in NSW then those matters should be addressed separately and discretely; insurance should not be used and should not be seen as a solution to these concerns.

Under the HBA, insurance under the HBCF forms part of the consumer protection regime for homeowners undertaking residential building projects. What is significant is that there are many other aspects of that framework that act to protect a consumer prior to an insurance claim.

In 2009, when the *Home Building Amendment (Insurance) Bill 2009* was read into the NSW Parliament the NSW Fair Trading Minister at the time Virginia Judge stated:

> *'Under the last resort insurance scheme a homeowner, including a strata corporation, is principally responsible for enforcing statutory warranties. Home warranty insurance is a safety net in the event that this is not possible. A homeowner needs to actively enforce their rights. They cannot sit back and simply do nothing waiting for a builder to die or go out of business before making an insurance claim'.*

Such observations are crucial to understanding the operation of the scheme, yet seem largely absent from the Draft Report.

The above statement recognises that the primary recourse for a consumer who finds defective building work is through the Statutory Warranties as set out under Section 18B of the HBA. These warranties act as the principal consumer protection mechanism, supported by contract regulation and a licensing framework.

Insurance under the HBCF 'steps in' where the builder is unable to fulfil their obligations under the Statutory Warranties.

It is important that the scheme not be mistaken for a dispute resolution vehicle. It is not appropriate for insurers to resolve disputes between builders and consumers - this task must be the responsibility of the State tribunal or courts. As outlined above when the two are fused in the same body there is moral hazard, since a finding in favour of one party or the other will have direct financial implications for the regulator.

Also, the differences between this form of insurance and other insurances are important. Insurance under the HBCF is not like workers compensation (which allocates risk based on payroll size and claims history) or third party insurance (which aggregates actuarially quantifiable risks to persons who have no control over the occurrence of that event).

As a safety net, insurance under the HBCF provides a minimum entitlement that cannot be abrogated and is distinguishable from consumer protection more broadly which can be described as a group of laws designed to ensure the rights of consumers as well as fair trade, competition and accurate information in the marketplace.

It is HIA's view that examining insurance under the HBCF through the lens of protecting homeowner confuses its purpose, promoting the scheme to something well beyond that which would generally be considered a 'safety net'. This creates a barrier to real reform. Insurance under the HBCF is not designed to resolve disputes between sellers and consumers but to shield consumers from the full consequences of a failure by the supplier to meet their legal obligations.

3.1 RESPONSE TO DRAFT FINDINGS AND RECOMMENDATIONS

HIA considers that the draft findings and recommendations that relate to section 3 of the Draft Report are beyond the scope of the terms of reference and were not raised in the April Issues Paper.

Dealing with these matters discretely and separately from any consideration of the efficiency or effectiveness of the NSW HBCF HIA would support the following comments made in the Draft Report that there is a need for:

- a sufficiently resourced Fair Trading, with expertise across all building aspects.
- Faster access to NCAT and time limits of the resolution of issues.
- NCAT directly engaging independent experts.

Draft Finding

1. ***Building issues can be costly and take a long time to resolve through the dispute resolution mechanisms that apply when a builder is still trading (ie, has not become insolvent, died or disappeared, or has had their licence suspended).***

Whilst the majority of construction is undertaken without issue or dispute, occasionally, disagreements develop between the homeowner and homebuilder. Such disagreements can occur during the course of construction, or in some instances many years after the house is completed.

In HIA's experience, most building disputes and disagreements arise because of one or a combination of the following: quality of work issues; unrealistic client expectations (often fuelled by an unfamiliarity with the building and construction processes); a poor understanding of the construction contract by the owner and poor contract administration by the builder; project management issues; and a breakdown in communications between the owner and builder.

Dispute resolution mechanism can always be improved, there are no 'winners' in a system that is lengthy, costly and cumbersome. However, as mentioned earlier, attempting to 'speed up' dispute resolution through an insurance solution including a first resort style approach is ill-advised.

Ineffective methods for resolving disputes and dealing with consumer complaints not only affect the cash flow and business operations of affected contractors, they impact on the industry at large, may erode consumer confidence and affect its reputation.

One of the key difficulties in devising an effective policy and model for residential construction is that home owners and residential consumers have little experience in commercial 'rules of engagement'. Rightly or wrongly they often become emotionally involved in the dispute and can focus on what they want or expect after the design and specifications are completed and the contract is signed. They measure their expectations in absolute terms – 'there are no grey areas' nor opportunity for compromise.

In resolving disputes between home owners and building contractors it is important to have mechanisms that are effective, prompt, low cost and also reflect the consumer protection environment in which the builder operates.

Draft Recommendation

1. ***That the NSW Government improve access and timeliness to dispute resolution processes, by ensuring Fair Trading and NCAT are sufficiently resourced and have the relevant expertise.***

HIA does not opposes this draft recommendation.

2. ***That Fair Trading develop a program of proactive investigations and audits of building work in the low rise residential sector, similar to the approach being taken by the Building Commissioner in relation to apartment buildings.***

HIA sees that the current approach by Fair Trading to the investigation and auditing of residential building sites is appropriate and the approach being taking by the Building Commissioner in relation to apartment buildings is inappropriate for the low rise residential sector.

For example, the current cohort of inspectors are ill-equipped and not appropriately qualified to carry out this function. As with the new apartment inspectorate, any proactive inspection regime would need to be underpinned with qualified industry professionals with recent and relevant experience. A significant investment in training and development would need to be undertaken.

This is likely to be an expensive approach with only limited prospects for being on the right site at the right time to resolve a dispute.

3. ***Fair Trading and NCAT should collect information and publicly report on the number and type of complaints (including construction type, issue type, value of rectification and other costs), and the time taken to resolve them.***

HIA suggest a cautious approach be adopted when looking to release this type of information publically. Also important is to determine the purpose of releasing the information – it may be that that data is/could be captured and used for internal purposes such as resourcing, education, targeted audit and compliance activity, without it needing to be public.

It would also seem sensible that the putting forward a recommendation of this nature be accompanied by a recommendation that an audit of the existing information is captured. HIA understands that across NSW Fair Trading and NCAT information regarding complaints and home building disputes is already captured and made publically available. For example the Fair Trading Complaints register provides monthly tallies of complaints against businesses. That information is available for 2 years and sets out includes:

- location of the store/business,
- product involved in complaint, and
- complaints by issue.

NSW Fair Trading also publish details regarding enforceable undertakings which includes details of the offence and enforcement action data is published and available for up to 2 years.

Finally, NCAT annual reports provide a breakdown of cases under the home building category including details such as the number of applications, finalisations and clearance ratios.

It is also important to consider that there is also potential that such an approach could have an effect on homeowners, who may be uncomfortable with those details of a dispute being made publically available, as they may, for example have an adverse impact on property value.

4. ***The lodgement of a complaint or dispute with Fair Trading or NCAT for a specified defect within the warranty period preserve a claim for insurance in relation to that defect. Currently, homeowners must also notify the insurer of an issue within the warranty period.***

HIA opposes this approach for the following reasons:

- Homeowners should be required to take positive steps to preserve their rights to make a claim, as is the case with all other forms of insurance.
- Homeowners should be required to take positive steps to mitigate their loss. As reflected in section 18BA of the HBA a homeowner has an express duty to mitigate their loss and take action to notify of that loss. This should apply equally to a claim for insurance under the HBCF.
- The notification requirements and other timeframes also limit the exposure to the HBCF. If all complaints and disputes to Fair Trading or NCAT triggered a possible insurance claims this could increase the insurance liability exponentially, increasing costs and adding yet another disincentive to private insurers entering the NSW warranty insurance market.

4. COSTS OF THE HOME BUILDING COMPENSATION FUND

HIA agrees that the best way to improve the efficiency of the scheme is if there is a choice of providers and a competitive market. However this will only be possible under a certain set of conditions, which are not recommended in the Draft Report.

Primarily, the costs associated with insurance under the HBCF are attributable to the following 3 factors:

- A monopoly insurance provider.
- Long and unpredictable tail defects warranty period.
- Problematic claims trigger.

These matters are elaborated on throughout this submission.

4.1 RESPONSE TO DRAFT FINDINGS AND RECOMMENDATIONS

Draft findings

2. ***HBCF premiums in NSW are significantly higher than premiums for similar schemes in other states.***
3. ***We estimate that the average claim value in NSW is around 50% higher than claims made under similar schemes in Victoria and Queensland (after adjustments have been made for differences in coverage and building costs).***
4. ***NSW has fewer claims than claims made under similar schemes in other states.***

These findings simply point to the long term mismanagement of the scheme and the failure to take appropriate steps towards real reforms. The reluctance to address the (at least) decade long position that the scheme has been operating at a loss has left the only lever to improve the financial sustainability of the scheme as one that focuses on increasing premiums.

Further, average claims costs are a direct result of the management and the prevention of claims leakage. This is caused by the acceptance of claims not covered under the policy, inadequate tendering and the situation where a claim can be brought within 10 years of the completion of the property meaning that claims can continue to develop for up to 13 to 14 years.

As outlined above there are clear steps that can be taken to redress these findings.

Draft Recommendations

5. ***SIRA report on costs as part of its annual performance monitoring review so that icare's costs can be more easily tracked over time, and compared with costs of the schemes in other states.***

While HIA does not oppose this draft recommendation, comparing costs is somewhat of a moot point unless there is some subsequent action to remedy poor performance.

6. ***The use of brokers become voluntary under the scheme, to provide builders with more options on how they manage their HBCF obligations.***

HIA have a number of concerns with this draft recommendation.

To fundamentally alter the distribution method for insurance under the HBCF is unsound, overstates the 'cost' of the brokerage system in NSW and will not have any significant effect on the long term viability of the fund.

Reducing administrative costs by manipulating the distribution model shuts the gateway to the private insurer market and removes a key element of individual risk ratings. Adopting this recommendation will make insurance under the HBCF a permanent fixture on the NSW Government's balance sheet.

The role played by intermediaries goes directly to the ability of a builder to obtain insurance.

The broker network:

- Distributes thousands of warranty insurance certificates per year;
- Plays a vital role as advocate during the initial and ongoing eligibility processes; and
- Manages and assists builders with the thousands of eligibility reviews conducted each year – the cost of which to the brokers, cannot be determined. .

To remove or attempt to replace the competitive and efficient private sector network that carries out these functions by arbitrarily removing brokers would ultimately be more costly and less efficient.

Furthermore, if the current system of intermediaries was replaced and brokers were not available for builder advocacy a bottle neck would occur within a government department with thousands of builders seeking advice and assistance from one source rather than multiple sources. This would inevitably impact on the quality of the decisions made.

Agent administrative cost represents underwriting and claims management of individual cases. It is a misapprehension to suggest that significant savings can be achieved against the functions that the agent is currently responsible for.

Further, changes made in 2017 to the brokerage arrangements and fee structures has meant that:

- From April 2017 icare ceased paying commissions to broker distributors effective. This change has brought the HBCF in line with icare Workers Insurance which does not pay commissions.
- Broker distributors have adopted a fee-for-service model where they now charge builders with competitively-set fees.
- Broker distributors' fees will be separate to the premium paid for HBCF insurance.
- Broker distributors decide how much they charge for their services independently and it is a matter between the broker distributor and their builder clients.

Therefore it is unlikely that any further changes would have any significant impact on the costs associated with the scheme.

7. icare's premium calculator provide the estimated premium for each builder to help homeowners better manage their costs and understand the insolvency risk associated with different builders.

The calculation of a premium is a complex matter and is not simply a reflection of the 'risk of insolvency'. Information considered when determining that premium include financials, the history and experience of key people, the length of time (by both individuals and business) in the industry, the type of projects carried out, even the location of a particular job etc, as such the premium should not be used as an indicator of competence. Further, builders are already required to separately disclose the cost of insurance in the contract, therefore a potential client already has that information prior to signing the building contract.

Better indicators of performance are licence checks, reference checks, obtaining multiple quotes and ensuring that the builder is complying with regulatory requirements.

5. REMOVING REGULATORY BARRIERS TO ENTRY

5.1 RESPONSE TO DRAFT FINDINGS AND RECOMMENDATIONS

Draft Finding

5. There are regulatory barriers inhibiting entry for private providers. In particular, it is unlikely that fidelity funds that are not regulated by the Australian Prudential Regulation Authority (APRA) could offer HBC cover in NSW under the current drafting of the legislation.

Draft Recommendation

8. The NSW Government amends section104A of the Home Building Act 1989 and associated Regulation to allow alternative indemnity providers to offer a discretionary (non-insurance) product.

HIA's response to this draft finding and recommendation is threefold.

Firstly, there is a need for some oversight of potential private providers seeking to enter the NSW HBCF market.

Secondly, to suggest that the current regulatory regime is the barrier to entry for private providers fails to paint a complete picture of the current situation. There are a number of structural barriers

embedded in the current scheme which are acting as strong disincentives to private providers, not the least of which is the loss history of the scheme.

Finally, suggestions that removing regulation in order to allow discretionary (non-insurers) to enter the market is ill-advised and exposes the home buying public to increased risk of dealing with a warranty provider of lesser financial standing.

These matters are elaborated on below.

5.2 The need for Oversight

HIA has stated on previous occasions that any warranty insurance product, including an Alternative Indemnity Product (AIP) including Fidelity Funds, that seeks to enter the NSW warranty insurance market be regulated by APRA. This is primarily for two reasons:

- Firstly, Fidelity Funds do not provide adequate consumer protection. The inability of a Fidelity Fund to unilaterally increase contributions poses a risk that losses as a result of claims cannot be covered nor recouped.
- Secondly, Fidelity Funds are not subject to the same oversight and regulation as other APRA approved insurance products. APRA has consistently over the years drawn attention to the fact that existing fidelity funds (constituted as a trust) generally do not have adequate risk management systems and internal controls in place, or sufficient capital, to satisfy APRA's Prudential Standards. Liquidity of assets and the forms in which they may be invested, gearing, and the methodology for determining the trust's risks and liabilities are also areas where fidelity funds are not required to comply with the same standards as insurers. There is no doubt that any potential NSW home warranty fidelity fund would also fail to satisfy APRA standards.

To adopt anything other than a strict approach to prudential supervision or to take an approach that would see the regulation of warranty insurance products go unmaintained would be an abrogation of governmental responsibility.

The refusal by SIRA of two licenses indicates that the regulatory framework is working appropriately.

In fact, the suggestion in the Draft Report of ways that discretionary funds could operate without diluting consumer protection by limiting their application to low-risk building segments (leaving icare with the higher risks) and establishing rules to govern how that discretion would apply simply amplifies the point that APRA regulatory oversight is required and that the operation of a non-APRA approved product including Fidelity Funds are inappropriate for the NSW HBCF market.

5.3 Real Barriers to Entry

While the current regulatory framework that requires compliance with SIRA requirements and also, for insurance products, compliance with APRA requirements is one factor that may weigh against entry by private providers into the NSW insurance market, without making other changes to the scheme design, regulatory changes will do very little to make the market attractive.

The real barriers to entry for both private insurance providers and AIP include:

- Private insurers are at a competitive disadvantage when compared to icare.

icare have not been subject to the same rigor as potential private providers, have access to data not publically available, a default customer base and claims history and business and financial data. This puts icare at a significant advantage.

Specifically that icare has been deemed a licensed insurer for the purposes of the regime, and is therefore exempt from a range of requirements that both AIP and APRA regulated insurers would be required to comply with. Further as icare is financially backed by the NSW Government they are also deemed to comply with the minimum capital requirements.

- The maintenance of a long and uncertain tail product linked with a nebulous claims trigger is an unattractive proposition to the private market.

The defects insurance cover period must be reduced; without such a change, private insurers are unlikely to ever re-enter the NSW HBCF market.

Under private market conditions this change would have a range of positive effects.

For the consumer the builder's obligations and responsibilities under the current 6 years statutory warranties applicable to major defects remains untouched. A consumer's fundamental right to have residential building work, completed and free from defects remains the centrepiece of the NSW consumer protection framework.

For a builder, reforms to the HBCF that would practically allow private insurers into the market would take significant pressure off premiums helping to maintain affordability. Further, a shorter and more certain 'tail' provides an incentive for a homeowner to report defects as soon as they arise increasing the likelihood of the builder being present to rectify which will reduce pressure on the fund.

Finally a confident, buoyant and active building industry is beneficial for builders, taxpayers, and the state Government.

In conjunction with this, the severing of the link between a warranty insurance claim (because of the insolvency, death, disappearance or licence suspension of a builder) and a breach of statutory warranty (by providing a separate and distinct claims trigger) would provide clarity and certainty in relation to what can be claimed. This would reduce the frequency of claims ultimately reducing frustration and litigation around the type of defects that can be the subject of a claim. This creates certainty and bolsters confidence in the industry.

Under these circumstances risk can be effectively quantified having a positive impact on premiums and ultimately housing affordability. Further, the product becomes truly reflective of its purpose creating clarity in the industry as to the application of warranty insurance.

It would also mean that industry, insurers and consumers can be confident in knowing the types of claims covered by warranty insurance which will in turn enhance a consumers understanding of the intent and purpose of the product.

Consumers retain their current rights under the warranties, and would be able to pursue these rights in the same way as they can in relation to other consumer products under the Australian Consumer Law.

- The 10 year limit on claims

The major defects cover period needs to be removed, or at the very least considerably shortened. This is a major barrier to the entry of private providers. The maximum 10-year cap on when claims can be made against home warranty insurance policies issued was introduced in 2011 and originally only applied to contracts entered into before 1 July 2010. Its intent was to remove the uncertainty around when claims could be made, and to facilitate the timely release to builders of bank guarantees and deeds of indemnity held by insurers.

Insurance providers could have to wait up to 10 years to earn revenue. In fact it is even longer than this. In NSW, if it can be demonstrated that the claim occurred within six years, it is possible to bring a claim for up to 10 years. As SIRA and icare would be aware, a claim can continue to develop for a number of years after the 10 years provided it was brought within the 10 years.

Claims can and do continue to develop for a number of years after the 10 year period has passed. Claim development from an actuarial sense can take up to 14 years at the extreme end. Given this, no private insurer is going to participate in a scheme that means you earn your premium over that period of time and where there is no certainty of a return of the capital investment.

- Minimum capital requirements

The fact that each of the split cover products requires minimum capital for each potential $340,000 claim means that where an insurer wishes to offer both products they are likely to have to double their minimum capital requirement due to the potential of a combine $640,000 of claims. By comparison icare will continue to offer the same cover under the same minimum capital requirements for a potential maximum exposure of $340,000 for cover for both limbs.

5.4 Concerns With Fidelity Funds

The current regulatory framework was purpose built to ensure that those wishing to offer a product to satisfy the statutory requirements for insurance under the HBCF were held to an appropriate standard. Without the current requirements, HIA sees that AIP's such as Fidelity Funds are not an appropriate option.

In reality, because Fidelity Funds are not subject to the same compliance and risk controls, they offer poor consumer protection as compared to a licensed and reputable APRA-approved insurer with reinsurance.

Particularly during the period of their infancy, Fidelity Funds will be undercapitalised and exposed to larger (class type) claims. They have limited reinsurance protection. They are also unable to unilaterally increase contributions, which poses a risk of loss to the fund, as claims cannot be covered nor recouped. This creates moral hazard for the government, who are politically exposed to the risk of "propping up" the fund in the event there are insufficient pooled funds to cover a collection of larger claims.

Further, because they have lower operational and capital backing costs, Fidelity Funds have a significant commercial advantage over regulated insurance businesses that are compelled to satisfy the full prudential requirements and scrutiny of APRA.

This creates an anti-competitive market environment. To ensure a competitive and viable market, HIA maintains the view that Fidelity Funds must be regulated on an equal footing with insurers regulated by APRA.

Due to their operation as a trust arrangement, there is a lack of transparency in relation to the management and operation of Fidelity Funds. This could have significant implications for consumer protection.

HIA sees that it is appropriate that before approving a product or issuing a licence, SIRA must carefully consider the financial position and constitution of the provider and proposed product. SIRA can also impose conditions on the licences of providers as well as require them to meet prudential standards and underwriting requirements, and to provide financial assurances if necessary to ensure competitive neutrality.

6. DOES THE REGULATORY FRAMEWORK INCREASE THE COSTS OF ENTRY TO THE HBC MARKET?

6.1 RESPONSE TO DRAFT FINDINGS AND RECOMMENDATIONS

Draft findings

6. That the HBC licensing framework unnecessarily duplicates APRA's role in the prudential supervision of insurers, increasing costs of entry to the scheme for insurers.

HIA agrees that there is currently a degree of duplication in the regulatory framework. HIA advised against this during consultation on the regulatory arrangements.

HIA's consistent position has been that both potential insurance products and alternative indemnity products simply be required to meet and comply with the APRA's prudential requirements.

7. That the regulatory framework deters entry by unnecessarily restricting how private insurers and providers compete in the market.

HIA agrees with this finding. It is APRA's role to regulate insurers. Those seeking to enter the market should simply be required to meet and comply with APRA requirements and not be required to meet both SIRA's regulatory requirements and the APRA requirements.

8. ***HBC is a 'long-tailed product', which means providers must hold capital to cover liabilities for up to 10 years, discouraging providers from entering the market.***

HIA agrees with this finding. As outlined above it is HIA's view that the tail should be shortened. In such a situation consideration could also be given to additional voluntary insurance cover purchased directly by the consumer.

Draft Recommendations

9. ***That SIRA simplifies its licence application process for insurers to recognise that APRA's prudential standards apply, removing the need for a duplicate assessment. This could reduce licence fees payable by insurers.***

It would seem reasonable and sensible to deem insurers that meet the prudential requirements by APRA to be licensed for SIRA's purposes. HIA would agree that non-insurer providers should remain subject to SIRA's licensing framework which should reflect APRA standards.

10. ***That the NSW Government:***

    - ***limits the application of sections 103BD to 103BG of the Home Building Act 1989 that regulate premium pricing to the default market incumbent, icare***
    - ***removes the requirement for SIRA to approve private insurers and providers' eligibility and claims models, in favour of a market monitoring arrangement where SIRA reports on market participants' performance against high-level principles.***

    This should be reviewed in five years or earlier if the market composition has changed considerably

HIA does not oppose these recommendations.

11. ***That the NSW Government requires icare to make available separate cost-reflective construction period and warranty period products so that a new entrant could provide construction period cover only.***

While HIA would support moves to require icare to make available separate cost-reflective construction and warranty period products that simply does not go far enough to resolve the fundamental issue regarding the operation of the split product.

The regulatory framework now allows for both split product offerings and combined product offerings. While the minimum coverage remains different between them, no private provider will offer each limb separately. The Draft Report argues that requiring a minimum of $340,000 to apply to each product would not drive up costs because claims are rarely made for both periods of cover. Whether a claim is actually made is irrelevant to the minimum capitalisation requirements that must be met. An insurer must ensure they are adequately capitalised in the event that the minimum cap of each limb is exhausted, increasing costs, including premiums and reducing the attractiveness of the market when providers can offer a combined product at (arguably) 50 percent less cost.

This fundamental inconsistency must be resolved.

7. INCREASING SIRA'S REGULATORY OVERSIGHT

7.1 RESPONSE TO DRAFT FINDINGS AND RECOMMENDATIONS

Draft Recommendations

12. An independent regulator determines icare's premiums for the HBCF to ensure they reflect efficient costs. SIRA's role, as the scheme regulator, could be expanded to provide it with determination powers. Alternatively, IPART, as the NSW pricing regulator, could be given the on-going role of determining icare's HBCF premiums.

HIA agrees with this draft recommendation. Whether it is the role of SIRA or IPART icare should be required to charge a premium equal to the actuarial forecasts and one which allows true competition from new entrants.

13. SIRA increases its regulatory oversight of icare by reviewing and determining icare's builder eligibility model and claims handling processes.

14. SIRA establishes appropriate KPIs against which it can measure and publicly report on icare's performance in resolving eligibility issues and finalising claims in a timely manner.

While HIA sees some merit in increasing SIRA's oversight over icare this approach must be considered with new entrants in mind. Private insurers may recoil at an approach in which the regulator is telling them how to determine how to accept risk and how to handle claims, other than what is currently required by law. This also has the potential to undermine and competitive advantage a private provider may be able to build into their processes and approach.

8. BUILDER ELIGIBILITY PROCESS

8.1 RESPONSE TO DRAFT FINDINGS AND RECOMMENDATIONS

Draft Recommendations

15. icare provides greater transparency in how it undertakes its eligibility assessments and how it determines individual builder loading/discounts used in risk-adjusted premiums

16. icare:

- ***Provides information in plain language in the Builder Eligibility/Change application form or the Builder Self Service Portal, why particular information is sought and how it would be used in determining a builder's eligibility.***
- ***Provides information in plain language on how the information provided by builders was used to determine their eligibility profile and their individual loading/discount, including any conditions of eligibility.***

- ***Makes clear any adjustments that have been made to take into account any industry specific circumstances eg, the adjustment for a pool builder in determining their eligibility to account for 'sleeper pools'.***
- ***Periodically updates the work undertaken by the Data Analytics Centre in 2016, to examine whether the factors previously identified and currently used, continue to be significant in predicting builder insolvency, and if there is scope to reduce the amount of information sought without necessarily increasing risk.***

17. icare reviews its dispute resolution processes to resolve eligibility issues in a more streamlined and timely manner

Broadly speaking HIA supports greater transparency and a more educative and consultative approach in relation to the eligibility process.

It is through the granting of insurance eligibility, that the scheme significantly influences the ability of a contractor in the residential construction industry to trade, including the type of work they can carry out, the value of that work and the number of jobs that can be on foot at any one time. In that way the scheme acts as, and is considered to be, a quasi-regulator. Decisions by icare affect the day to day livelihood of those in the industry and warranty insurance is consequently an emotive issue for HIA members. Eligibility limits can unduly restrict the growth of a residential builder and the imposition of risk mitigation measures to have such limits lifted (often through the piercing of the corporate veil) is needlessly excessive and onerous. The limits also impose significant hurdles for new builders entering the market.

HIA agrees with the Draft Report's observation that icare and any other provider should be responsible for managing its own risks and permitted to have the flexibility to set their own eligibility criteria, to do otherwise would undermine the principle of encouraging a competitive market.

It is also of note that the draft recommendations appear to make a concession regarding the complexity and onerous nature of the eligibility process. While improvements can and should be made, recommendations to remove the broker system sit at odds with the recognition that those engaging with the system generally need support to navigate it.

The need for transparency must also be balanced with the reality that scheme underwriters and any new insurer entrant should not and will not disclose absolute underwriting criteria. Doing so in the past has led applicants to orchestrate their application to falsely meet the criteria. The risk of requiring absolute transparency is that it would make brokers and underwriters irrelevant, an unappealing outcome.

The function of the underwriter is to assess the factual information and determine risk based on that information. If the applicant is made aware of the information which may discredit the application then that information will most probably not be provided. Brokers on the other hand can advocate for the client and ensure for the underwriters sake the information required is provided in a true and factual way. In the absence of brokers, builders would require assistance of their accountants in navigating eligibility assessment and this would come at a much greater expense.

HIA is supportive of updating the data used in the eligibility process. Beyond this however, underwriting needs to use real time data and analytics to better understand emerging risks. Currently underwriting is done by analysing accounts that are between 12 and 18 months old.

9. HBCF PRODUCT SPECIFICATIONS

9.1 RESPONSE TO DRAFT FINDINGS AND RECOMMENDATIONS

Draft Recommendation

18. SIRA produce guidance for the building industry that addresses the following questions:

- ***For contracts that require HBCF cover, whether items such as soft-scape landscape works and pool equipment can be excluded from HBC requirements***
- ***How to allow for variations in the cost of HBCF in contracts, if the exact contract price is not known at the time the contract is signed***
- ***Whether head contractors can require subcontractors to also purchase HBCF cover for subcontracted residential works exceeding $20,000***
- ***Whether HBCF cover is required for alterations and renovations for multi-units above three storeys.***

HIA does not oppose the development, in consultation with industry, of further guidance on the above matters. However, HIA does not see that there is much practical controversy around these issues, for example, currently the obligation to take out insurance under the HBCF sits with the builder who is engaged by the homeowner and any subcontractors engaged by a builder are not required to take out insurance.

The need to provide for the cost of insurance in a contract for residential building work has created the difficulty identified in the Draft Report.

Under the HBA a builder cannot do any work, or take any money until insurance under the HBCF is in place. However, the insurer requires a signed contract before granting insurance cover. Not being able to receive any money without having insurance cover for a project affects the certainty of progressing on the basis of that contract.

This difficulty identified in the Draft Report arose from changes as a result of the *Home Building Amendment (Compensation Reform) Bill 2017*. The amendment, now s 7(2)(f1) of the HBA, relating to the cost of cover is one for which HIA sees no purpose.

On its website, SIRA provides some rather unclear guidance about building contracts and HBC cover. The following guidance is directed to builders:

> *Your contract must disclose the total amount of money that you had to pay for the cover (which may include brokerage, fees and taxes).*
>
> *If the contract will be signed before you buy the cover, it must include a reasonable estimate of what the cover will cost.*

HIA makes the following observations:

The legislation requires that a contract must contain the 'cost of cover' (s 7(2)(f1)). It is not clear whether the 'cost of cover' is confined to the premium only, or the premium plus brokerage, fees and taxes. Including this information on SIRA's website, other than providing SIRA's view, does not provide clarity on the matter. The use of the phrase 'cost of cover' would tend to lead to the interpretation that it should be confined to the premium only.

In respect of the guidance relating to a reasonable estimate, HIA observes that although this might be a desirable outcome, HIA is of the view that there is nothing in the legislation that permits the use of a

reasonable estimate in the contract. The phrase ‘cost of cover,’ may be ambiguous in respect of what is to be included in arriving at the cost, but probably cannot be read as being wide enough to embrace the notion of an estimate. A court or tribunal may take the same view. Consequently, SIRA’s guidance poses a risk to members who seek to use an estimate to satisfy the legislative requirements.

During the reform consultation period, HIA argued against the insertion of the cost of cover provision into the HBA as the requirement to attach the certificate of insurance was already sufficient protection for the home owner. HIA’s primary position would be for the cost of cover provisions to be removed, but failing that it may be possible to amend the regulations in such a way as to embrace the use of reasonable estimates when dealing with the cost of cover.

The risk of doing something that does not comply with the legislative requirements, notwithstanding what the regulator advises means that there is an inherent risk and potential cost to the business.