



SUBMISSION BY THE
Housing Industry Association

to the
WA Home Indemnity Insurance Review

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1. Executive Summary

- 1.1.1 The Housing Industry Association (HIA) welcomes the opportunity to contribute to the review of the WA Home Indemnity Insurance scheme.
- 1.1.2 HIA supports the review, but considers that the current framework is fully functional and provides appropriate consumer protection under an acceptable insurance framework. That is not to say that there are not improvements that could be made, provided these can be done at a reasonable cost that does not exceed the value to consumers of any additional benefits.
- 1.1.3 The discussion paper accompanying the review broadly deals with components of the building framework, namely:
 - *The appropriateness of Government involvement*
 - *The insurance model; and*
 - *The role, responsibilities and accountabilities of the institutions involved.*
- 1.1.4 HIA considers that some level of Government involvement in the home indemnity insurance marketplace is justified to ensure acceptable levels of consumer protection, and a stable insurance market.
- 1.1.5 HIA also considers that a voluntary scheme would not provide the levels of consumer protection desired by the Government.
- 1.1.6 If home indemnity insurance is to be compulsory, the WA Government should implement a competitive insurance scheme which entitles builders to obtain any level of warranty coverage they are prepared to pay for, based on risk, turnover and performance.
- 1.1.7 There is a need to attract additional insurers into this market to ensure that competition can operate effectively. Any measures which would discourage additional insurers entering the market should be avoided, if possible.
- 1.1.8 Interstate comparisons favour the current WA scheme, and proposals to adopt superficially attractive measures from other States need very careful consideration.
- 1.1.9 The Queensland scheme is not really 'first resort' as the QBSA has power to direct builders to do work or lose their licence. A true 'first resort' building insurance scheme requiring insurers to pay out on all claims and pursue builders through the courts, but without the power for insurers to suspend or revoke builder licenses, is simply not sustainable.
- 1.1.10 The only material difference between Queensland's so-called 'first resort' and WA's so called 'last resort' insurance scheme lies in dispute handing.
- 1.1.11 Annual professional indemnity warranty insurance policies lack a guarantee of cover through the warranty period, have additional consumer protection concerns and should not be used as a substitute for the current project-based home indemnity insurance.
- 1.1.12 A Fidelity Fund would not be a viable scheme, as was demonstrated when one was tried in the ACT. Also, the costs of establishing such a fund, until it built up a sufficient pool of working capital, would be very significant.



- 1.1.13 HIA considers that the extension of home indemnity insurance to subsidence should be carefully investigated to ascertain if this is really necessary in WA and can be provided by insurers at a reasonable and affordable price. If such additional cover is considered necessary, alternative ways of providing it should be considered, including through home and contents insurance.

2. Introduction

- 2.1.1 HIA is the premier industry organisation in the home building sector of the Australian economy, and represents some 34,000 members throughout Australia and 4,000 in WA. It employs a professional staff of some 350 persons and forms its policies through an internal democratic system of committees made up of its members serving in a voluntary capacity.
- 2.1.2 HIA Members are the builders with whom consumers deal when contracting for home indemnity projects. In addition, they are the purchasers of statutory home indemnity insurance.
- 2.1.3 HIA is also a participant, together with AON Risk Services, in a joint venture insurance brokerage company, HIA Insurance Services Pty Ltd (HIAIS). HIAIS is a commercial operation whose sole function is that of an insurance broker, specialising in delivering insurance products, and providing insurance advice and advocacy to the residential building industry. HIAIS operates as an authorised representative of Aon Risk Services Australia, which holds an Australian Financial Services licence. HIA originally entered into this arrangement in order to ensure that its members were able to obtain access to home indemnity insurance at the best possible price.
- 2.1.4 This joint venture between an association and an insurance broker is a unique structure in the Australian insurance distribution industry, and has many benefits. The benefits of the joint venture structure is that it combines the strength, infrastructure and insurance market expertise of Australia's largest broker Aon, with the deep understanding that the HIA has of the residential construction industry and the needs of those operating within it. This allows that knowledge and expertise to come together to assist HIAIS to develop a range of industry leading insurance products and services, that meet the real needs of its customers, including HIA members.
- 2.1.5 HIA provides this explanation at the outset simply to clear up any possible confusion between HIA and HIAIS. This submission is made by HIA, any views expressed herein are HIA's own and not those of HIAIS.
- 2.1.6 Furthermore, HIA does not consider that its involvement in HIAIS creates a conflict of interest such as would prevent it putting forward the views of its members on the issues raised in the consultation paper. HIA's income from this joint venture is a relatively minor element in its overall finances, and in any case HIA's policies are determined not by its business interests but by the votes of its many thousands of individual members through HIA's democratic policy formulation processes.

3. Previous Consideration of Issues.

- 3.1.1 There have been a plethora of inquiries into this type of insurance in recent years. The Australian Senate Economics Committee in 2008, the Victorian Legislative Council in 2010, and the Governments of NSW and Victoria in 2012, have all held or are currently holding inquiries.



3.2 HIA involvement in this area

3.2.1 HIA has made submissions to all of these past inquiries on this topic. Copies of the HIA submissions to other inquiries are available from HIA. Some are on the HIA Website www.hia.com.au.

3.2.2 HIA particularly wishes to draw attention to the Senate Inquiry in 2008, whose terms of reference covered all States, and were:-

“Australia's mandatory Last Resort Home indemnity Insurance scheme, including:

- 1. the appropriateness and effectiveness of the current mandatory privatised last resort Builders Warranty Insurance scheme in providing appropriate consumer protection and industry management.;*
- 2. the reasons for and consequences of the ministerial decisions relating to the removal of consumer protection provisions in respect of Corporations Regulation 7.1.12(2);*
- 3. the ramifications for the future supply of this insurance product following the draft recommendation from the Productivity Commission report released in December 2007;*
- 4. any potential reforms and their costs and benefits which may lead to appropriate consumer and builder protection and improved housing affordability; and*
- 5. any related matters.”*

3.2.3 In that regard, the Senate Committee (majority report) did not conclude that the current builders warranty schemes were inappropriate or ineffective. On the contrary, the Committee found that the schemes did provide consumers with the necessary protection, and specifically rejected suggestions that it be voluntary rather than mandatory. The Senate Committee also rejected calls for this insurance to be a government monopoly. The full recommendations are set out at Annex A.

3.2.4 While those inquiries focussed mainly on the insurance aspects of consumer protection, HIA notes that this is a major topic in the current inquiry. HIA respectfully submits that the findings of the Standing Committee on Finance & Public Administration and the Senate Committee on these terms should be relevant and persuasive in this inquiry.

3.2.5 HIA fully supports the Senate Committee's finding that consumers need the protection of home indemnity insurance and that the cost is not an unnecessary expense. Without it, consumers are exposed to the possibility of catastrophic loss if their builder goes into liquidation with their home unfinished.

3.2.6 HIA also considers that a proper understanding of the nature of the current insurance arrangements, and their role in the dispute resolution process, is first necessary in order to understand how disputes occur and might best be managed.



- 3.2.7 In particular, HIA believes that much of the debate regarding first resort versus last resort insurance is misconceived.

4. The Nature of Statutory Home Indemnity Insurance.

- 4.1.1 Statutory warranties and home indemnity insurance should not be confused as being the same thing. The first is the legal responsibility of the builder (statutory warranties) and the second (insurance) is consumer protection set up to protect against losses where the builder is unable to meet their legal responsibilities due to death, disappearance or insolvency.
- 4.1.2 Statutory warranties are implied in legislation in each State and are the responsibility and obligation of the builder to the consumer. Indemnity insurance has historically been designed to protect home owners from builder default and to act as a safety net for consumers where their builder has died, disappeared or become insolvent. The greatest risk to the consumer, and the greatest area of insurance payout, is loss incurred as a result of non-completion of their project.
- 4.1.3 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 regulator/licensing body. 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. One of the major reasons for the demise of the Housing Guarantee Fund in Victoria and the NSW Building Services Corporation was exactly this confusion of roles.
- 4.1.4 Also, the differences between this form of insurance and other insurances are important. Warranty insurance 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). In this case the policy cover is against events such as builder disappearance or insolvency that are to a considerable extent within the control of the builder themselves. Similar considerations apply to first resort insurance and professional indemnity insurance. This aspect needs to be addressed by proper risk assessment as well as by existing licensing controls.
- 4.1.5 A large part of the reasons for consumer complaints about home indemnity insurance in the past was again the false perception that home indemnity insurance was insurance against workmanship defects. From the insurer's point of view this was irrelevant, because it was the builder's responsibility to rectify workmanship faults; what counted was the risk that the financial stability and capital resources of the builder were insufficient to ensure they could meet these responsibilities.
- 4.1.6 That was the risk that was being insured, and builders which had insufficient capital as a proportion of work outstanding, or which had opaque financial and management information systems, were not seen by insurers as good risks. Such builders were therefore limited in the risk coverage which insurers were prepared to extend to them.
- 4.1.7 The results have been that, as compared with the industry pre-1997, home builders as a group are much better capitalised and also have better financial management structures. This has led to far fewer financial collapses by home builders since 1997 as compared with the past. It has effectively ensured one



of the objectives identified by the Consumer Affairs Officers in 2002, that of consumer confidence in the industry.

- 4.1.8 HIA considers that it is important for industry stability that insurers continue to assess risk and insure builders accordingly. This prevents entry into the market of builders who have no sufficient financial capacity to comply with their obligations under the Act, and who are likely to go into liquidation with substantial adverse affects on consumers.
- 4.1.9 It is HIA's experience that the problems of information asymmetry referred to at p.13 of the Issues Paper are eminently manageable. HIA has worked closely with HIA Insurance Services in developing assessment tools for builder risk rating, which have been very successful. Although this is long tail insurance, experience over the last ten years since the collapse of HIH Insurances and FAI Insurances has seen the progressive refinement of the risk assessment system.
- 4.1.10 HIA considers that there is ample capacity in the private insurance market to support the continuance of this type of insurance.
- 4.1.11 Factors affecting the entry of competitors into the marketplace include the size of the market, the availability of a strong brokerage network, the availability of an insurer's own strong internal risk assessment mechanisms specifically adapted for this market, and the overall strength and level of activity of the home construction market.
- 4.1.12 This type of insurance is long tail, and as such represents an area of enhanced risk for insurers. Although claims must be brought within 6 years of practical completion, it is very difficult for insurers to foresee costs many years in the future and price appropriately.
- 4.1.13 As such home indemnity insurance is relatively commercially unattractive to insurers when looked at in isolation. As part of a comprehensive suite of insurance products offered to home builders, it plays an important part, and HIA understands that most insurers look at it in this light.

4.2 Competition Issues

- 4.2.1 In these circumstances, an important issue for the Government to consider is whether premiums should be set on a commercial basis having regard to the risk profile of individual builders or whether all builders are to be treated as equal risks and charged premiums based solely on the value of work done, as in Queensland.
- 4.2.2 HIA considers that the Government should retain a scheme which entitles builders to any level of warranty coverage they want with premiums set by the insurer based on risk, turnover and performance. It is important that individual builder ratings are maintained to reward good (low risk) builders who operate sound and well capitalised businesses, and ensure that they do not cross-subsidise poor risks. Given a reasonable degree of competition in the insurance market, this is not unfair or unreasonable.
- 4.2.3 Equally importantly, a flat (one size fits all) rate promotes an environment conducive to undercapitalised businesses undertaking larger volumes of work, funded through anticipated future cash inflows. This, in itself, presents an unacceptable business risk to the Government's underwriting arrangements.
- 4.2.4 Factors including gross margin, net tangible worth, costing systems, debtor collection and creditor position can point to an inherent level of risk and potential solvency threat. Ultimately, consumers pay the cost of this warranty



insurance and accordingly risks need to be properly priced to avoid upward pressure on policy premiums.

- 4.2.5 Over recent years, most builders have managed their businesses in a positive way, ensuring profits are retained so that adequate capital exists for less buoyant construction periods. Builders have been rewarded through the benefits of better business practices and results, and also from a differentiated premium which rewards those results. Maintaining risk based premium settings provides an important and ongoing incentive.

4.3 Are home indemnity insurance premiums set at a reasonable level?

- 4.3.1 HIA considers that the only way Government can be assured that premiums paid by consumers are set at a reasonable level is to allow them to be set in a free and fair competitive market. In such a market, premiums will fluctuate but over time will be set by insurers as low as is feasible having regard to risk experience and actual costs. Prices set by government monopolies such as in Qld will over the long term always be higher than those set by a free market.
- 4.3.2 Given the standardisation of product, as noted above, the only way such market-set premiums can be reduced is to reduce the costs of administration, and especially the costs of dispute resolution.

5. Last Resort versus First Resort Insurance

- 5.1.1 Both consumer and builder critics of the current WA scheme have pointed to Queensland's 'first resort' insurance scheme administered as a statutory monopoly by the Queensland Building Services Authority (QBSA) as an attractive alternative. However the Qld scheme needs to be looked at as a whole.
- 5.1.2 To categorise the Qld scheme as 'first resort' is not entirely correct. Just as in other States, QBSA, Fair Trading 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 QBSA home indemnity policy insurance is triggered. This represents the vast majority of insurance payouts in all States and Territories.
- 5.1.3 However, unlike other States, where a Qld licenced builder refuses to rectify work that QBSA considers is defective, QBSA will complete the work and pursue the builder for the cost. This is facilitated by QBSA 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 QBSA Act to pay for insurance debts, costs of doing work and fines, as an incident of licensing.
- 5.1.4 HIA considers that this process also involves a conflict of interest, not to say obvious moral hazard; any work the QBSA can force a builder to do is work that it will never have to pay out on one of its insurance policies.

5.2 Natural justice

- 5.2.1 There are also significant issues of natural justice. Under current QBSA dispute resolution processes, inspectors issue contractors formal directions to rectify, after conducting a telephone "mediation" and short site visit without even first giving the contractor a written request to rectify the allegedly defective work. There is no requirement for the direction to be 'reasonable'.



- 5.2.2 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 QBSA decisions that their work is defective and must be rectified.
- 5.2.3 Where the builder disputes the QBSA's assessment, the matter will be resolved by the Qld Civil and Administrative Tribunal, but in the meantime the consumer is relieved from having to pursue the builder and the work in dispute is rectified by the QBSA at no further cost to the consumer.
- 5.2.4 It will be seen that the essential difference between the Qld scheme and most other States' 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.

5.3 Cost comparisons

- 5.3.1 While direct comparisons may be inexact owing to the differences in cover and the fact that in WA premiums vary with the builder, evidence presented by HIA to the Senate in 2008 demonstrated that the premiums under the QBSA scheme have historically been much higher than those in other States. This disparity still remains - as a current comparison, a \$200,000 home building contract would cost \$1994.55 to insure in Qld, while typical prices in WA would be below half this.
- 5.3.2 There are a number of other difficulties with the Queensland system. Builders find that on the issue of whether or not work is defective, the QBSA is accuser, judge and jury. While this is of course advantageous for the individual consumer complainant, from an industry perspective, builders in Qld 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 QBSA ruling on workmanship is in many cases prohibitive.
- 5.3.3 Thus there is some additional cost burden to the Queensland industry (which must eventually be paid for by Qld home owners) which is not incurred in WA, where only the SAT determines, after a fair hearing, whether building work is defective.
- 5.3.4 Also, the overall high degree of regulation in Qld has associated administration costs for both Government and business, which is a hidden cost ultimately borne by home buyers (as the QBSA is required to be self-funding).
- 5.3.5 The QBSA, 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 QBSA. 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.
- 5.3.6 The QBSA offers the same insurance premium to all builders irrespective of the builder's past record for poor work. There is therefore no price incentive to maintain a good building record. As the QBSA does not discriminate for insurance, the QBSA has introduced complex reform after complex reform in recent years to allow it to ban builders from holding a licence for, among other things, financial failure or grossly defective work.
- 5.3.7 QBSA combines the roles of insurer and licensor of builders. In that regard it has a conflict of interest, 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.

- 5.3.8 That this is not a theoretical aspect of home indemnity insurance is shown by the fact that, except in Queensland, the number of occurrences of home builder collapses, and their cost, has significantly declined in the last 10 years in States with private insurance. In HIA's view, this is very substantially due to the risk assessment carried out by underwriters and the limiting of insurance cover on the basis of that risk. Arguably this has been a more successful way of managing the industry than the Qld licensing model.
- 5.3.9 QBSA'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 \$3300 on the roof of a strata title property is required by the QBSA 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 home indemnity 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.
- 5.3.10 HIA notes that evidence given to the Senate inquiry by HIA Insurance Services was that the most comparable state to Queensland in terms of residential building activity would probably be Victoria, but the total cost of the Queensland scheme is 2 to 3 times that of Victoria, even though Queensland's total building activity was only 5 to 10% higher at that time.

5.4 Benefits comparisons - Minimum insurable values

- 5.4.1 It is also misleading to consider it as a benefit that "the Queensland scheme stands out as one in which the need for insurance is triggered even for relatively low values of work and one in which the maximum payable value from an insurance policy is relatively high" (p.10 of the Issues Paper). As explained above, the low values of work for which policies are required in Qld combined with the minimum policy premium is merely a revenue-raising device as in such cases the premium considerably exceeds the cost of the risk.

5.5 Benefits comparisons - Maximum Payable Values

- 5.5.1 HIA points out that the high payable value in Qld quoted in the Paper is incorrect - it is actually \$200,000 for non-completion and a further but separate \$200,000 cover for post-completion defects, and the chances of anyone being able to scoop the pool for the whole \$400,000 are quite remote. In HIA's experience the \$200,000 cap is very seldom reached in either case.
- 5.5.2 If that is so, Qld consumers are arguably paying the QBSA for some insurance cover that they do not really need.
- 5.5.3 In any case a higher payable value does not mean that consumers receive higher payouts – it is simply a cap, not necessarily a benefit. As consumers' loss is the cost of rectifying any defects, or the cost of completing an incomplete home less any progress payments the consumer still has to make, the total value payable under the policy will always be far less than the total



cost of the home. However the relationship between the contract value and the actual loss is by no means a direct one.

- 5.5.4 It should be borne in mind that any increase in the cap, as it increases the insurer's risk to a small extent, will correspondingly increase prices by a small amount on all policies, while being of use in only a very few. This is an aspect of spreading the costs to all owners of relatively rare disasters affecting only a few, which may or may not be acceptable in the circumstances.
- 5.5.5 On the other hand there could be cases where a cap which is set too low is largely used up in completing the home, leaving little headroom for claims by any subsequent purchaser if defects become apparent up to 6 years later.
- 5.5.6 On that comparison, the present \$100,000 overall cap in WA, when compared to the price of an average home building contract, is by no means unreasonable.
- 5.5.7 HIA is not aware of any problems having arisen with the existing level of cap in WA. While HIA accepts that any purely monetary amount in legislation must inevitably require periodic reconsideration and possible updating to reflect changes in value of money over time, this should not necessarily move in line with the CPI, as home building costs have in the past not moved in any obvious relationship with CPI.
- 5.5.8 HIA does not support caps based on percentages. The costs are harder to assess on an actuarial basis and they impose a cost on all home builders for the benefit of those building more expensive homes. Arguably, where losses exceed the current \$100,000 cap, the consumer is constructing an unusually expensive house and might be able to bear losses in excess of the cap more easily than a consumer constructing a more modest house. The scheme after all is meant to be a consumer safety net.
- 5.5.9 The additional moral hazard involved with percentage caps is also an important consideration in any proposals to alter existing scheme caps.
- 5.5.10 In cases where the loss exceeds 20% of the contract price, the builder would have been paid so much in advance that the owner knew or should have known it was making large payments for work not yet done, and thereby undertaking a considerable risk, which is wholly within the owner's control and not the insurers'.
- 5.5.11 The only other explanation for a non-completion claim exceeding 20% of the contract price would be a situation where the contract was so grossly underpriced that either the owner knew or should have known that to be the case, and the owner is in the position of making a windfall gain by getting building work completed by the insurer to a value far in excess of what the owner had agreed to pay under the contract.
- 5.5.12 For these reasons, and also to protect the viability of the scheme, and so that it is more clearly directed towards consumer protection rather than delivering windfall benefits to consumers, HIA considers that the Government should not alter the current cap. HIA considers that the cap could not be increased without having an unfavourable effect on current premiums and without making the product less attractive for insurers to offer.

5.6 Problems of Pure First Resort Schemes

- 5.6.1 For the reasons set out above, HIA considers that the only material difference between Queensland's so-called 'first resort' and so-called 'last resort' schemes lies in dispute handing.



- 5.6.2 A genuine first resort insurance scheme managed by insurers, with insurers required to pay out on all 'confirmed' claims and attempt to recover from builders, but without the power to suspend or revoke builder licenses, 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.
- 5.6.3 Insurers experienced loss ratios in excess of 300% under previous first resort schemes. Under the previous first resort scheme homeowners were able to claim against an insurer if there was a breach of statutory warranty, regardless whether the builder was still in business. The insurance cover was activated usually by a termination of the building contract.
- 5.6.4 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.
- 5.6.5 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. The emphasis should be on correcting the dispute resolution process and continuing to provide a last resort safety net.

6. Government as a Bearer of Risk

- 6.1.1 In principle, HIA considers that the private insurance market should bear all of the risks of home indemnity insurance. However this may not be practicable. HIA notes that the Governments of both Victoria and NSW are actively involved in the provision of home indemnity insurance, albeit with different degrees of risk to that in WA. In Qld, the Government is the initial bearer of risk but much of this is reinsured with the commercial insurance sector.
- 6.1.2 In relation to the indicia of market failure set out at p.16 of the Issues Paper, HIA considers that most are present to some degree in the home indemnities insurance market
- 6.1.3 *Information asymmetries* include the fact that consumers contract for a house to be built once or twice in a lifetime, and cannot be expected to have the information level of a professional licenced builder. Also, consumers cannot know the financial condition of the builder and are thus vulnerable to builder insolvency. However, as stated above, HIA does not consider that it is difficult for insurance companies to set premiums at an appropriate level.
- 6.1.4 *This is a non-competitive market* only to the extent that the product is standardised by a Government agency and competition can occur only in relation to price and service levels. In some States (NSW, Qld) the price is also fixed by a Government agency. However, HIA considers that this is not a market with a natural monopoly – there is no structural reason why perfect competition could not occur, at least on the retail side.
- 6.1.5 *Externalities* exist in that the insurance is for the benefit not only of the owner under the building contract but their successors in title. Protection of subsequent purchasers is an important consumer protection measure linked to building approvals and inspections.
- 6.1.6 *Public Goods* however do not seem to be involved as a characteristic of the home indemnities insurance market.



- 6.1.7 History has shown that without some government involvement to make insurance compulsory and regulate its provision, consumers would largely not purchase home indemnity insurance and the costs of builder insolvency will fall very unequally, often on governments themselves by way of rescue packages when a licensee becomes insolvent.
- 6.1.8 Nor would insurers be prepared to sell into a market where consumers and builders can choose what risks to insure and thus select against the insurer. The withdrawal of insurers from the Tasmanian market once it became voluntary is an example of this. It is not just a decrease in demand but a loading up of insurers with bad risks that is an inescapable consequence of making insurance voluntary. Under the current WA scheme, some of this bad risk would necessarily fall on the WA Government.
- 6.1.9 However, HIA is not convinced that the operation of the WA Government in this market by way of bearing part of the risk is a significant factor on the price at which insurance is sold. HIA notes that the price of insurance in WA is comparable with the price in other States such as Victoria where the Government bears none of the risk, and in NSW where the Government bears all of the risk.
- 6.1.10 HIA considers that the public benefits of home indemnity insurance justify the involvement of Government in this particular market, if that is the only way it can continue to operate.
- 6.1.11 HIA has no information as to whether the State Government is being adequately compensated for the risks it currently holds. That is a commercial question for negotiation between the Government and insurers.

7. Mandatory Requirements and Consumer Choice

- 7.1.1 As discussed above, as an organisation committed to free enterprise and open competition, HIA supports maximum consumer and industry choice. Therefore HIA's national policy is that home indemnity insurance should be voluntary.
- 7.1.2 HIA also acknowledges that if it were voluntary, it would probably be purchased by relatively fewer consumers, principally the wealthier and better informed who are least in need of protection. The contraction in market size and opportunity to select against the insurer means that, as in Tasmania, it may cease to be offered as an insurance product.
- 7.1.3 The disinclination of consumers to purchase such insurance stems from their lack of information and natural inclination to minimise costs on what is a very major and expensive purchase. And no home buyer would be prepared to spend extra for coverage for subsequent purchasers.
- 7.1.4 As discussed above, without insurers restricting home building activity to those builders who are acceptable risks for the amount of work undertaken, the market would be open to entry to those who do not have sufficient financial and material resources to meet their obligations under the Act. This would create unfair competition and lead to a greatly increased number of builder collapses.
- 7.1.5 In these circumstances of information asymmetry and potentially catastrophic loss from builder insolvency, death or disappearance, it can be argued to be in the interests of society as a whole for compulsion to be maintained.
- 7.1.6 If it is to be maintained as compulsory, it would be administratively inconvenient and much more costly for consumers if they and not builders were to be required to take out the insurance policy.



- 7.1.7 HIA notes in passing that it is not just an information asymmetry issue - most insurance claims arise from insolvency, not workmanship issues, and therefore the analysis at the bottom of p18 of the issues paper is misdirected. There is no way consumers can know in advance that the builder is going into liquidation before completion – in most cases not even the builder can know that.

8. Dispute Resolution Procedures

- 8.1.1 HIA notes that the issues paper does not specifically focus on dispute resolution but this is an essential aspect of the working of the insurance model.
- 8.1.2 HIA considers that an effective dispute resolution process relating to the performance of home indemnity should have the following features:
- 8.1.3 *easy to understand, and simple to invoke and operate;*
- 8.1.4 *affords natural justice;*
- 8.1.5 *resolves disputes in as efficient and effective a manner as is possible (including being able to readily identify at the outset, the threshold question as to whether or not a “defect” warranting further action exists); and*
- 8.1.6 *involves procedures (including procedures relating to the enforcement of any judgment that is handed down) that are both expeditious and guarantee due process.*
- 8.1.7 HIA supports effective even-handed administrative dispute resolution procedures, including ADR (binding where agreed), followed where necessary by referral to a specialised, knowledgeable, independent building jurisdiction (whether that be a tribunal or division of the courts).

9. Alternative Regulatory Approaches

9.1 Voluntary Home Indemnity Insurance Scheme

- 9.1.1 For reasons set out above, HIA considers that a voluntary scheme is unlikely to meet the government’s consumer protection objectives.

9.2 A First Resort Scheme

- 9.2.1 For reasons set out above, HIA considers that a true first resort scheme is unworkable. Likewise, a scheme based on the Qld model is undesirable, and likely to greatly increase premiums and costs to consumers overall. It is also likely to involve very significant initial expense for the WA Government in creating a greatly enlarged regulator with an integrated insurance arm.
- 9.2.2 HIA disagrees that first resort schemes on the Queensland model offer a greater level of consumer certainty and protection than do last resort schemes.

9.3 A National Scheme

- 9.3.1 Logically, a national scheme based on uniform State and Territory legislation could not exist until uniform national builder licensing has been implemented, and even then, State differences in regulated building contracts and dispute resolution mechanisms will remain, reinforced by differences between State judicial systems.
- 9.3.2 HIA considers that while such an idea is economically attractive in principle, and would be welcomed by insurers, it is not practically achievable in any reasonable time frame. While there has long been a good level of co-operation and information sharing between States in the consumer protection area, no



State has even taken up the simple idea (proposed by the Senate in 2008) of a nationally harmonised scheme of detailed reporting of Domestic Building insurance, to allow meaningful interstate comparisons.

- 9.3.3 The intense and unforeseen difficulties encountered with other recent proposals for national uniformity of State laws suggest that WA should not defer any needed reform of its own scheme at this stage, or expect that a national home building insurance scheme could be developed (for example under COAG auspices) in the foreseeable future.

9.4 Separation of the Insurance Product

- 9.4.1 HIA completely disagrees with suggestions that separating the two areas of coverage in a home indemnity insurance policy would lead to simplicity or cost savings. This could only result in increased transaction costs and additional arguments about which policy should apply in a particular fact situation. Consumers would not be aided by widening the area of legal dispute available.

9.5 Annual policies

- 9.5.1 The HIA has been a constant critic of the use of annual policies, in particular annual PI policies, since they were first mooted.
- 9.5.2 The principal problem with annual professional indemnity policies is the lack of a guarantee of cover through the warranty period. Further, the use of PI policies gives rise to additional consumer protection concerns.
- 9.5.3 Despite HIA's opposition to the accreditation of professional indemnity policies in NSW and Victoria prior to the commencement of the private warranty schemes, these products were endorsed by the regulatory authorities. The regulatory authorities seemed more intent to encourage competition against the HIA-endorsed Home Owners Warranty scheme, which eschewed professional indemnity policies in favour of job-specific insurance policies issued in the name of the home buyer.
- 9.5.4 Because the annual professional indemnity policy did not cover the consumer for the long-tail warranty, some insurers and brokers were able to offer builders the superficial attraction of an initially lower premium relative to the alternative job-specific policies, which covered the full statutory warranty. Both FAI and HIH were able to grow aggressively their market share of Home indemnity insurance in NSW and NSW on the back of the deficient, annual professional indemnity policies.
- 9.5.5 The preponderance of annual professional indemnity policies issued by FAI and HIH in NSW and Victoria made the task of identifying home buyers affected by the collapse of HIH considerably more cumbersome and costly than it needed to be. Many builders who had purchased the "cheaper" professional indemnity policies from FAI/HIH were faced with having to purchase run-off cover for the balance of any warranty period. With existing insurers unwilling to provide "run off" cover, the NSW and Victorian Governments decided to extend their HIH rescue schemes to cover clients of builders with existing professional indemnity policies.

9.6 Problems with annual policies

- 9.6.1 The major problem with annual cover is that policies are issued on an annual basis, and the current policy only covers claims in the current year. There is no cover in place for the balance of the warranty period. That has to be arranged, and paid for, each year during the warranty period.



- 9.6.2 Put simply, the insurer is not bound to cover the insured for more than the current year, with the consequent enormous uncertainty as to whether cover will be available for the whole warranty period.
- 9.6.3 Also, there are enormous practical difficulties in ensuring that continued renewal happens. It is simply not possible to effectively police.
- 9.6.4 Because of this, in many cases renewal will not occur, and homeowners will be left without cover during the subsequent years of the warranty period. This has actually occurred recently in NSW, with a builder changing to job specific insurance and leaving approximately 170 jobs uninsured.
- 9.6.5 Examples of likely/actual problems are:
- the builder just decides to not keep getting insurance;
 - the annual insurer decides not to renew, and no other insurer agrees to continue to insure;
 - the annual insurer decides to increase premiums, and the builder just switches to job specific insurance without obtaining and continuing run-off cover;
 - the builder goes into liquidation, and the liquidator disclaims responsibility to continue to renew the policy;
 - owner-builders will take out an annual policy for the year they sell the property but, once the property is sold, they simply will ignore their obligation to renew.
- 9.6.6 The Victorian Ministerial Order for PI insurance attempted to address some of these enormous practical difficulties.
- 9.6.7 For example, one section in the previous Ministerial Order states that, if a builder becomes insolvent, cover continues for the balance of the warranty period. But this does not address all the above problems, nor does it ensure all homeowners are covered. If the builder has been uninsured because no-one will insure, and then goes broke, there is no existing cover to automatically run on.
- 9.6.8 Also, and remarkably, under the Order, the run-off cover could cease if a PI insurer pulls out of the Home indemnity Insurance market. If they do decide to back out of their schemes, homeowners will be without cover.
- 9.6.9 From the builder's perspective, annual policies also present major issues. If the insurer decides on a massive premium increase, the builder will likely have little choice but to pay it. If the insurer refuses to renew, again the builder will be in difficulty, as it seems unlikely that another insurer will want to undertake the risk.

9.7 The benefits of job specific cover

- 9.7.1 As opposed to the problems of annual policies, job specific policies have extremely significant benefits which annual policies do not, particularly:
- 9.7.2 Job specific insurance is in the name of the owner, and thus provides easy access for the owner to the insurer if a claim eventuates.
- 9.7.3 Job specific insurance has far greater capacity to protect consumers and the industry from builder failures, because it gives the insurer the ability to cancel the eligibility of recalcitrant builders.
- 9.7.4 Annual insurance does not have this flexibility. A builder can continue to trade delinquent for months (in fact, for up to a year!) until the policy comes to an end. The insurer cannot cancel the annual policy, because the *Insurance*



Contracts Act does not allow cancellation on the basis that the risk deteriorates. An insurer therefore might be aware that a builder was in grave danger of collapsing, and yet be totally powerless to prevent it from continuing to enter into contracts and thus prejudice consumers, as well as the insurer itself.

9.7.5 With job specific cover, however, the insurer is able to refuse to provide further covers. The insurer can make underwriting decisions virtually on a daily basis taking into account such factors as:

- number of jobs undertaken (any sudden increase in job numbers is a sign of danger);
- the price of each individual contract, as compared to the builder's average price, and the industry average (signs of danger are under costing as compared with these averages, or a builder taking on a contract out of its league, such as the case of an \$80,000.00 house builder taking on a \$500,000.00 job);
- progress payment anomalies;
- industry feedback;
- consumer complaints; and
- other information as to deterioration of financial viability..

9.7.6 Thus, the underwriting practices associated with job specific cover are an important driver to weeding out the unacceptable builders. They better protect consumers from builder crashes.

9.7.7 This is very important, as even the most comprehensive insurance is never the complete answer if a builder crashes. The owner still suffers anxiety and stress, and delay in completion of their home. It also inevitably costs them a considerable amount of their own time.

9.7.8 Not only the home buying public, but also the insurers, have an obvious interest in minimising builder failures. So does the Government, in order to minimise political fallout and to preserve the efficacy of the legislated scheme.

9.7.9 Government, insurers and the home buying public accordingly all have an interest in the use of job specific insurance because it provides the best drivers for maintaining sustainability in the industry.

9.7.10 It must be noted that, as in WA, the schemes which have operated successfully, and with little or no consumer backlash, for many years (that is, SA since 1985, ACT since 1988 and Tasmania 1992 - 2009) all only allow for job specific cover. It is a proven product.

9.8 Which type of policy will cost more in the long run?

9.8.1 It has been baldly asserted that job specific cover is more likely to result in serious premium escalations down the track, as compared with annual cover. The assertion has been made without any statistics or facts to support it, and has not proven to be the case after many years' experience of such schemes.

9.8.2 Should the passage of time after the issue of a policy indicate that costs associated with the risk are higher than forecasted, on what basis can it be suggested that those issuing job specific policies will increase their premiums, but if everybody was issuing annual policies, they would somehow react differently? The suggestion ignores the commercial reality that increased claims costs will drive up premiums across the board.

9.8.3 Also, job specific cover is paid for up-front. There is no extra cost to be paid for that specific cover at all. If it should prove that costs associated with that risk



escalate down the track, the insurer has no ability to get further money out of the original insured. It can only escalate its premiums for future covers.

- 9.8.4 On the other hand, the insured dealing with an annual insurer does not know its final total price for the cover on a particular home until the warranty period ends. It is stuck with any cost escalation over that period.
- 9.8.5 Bald assertions of likely significant cost escalations over time with job specific policies is completely at odds with the interstate experience over the last 12 years (20 years if you also look at the experience of the SA voluntary scheme which operated from 1977). The simple fact is that policy premiums for job specific cover have remained stable in one of the world's most mature Home indemnity insurance markets.

9.9 Concerns associated with PI insurance

- 9.9.1 The PI version of the annual policy is fraught with even more difficulty. PI suffers from the following further major disadvantages:
- Professional indemnity is a style of policy that gives a professional person cover against their own negligence. Such a policy does not really work as a driver to get builders to live up to their contractual and warranty responsibilities. It is a species of moral hazard for builders facing cost pressures.
 - Any payout under the PI policy must be forwarded to the builder. There is a risk that the builder will get the cheque, cash it, but not use it to fix the work, or not fix the work properly.
 - Another possibility is that the builder goes into liquidation, and the liquidator claims the right to take the insurance monies.
- 9.9.2 The Commonwealth *Insurance Contracts Act* radically altered the law of insurance to give numerous protections for an insured. Examples of the protections given in that Act are:
- *provision of notices setting out the insured's rights*
 - *restrictions on insurers avoiding claims because of late notice, or because of failure to preserve through doing further work and so on (s.54, Insurance Contracts Act)*
 - *insurer's obligation to notify of unusual terms.*
- 9.9.3 Because the owner is not the insured under PI insurance, they do not have these, and other, very important rights. For example, the insurer could refuse a homeowner's claim on the basis that the builder was in breach of its duty of good faith, or had affected its subrogation rights.
- 9.9.4 Convoluted provisions in the Victorian Ministerial Order which purport to preserve the important protections in s.54 of the *Insurance Contracts Act* as if the owner was the insured, rather than the builder, are artificial and untested. They are also likely to lead to much litigation.
- 9.9.5 Most importantly, on our legal advice, they are likely to be completely inadequate in securing the same protections for homeowners as they enjoy as "insureds".

9.10 Fidelity funds

- 9.10.1 In May 2002, the Western Australia Government released the draft Home Building Contracts Amendment Bill 2002 for comment.



- 9.10.2 The purpose of the Bill was to harmonise the relatively few legislative provisions needed to achieve consistency with the Victorian and New South Wales reforms, in particular, the introduction of a \$10 million cap on Liability in relation to home indemnity / warranty insurance.
- 9.10.3 The Bill also introduced provision for approved mutuals or similar funds, with the intention of Government to build competition in the home indemnity / warranty market.
- 9.10.4 However, in response to concerns raised by the industry and community, the Government subsequently announced the provision of the Bill relating to mutuals would be amended to require:-
- Funds not regulated by APRA (either because the fund is considered to not provide insurance or APRA makes a determination that the Act does not apply) will require approval of a regulatory regime established by the State Government;
 - The regulatory regime will require a detailed independent financial and actuarial assessment to ascertain the viability of the proposed fund;
 - Any competitive advantage, due to the fact that the fund is not regulated by APRA, is to be offset by the regulatory regime; and
 - The funds will no longer be exempt from the requirement for adequate excess of loss insurance.
- 9.10.5 The amendments to the *Home Building Contracts Amendment Bill* clearly illustrates the commitment of the Western Australia Government to creating a sustainable home warranty market without compromising the fundamental requirement for consumer protection.
- 9.10.6 HIA is concerned that funds that do not comply with the requirements of APRA may not provide the level of protection to builders and consumers that the current APRA complying private warranty insurers provide.
- 9.10.7 The United Medical Protection Fund that recently collapsed in Australia is an example, as is the New Home Warranty (NHW) Fund in Canada which collapsed in 1999. NWH was established by the Canadian Home Builders Association of British Columbia as a “non profit” venture. It operated in competition against insurance policies sold by underwriters and captured a large share of the market.
- 9.10.8 On the basis of historical claims history NHW believed it had accumulated significant annual operating surpluses. NHW had set aside a “reserved fund” but did not have appropriate re-insurance protection or catastrophe cover.
- 9.10.9 In the late 1990’s numerous claims arose in British Columbia over damage caused by water ingress to between 300-600 residential buildings, resulting in the collapse of NHW.
- 9.10.10 The collapse became known as the “leaky condo crisis” with direct repair costs of around \$500-\$800 million and an ultimate cost to British Columbia of over \$1 billion dollars. This was a major catastrophe for their economy and the Government was forced to implement a relief program of providing grants and interest free loans to homeowners to assist in meeting the cost of repairs
- 9.10.11 Litigation is still ongoing against designers, architects, engineers, contractors as well as the municipal authorities that approved the building works resulting in the restricted availability of Professional Indemnity Insurance.
- 9.10.12 The NHW model is now internationally recognised as being flawed and British Columbia has subsequently passed the *Homeowner Protection Act*, requiring



home warranty insurance to now be prudentially regulated by the Canadian Financial Institutions Act, the equivalent prudential framework to that which APRA operates in Australia.

9.11 Concerns with the introduction of a Fidelity Fund

9.11.1 Fidelity Funds enable an insurance product to be offered to consumers, however in HIA's view they do not provide the same level of consumer protection to that provided by an insurance policy subject to APRA scrutiny.

9.11.2 Fidelity Funds are considered inherently flawed, in that they:

- Enable an inappropriate and prudentially deficient entity, ie. a mutual fidelity fund, to offer what is effectively an "insurance product" to consumers and carry on an "insurance business";
- Operate outside of the established prudential framework for insurers and insurance business which is nationally regulated by the Australian Prudential Regulatory Authority (APRA) and Commonwealth legislation including the *Insurance Act 1973*, the *Insurance Reform Contracts Act 2001* and the *Insurance (Agents and Brokers) Act 1984*;
- Do not guarantee that the prudential regulation of "insurance business" and "fidelity fund schemes" will be of equal standard to that which applies to "approved insurers" and "residential building insurance policies"
- Establish single product funds to small isolated markets and hence lose the ability to spread claims losses across other product lines and other States
- Create an anti-competitive market environment, where the Funds will have a significant trading advantage over the other insurance businesses which are compelled to satisfy the full prudential requirements and scrutiny of APRA.
- Resulting in monopoly arrangements for the Funds, with two major Warranty providers have already indicated their intention to withdraw from the markets in which the unregulated funds operate, due to this unfair competition..

9.11.3 The establishment of fidelity funds in HIA's view would disregard the prudential standards introduced under the *General Insurance Reform Act 2001*, and would appear to compromise the sustainability of the funds and consequently the fundamental requirements for the actual consumer protection that the warranties are supposed to afford home owners.

9.11.4 HIA contend that the funds carry on "insurance business" in that they provide coverage to consumers in accordance with respective home indemnity / warranty legislation and in competition with other private insurers.

9.11.5 HIA recommends that any proposed fidelity funds should be thoroughly investigated by APRA and if deemed "insurance business", should be subject to full APRA scrutiny and compliance with the Prudential Standards introduced under the *General Insurance Reform Act 2001*.

9.11.6 Another major concern with the fidelity fund is that the fund does not have the ability to place any sideways or layered portfolio reinsurance protection, therefore the fund is unable to adequately sustain multiple builder failures to Probable Maximum Loss in the portfolio, which could ultimately lead to failure of the fidelity fund.



9.11.7 The failure of any one of the largest ten builders in WA due to their turnover size, geographical spread and number of dwellings under construction from a Probable Maximum Loss scenario would equal the maximum liability of the fidelity fund.

10. Subsidence Insurance

- 10.1.1 The subsidence insurance currently available in Qld is a form of additional home structural insurance undertaken by the QBSA in its own right for 6 years after completion. It is designed to address specific climatic and geological conditions in Qld which find little direct parallel in WA.
- 10.1.2 HIA does not consider that there is a case for the introduction of such insurance in WA.
- 10.1.3 So far as HIA is aware, there is no significant subsidence problem in WA home building. HIA notes that a very high proportion of WA homes are built on sand plane where adequate site classification procedures exist.
- 10.1.4 Although described as 'no fault', this is so only from the consumer's point of view - where the QBSA decides that the builder is at fault, the QBSA will direct them to rectify, which may trigger the builder's (or architect's or engineer's) own PI insurance. In the case of landslip there is potentially a claim against the product liability section of a builder's contract all risk policy where a specific event has caused the product to fail.
- 10.1.5 If the builder fails to rectify, is bankrupt, disappeared, etc, then as with other defective insured building work the BSA will pay under the insurance policy for the work to be done and backcharge the builder if he is still available. The BSA does also actively pursue engineers and land developers for recovery of its costs for subsidence claims. But it is an expensive process and a lengthy one.
- 10.1.6 The above process is more or less the same as in other States and Territories. On the other hand, where the QBSA decides the subsidence is an act of nature, it will pay for repairs to be done without backcharging or pursuing the builder or other party.
- 10.1.7 HIA understands that this is proving to be a very expensive part of the BSA's insurance arrangements – in 2010-11 there were \$10.8m in subsidence claims, \$14.6m for defective works and \$13.7m for non-completion
- 10.1.8 By contrast, subsidence is at present in WA a warranty issue and not an insurance issue. Where subsidence occurs within 6 years after completion, as a result of faulty design and/or construction, and causes a structural defect in breach of a statutory warranty, the home indemnity policy will respond if the builder does not (by reason of death, bankruptcy or disappearance). Therefore the issue is whether the statutory warranty has been breached.
- 10.1.9 Currently, disputes arise over subsidence where consumers try to prove builder fault (and thus within policy coverage) while builders point to architect's design faults, inadequate engineer's reports, and consumer actions such as over-watering and tree planting that have resulted slab movement. Such possibilities do not include acts of nature or other causes such as collapse of forgotten mine shafts which are truly unforeseeable. In HIA's experience, proof of causation is often very difficult, where experts will frequently disagree, and the cost of a thorough exploratory excavation and investigation is unaffordable by consumer litigants.



- 10.1.10 From the point of view of consumers, the arguments in favour of creating new subsidence insurance benefits where the builder is not at fault are thus readily understandable.
- 10.1.11 HIA accepts that where subsidence defects arise during the first few years of a building's life they may not be the fault of anyone but the result of unforeseeable natural processes. Such defects are very uncommon but are usually very expensive to rectify, and arguably should not be imposed on a consumer whose new house may have been rendered uninhabitable by the subsidence. The average new home owner would be unlikely to have, or to be able to borrow, the funds to make the necessary repairs.
- 10.1.12 In such cases, arguably some form of pure subsidence insurance (as opposed to insurance covering breach of builders' warranty) should be available to assist the consumer in what is almost always a catastrophic situation.
- 10.1.13 The situation is not however quite as simple as in Qld, where the QBSA insurer is also the judge of whether the builder is liable for breach of warranty or not. In WA any pure subsidence insurance would respond only in cases where there was no breach of warranty. Therefore insurers would have to decide this warranty issue, and so become involved in dispute resolution processes where the builder is still available.
- 10.1.14 A dispute resolution process is logically separate from the insurance process and that dispute resolution should be the responsibility of the government regulatory body. In principle, Governments should look after disputes and insurers should look after the safety net. Therefore introduction of pure subsidence insurance will raise difficult issues for insurers.
- 10.1.15 In addition, if insurers were required to extend this cover, it would be difficult to price the risk, and they would be likely to require builders to obtain geotechnical reports on a block by block basis at an additional cost of up to \$3000 per block.
- 10.1.16 All this would have a cost to all consumer home builders, and may be something insurers would not readily wish to undertake. The Government should be hesitant before adopting anything that reduces affordability and discourages insurers from entering or remaining in this market.
- 10.1.17 HIA also cautions that in this area, as in others, there must be careful attention given to what is a defect and what is something within normal tolerances arising out of industry custom and practice. Some fine cracking is not unexpected as a newly built home settles and can be cosmetically rectified as it is not a structural issue. HIA publishes a *Standards and Tolerances Guide* to help resolve the issue of how much variation amounts to a defect.
- 10.1.18 HIA questions why, if pure no-fault subsidence insurance is to be provided for all new homes, it should come to an end 6 years after construction, when the subsidence is by definition unrelated to any flaw in the construction process.
- 10.1.19 It seems to HIA that this issue is best addressed in other ways, such as through including it as a minimum condition in policies of home and contents insurance. Subsidence is generally not covered by home and contents insurance unless it can be shown to be the result of flood or other insured event.
- 10.1.20 HIA does not oppose the proposal that the Authority investigate whether the benefits of inclusion of subsidence insurance exceed its costs, but HIA considers that the Authority also investigate whether the insurance industry



would be willing to offer such insurance either separately or as part of the statutory policy, and whether mandatory home indemnity insurance on new construction is the best vehicle for such cover.

11. Conclusion

- 11.1.1 HIA considers that there is no justification in the WA Government moving to change the present insurance-based model.
- 11.1.2 It is HIA's position that insurance is best provided by free and fair competition in the private marketplace. At present, the private insurance market in WA is working effectively to provide the required level of statutory cover at an affordable price.
- 11.1.3 Insurance should remain mandatory.
- 11.1.4 HIA considers that the Government should maintain a scheme which entitles builders to any level of warranty coverage they want to buy, but with price set according to risk, turnover and performance.
- 11.1.5 PI insurance and Fidelity Funds have many drawbacks and should not be used.
- 11.1.6 Subsidence insurance on the Qld model is, on current information, not necessary or justified in WA.

Housing Industry Association Ltd

16 August 2012



ANNEX A - RECOMMENDATIONS OF THE SENATE ECONOMICS COMMITTEE - 2008.

Recommendation 1

8.10 The committee recommends that all parties receive a copy of the insurance certificate, summary of product and dispute resolution procedures. The committee recommends changing the name of the insurance.

Recommendation 2

8.22 The committee recommends that COAG and the Ministerial Council on Consumer Affairs (MCCA) should pursue a nationally harmonised 'best practice' scheme of consumer protection in domestic building.

The scheme should include but not be limited to:

- ♦ disciplinary procedures and penalties;
- ♦ clearer definition of defective work;
- ♦ quicker and easier dispute resolution;
- ♦ the proposed 'loss of licence' insurance trigger;
- ♦ the HIA's 'guarantee of completion' and related proposals,
- ♦ and better information for consumers (including information on builders' licence record and average cost of premiums).

Recommendation 3

8.28 The committee recommends that COAG and the Ministerial Council on Consumer Affairs should pursue a nationally harmonised scheme of detailed reporting of Home indemnity insurance.

Recommendation 4

8.34 The committee recommends that Home indemnity insurance should be included in the National Claims and Policies Database.