



COMMONWEALTH OF AUSTRALIA

# Official Committee Hansard

## SENATE

STANDING COMMITTEE ON ECONOMICS

**Reference: Australia's mandatory last resort home warranty insurance scheme**

FRIDAY, 13 JUNE 2008

SYDNEY

BY AUTHORITY OF THE SENATE



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**SENATE STANDING COMMITTEE ON  
ECONOMICS**

**Friday, 13 June 2008**

**Members:** Senator Hurley (*Chair*), Senator Eggleston (*Deputy Chair*), Senators Mark Bishop, Bushby, Joyce, McEwen, Murray and Webber

**Participating members:** Senators Abetz, Adams, Allison, Barnett, Bartlett, Bernardi, Birmingham, Boswell, Boyce, Brandis, Bob Brown, Carol Brown, George Campbell, Chapman, Colbeck, Jacinta Collins, Coonan, Cormann, Crossin, Ellison, Fielding, Fierravanti-Wells, Fifield, Fisher, Forshaw, Heffernan, Hogg, Humphries, Hutchins, Johnston, Kemp, Kirk, Lightfoot, Lundy, Ian Macdonald, Sandy Macdonald, McGauran, McLucas, Marshall, Mason, Milne, Minchin, Moore, Nash, Nettle, O'Brien, Parry, Patterson, Payne, Polley, Ronaldson, Scullion, Siewert, Stephens, Sterle, Stott Despoja, Troeth, Trood, Watson and Wortley

**Senators in attendance:** Senators Eggleston, Hurley, Joyce and Milne

**Terms of reference for the inquiry:**

To inquire into and report on:

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

- a. the appropriateness and effectiveness of the current mandatory privatised Last Resort Builders Warranty Insurance scheme in providing appropriate consumer protection and industry management;
- b. 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);
- c. the ramifications for the future supply of this insurance product following the draft recommendations from the Productivity Commission report released in December 2007;
- d. any potential reforms and their costs and benefits which may lead to appropriate consumer and builder protection and improved housing affordability; and
- e. any related matters.

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**Committee met at 9.03 am**

**CHAIR (Senator Hurley)**—I declare open this public hearing of the Senate Economics Committee. The committee is inquiring into home warranty insurance. I welcome you all here today. The committee has authorised the recording, broadcasting and rebroadcasting of these proceedings in accordance with the rules in the order of the Senate of 23 August 1990 concerning the broadcasting of committee proceedings. I put on record that committee witnesses are protected by parliamentary privilege with respect to their submissions and evidence. Any act which may disadvantage a witness on account of their evidence is a breach of privilege. While the committee prefers to hear evidence in public, we may agree to take evidence confidentially. The committee may still publish or present confidential evidence to the Senate at a later date. We would consult the witnesses concerned before doing this. The Senate can also order publication of confidential evidence.

Before we commence, I would like to read into the record a response from Senator Helen Coonan to statements made at our first hearings held in Canberra. The letter is as follows:

Inquiry into Home Warranty Insurance

I refer to earlier correspondence.

The evidence given by Mr. Dwyer in these proceedings, reflected also in his written statement, claiming that as Minister for Revenue and Assistant Treasurer I had responsibility for an amendment to the Corporations Regulations impacting the Builders Warranty Insurance Scheme, is wrong.

I attach an email dated 27 May 2008 from Mr. Joseph Picot, Analyst with the Financial Systems Division of the Australian Treasury that confirms:

*“For your information, Corporations Regulation 7.1.12 was made on October 8 2001, the responsible minister being the Minister for Financial Services and Regulations, Joe Hockey.”*

*“The regulation came into effect on 11 March 2002, at which time the responsible minister was the Parliamentary Secretary to the Treasurer, Senator Ian Campbell.”*

I was not in the ministry when the Regulation was made, nor was I the responsible Minister at the time it took effect—a year later.

In fairness to Mr. Hockey and Mr. Campbell, I respectfully suggest to the Committee that the objectives of the Inquiry would be greatly served by inviting the Department of Treasury to provide evidence as to the background and reasons for the relevant amendment to the Corporations Regulations and the materiality of Ministerial decisions, (if any), rather than leaving it to Mr. Dwyer’s speculation.

Giving Mr. Dwyer the benefit of the doubt, it may be open to conclude that he made his incorrect claims as to my Ministerial role in ignorance, and that he was not motivated by malice.

Assuming Mr. Dwyer has made a genuine mistake, the Committee may wish to afford him an opportunity to correct the record and withdraw the false assertions he has made about me.

I believe that this could be done by an exchange of letters with the committee rather than inconveniencing Mr. Dwyer by re-calling him.

I reserve my right to make further comment should it be necessary.

I request that this letter be read into the record at the commencement of the Hearing on 13 June 2008.

Yours sincerely,

Helen Coonan.

**Senator EGGLESTON**—Could I ask that Senator Coonan's letter be sent to Mr Dwyer so that he is aware of its content, and could we invite him to respond if he so desires?

**CHAIR**—Yes.

**Senator EGGLESTON**—Thank you.



[9.07 am]

**CHAKOUCH, Ms Lydia, Secretary, Building Action Review Group Inc.**

**ONORATI, Mrs Irene, President, Building Action Review Group Inc.**

**CHAIR**—We welcome to the table the Building Action Review Group. Would you like to make an opening statement?

**Mrs Onorati**—Yes, thank you. Madam Chair and Senate committee members, on behalf of the Building Action Review Group I welcome the Senate Economics Committee inquiry into mandatory home warranty insurance. For those who do not know, BARG is an independent unfunded advocacy consumer group. I have been its president for 20 years, since 1988. I will be brief in my submission today to allow time for questions, but from my brevity, please do not underestimate the depth, the scope and the gravity of these issues.

The home warranty insurance has been and continues to be in crisis. It is not most definitely what the New South Wales parliament intended when it established it in 1971; that is, a mandatory insurance for the protection of consumers. Over the years we have seen many state and federal building industry inquiries and amendments representing major overhaul of consumers' protection, giving guarantee of services, speedy and fair process of complaints and dispute resolution. Private home warranty insurance commenced in May 1997 to provide better consumer protection. To date, this protection is still lacking. It is of great concern that the recent amendments to home warranty insurance have affected intensely and extensively consumers' lives; the lives of many honest families have been shattered as a result of such unconscionable conduct by phantom consumers' protection.

The home warranty insurance cannot be examined in isolation of the home building process. As detailed in our lengthy written submission, there are other critical factors that make up a warranty system: an efficient regulatory authority to strenuously enforce the legislation; compliance with building standards; advice to building consumers; and an independent, efficient dispute resolution and appeal mechanism. Since the government privatised the home warranty insurance, the situation has been on a downward slide for builders and consumers. In fact, the government acknowledged the need for reforms to the home warranty insurance by establishing four inquiries within 13 months. I refer you to the four inquiries at which BARG has indicated the negative impacts and the significant downgrading of the rights of consumers. These are: the national review of home builders warranty insurance and consumers' protection by Professor Percy Allen; the New South Wales Joint Select Committee on Quality of Building—the Campbell inquiry; the Legislative Council Standing Committee on Law and Justice report on the Home Building Amendment Insurance Act 2002. This committee acknowledged the negative impacts of the amendment act on consumers by stating at paragraph 4100:

The information presented to the Committee indicated [BARG's] overall impression that the Amendment Act further downgraded a scheme that already failed to protect consumer interests. (The committee has identified further the pre-existing concerns about the scheme that were raised by BARG in paragraph 4.100 to 4.117.

Further, the committee noted that the Law Society was also of similar view; that is:

The Amendment Act represents a significant downgrading of the rights of consumers

In relation to the extent of cover, the committee noted that BARG raised some issues and concerns that pre-dated the amendment act. The committee therefore urged the government:

... to consider these issues in any future review of the scheme that it may undertake and made the following recommendation:

*Recommendation 14:*

*The Committee recommends that the New South Wales Government examine the possibility of a supplementary catastrophe fund to consider claims for consumers who have received full payment of \$200,000 for a home warranty insurance policy and still require additional funds to demolish, rectify or reinstate a building ...*

BARG was not aware that the government established this catastrophe fund until the Hon. Linda Burney, Minister for Fair Trading, in her recent media release dated 16 May 2008 dealing with the Beechwood Homes insolvency, stated:

In the event that claims are made on home warranty insurance, the system is structured so that the insurer—

Vero, in this case—

would be responsible for the first \$5 million and its private reinsurer would cover the next \$5 million. Any additional amount required would be covered by the New South Wales Government's catastrophe reinsurance arrangements which are funded through the premiums on written policy. Any suggestion that taxpayers would be slugged is just nonsense.

It is commendable that the government has implemented the above inquiry's recommendation; thus the catastrophe fund will rescue consumers from the inadequacy of the current home owners warranty scheme. We prepared a sample of 12 BARG member cases to demonstrate to the committee the deleterious and catastrophic consequences suffered by consumers. I provide you with a copy, attachment 1.

Another inquiry is the New South Wales Home Warranty Insurance Inquiry by Richard Grellman. The government accepted this inquiry's seven primary recommendations and stated that it is determined to ensure that we have a stable and viable scheme that provides protection for consumers, affordable accessible insurance for builders, and transparency and accountability for insurers. I will not comment on this; it will take too long.

Five years later there is consensus that nothing has happened. If anything, it has become even worse. It is evident that the regulations governing home building and home owners building insurance are failing to protect consumers. On 17 September 2004, BARG brought to the attention of the Home Building Service manager serious concerns regarding the home warranty insurance conduct and the improper use of policy clauses which are contrary to the state's statutes. A written submission supported by 10 case studies, but representative of many other BARG members, was provided by BARG to the Home Building Service. I provide you with a photocopy, attachment 2. We were advised by the Home Building Service that these files were

handed to the scheme board. On 12 July 2006, after numerous requests, BARG had a meeting with the Home Warranty Insurance Scheme Board Chairperson, Mr Greg McCarthy, who advised us that the scheme board had not looked at these files. We provided him with a copy of BARG's submission on the day. He also advised us that the scheme board dealt only with the last resort insurance schemes not past insurance claims. BARG emphasised that last resort members were facing effectively the same problems irrespective of the scheme—the same policy clauses are in the first and last resort; I refer to copies of the product disclosure statements and to the clauses of the first resort policy which cover the first and last resort.

BARG is incensed that the chairperson of the scheme board, Mr McCarthy, did not address BARG's concern either at the meeting or subsequently. I refer to correspondence and attachments 54, 55 and 56 quoted in our written submission at page 43. I provide a copy of these attachments. They are very relevant because, from reading them, you will realise what happened.

Summing up, the systemic failure continues and is demonstrated in the samples of BARG's cases which show the following pattern. First, home owners warranty certificates are not provided by builders. More importantly, the home warranty insurance policy and/or PDSs are not provided to home owners when signing a building contract. It is mandatory law that insurers disclose product disclosure statements to clients but this is not prescribed in the Home Building Act, unfortunately. Third, the CTTT objective to mediate voids home owners warranty insurance—I refer to clauses 21 and 29 of the policy and clause 8 of the PDS, subrogation. Fourth, if the insurers product disclosure statement is provided to home owners, they become aware and they are warned not to settle. Fifth, Vero denies claims based on policy clause 29, High Court decision *res judicata* (Estoppel), *Onorati v. Philips*—unfortunately my name is there. Other home owners warranty insurance relies on similar technicalities. Six, the practice of splitting contracts. Seven, protracted building disputes from three to eight years—in once case, 15 years. There were three builders and she needs a fourth one to rectify it. Eight, consumers run out of money to appeal against adverse decisions. Nine, consumers cannot win, even though the CTTT decision is in their favour because they have no money to bankrupt their builder to lodge a claim with the insurer, and/or if the builder is bankrupted the home owner's claim is minimised by the insurer. The home owner has no money left to appeal the insurer's decision in the courts once again. Ten, consumers are scared to go to the CTTT, especially after the evidence heard at the hearing on 2 November 2007 during the parliamentary inquiry into Home Building Services. Eleven, consumers reach settlement by mediation with insurers under duress due to financial constraints after protracted and costly disputes. These occur in two ways—and we have examples. Firstly, unfair mediation to desperate home owners who are forced to accept inadequate rectification of defects—patch up—and no costs are awarded. Secondly, when home owners do not accept the terms of mediation, although no written or signed agreement was executed, the insurer summons the home owner to the High Court for breach of mediation agreement although, after two years of dispute, the High Court dismissed this matter. Vero has now appealed this decision to try to enforce the mediation agreement once again. This is abominable.

The above list, although not comprehensive, demonstrates the complete failure by the present regulatory system to properly monitor and investigate complaints and grievances against insurers and prosecute the breaches of the Home Building Act 1989. Consumers need to be confident that a compulsory insurance scheme is administered fairly for all; currently it is not. BARG congratulates Senator Christine Mills on successfully moving to refer the issue to the Senate

Economics Committee. BARG believes only the Queensland scheme currently operates in the best interests of consumers.

I thank you for the opportunity to address the Senate committee. The problems are so numerous and complex that it is not possible to cover all aspects in great detail in the short time today. I am prepared now to answer all your questions. Thank you.

**CHAIR**—Thank you, Mrs Onorati. You have been involved in this for a long time, and I think you understand the issues very well. This committee is, of course, principally looking at the last resort warranty scheme, but we are also putting in some consideration of where intervention is necessary. You would be well aware that the mandatory home warranty insurance scheme began because of the failure of an insurance company that did provide an earlier insurance scheme. It really was intended as a last resort. Given that background, and apart from the Queensland scheme, would there be any way to make the existing scheme in New South Wales fairer?

**Mrs Onorati**—As I say in the BARG written submission, and in my presentation today, we cannot examine in isolation home owners warranty insurance. There are other critical factors that contribute to a warranty, and the most important is an efficient regulatory authority to strenuously enforce the legislation. This is not happening. We have demonstrated that in our three files with attachments of documents extracted under FOI from the files of the Office of Fair Trading or Home Building Services—builders' licences, how they originally achieved them. There have been many examples, but unfortunately I have not provided you with all the attachments. These are the voluminous documents here. The submission is only about 60 pages plus the two supplementary submissions in which I reply to what the Office of Fair Trading said about our submission. So, yes, definitely we need a new system. There are no ifs or buts about it.

There is no consumers advisory—I did not mention that. I am not funded, as I said, and my secretary has two jobs and still fights to pay the mortgage. She had to fight her building dispute, and she is one of the claims that has been patched up, and she still pays. We need compliance with the building standards—the council DA approval of critical stages of inspection, the council final occupation certificate or PCA. There are all these things. As I said, an independent efficient disputes resolution mechanism for appeal is needed.

I have said enough for BARG and about the cases. In the table of samples, when you look at it—and I was hoping you would ask me questions about that because this is the mirror of what happens—I think there are about four last resort and about eight first resort cases. I would have many other cases, and that is how I discovered the PDS; I did not even know it existed. That gentleman has walked out losing money; he could not continue to assist me. It was a last resort. Therefore, yes, there is a need for a lot of things, and it is very hard to regulate all these.

We have been promised all these things with all the inquiries. I can refer you to them. My addresses are all over the place. Professor Percy Allen has called me many, many times and I cannot refer to what he said about the last and first resort and about punishing insurance fraud. He has a particular page—if you refer to what he says. Therefore we have lost trust, can I say, in the statutory authorities in the government. I am sorry to say that, because I think it starts there. There is something wrong from the top, because the legislation is breached and the people who breach it are not strenuously prosecuted. Therefore the breaches continue. The same builders—I can give you names, and I think they are there—let their licence expire and then they go back

and get a new licence. They get their wife or their son, but they still are the qualified supervisors of their company. This is ridiculous. It is too much to take. We have had enough. We need a new system.

**CHAIR**—What do you think of the Tasmanian approach which is simply to say we will not have a mandatory last resort warranty system anymore, because at least consumers realise that they do not have a system that—

**Mrs Onorati**—Unfortunately, I do not know enough about that. All I can say is that perhaps there cannot be anything worse than what we have now. I have lost everything. I have worked in this lovely country for 54 years. More importantly, I lost my husband. This is why I dedicate my life to helping consumers. This is the only reason. There is no-one out there to think of these poor people and what happens to them. In every case I feel that it is mine coming back again. Of course I lost everything I had, and we were very well off. This is why we survived, but I will not go into that. I just wanted to explain to you why for 20 years I have continued to do this—and you can see my case is quoted as a precedent for the same reason—because of the PDS or the insurance policy, and the defects were not put on the first time, and you could not go back.

**CHAIR**—This is an issue in which I am interested too. You said that when you sign the builder's contract, of course you do not cite the insurance and you have no opportunity to examine the policy and see exactly what it is that is covered. I think this is one of the origins of the misunderstandings about whether or not you are covered for various things that you think you might be. Until the contract is signed it is very difficult for the builder to get insurance.

**Mrs Onorati**—No, that is incorrect, I beg your pardon. The builder can apply for insurance. There are two methods, and if Mr Dwyer is still here he could answer this question better. I am aware that they can have blanket insurance. They are also given a booklet that they fill in themselves, and we do have some monkey business there too. As I say, there are so many problems; it is like you asking me to put the ocean into a bucket here this morning. I do not know what else to say. It is terrible what is going on. Really, please believe me, for a woman of my age to dedicate my whole life to these people, when I have so many personal problems, and to work up to one o'clock seven days a week and get up at three o'clock, it must be very serious. I cannot accept this going on anymore. I have addressed the crossbenches also and all the inquiries, saying, please, please, if you do not want to do it as a government, do it as Christians. Put a hand on your conscience and do something about it. Feel for all these people. I mean, people are sent bankrupt. They are losing their house. Families with four kids are living in rental premises and they have lost everything. I cannot emphasise how serious this is.

This PDS is interesting. It is important to start many things, not only the clauses—and I do not know how much time I have. It crosses over the federal law. It says:

Important notice: the policies made of this policy wording, any endorsement of the certificate of insurance. You should read those documents together to tell you what we cover—

We do not have the documents anyway so how can we read them together? It goes on:

what we exclude, what we pay to settle claims and other important information. Please note that you have obligations under the policy with which you must comply, otherwise we may not have to pay your claims.'

Then it has, 'Duty of disclosure'. They are referring to the Insurance Contract Act 1984 to disclose the insurance. What about the disclosure to us? It goes on and on. I am not a solicitor and I obtained this by asking two BARG members as a last resort to ring Vero and demand it. They did not even know that it existed. As you can see, the photocopy has the date and the name of the person that got it for me. We are not consulted. We do not exist—I will not go into that.

There have been media releases since the early 1990s—1993—and, Minister Richard Amery, a great man, said—and I will never forget—that 50 per cent should be consumer consultation. But that has not happened. We do not know what is happening. We do not receive anything. We are not on their mailing list. We write to ministers but we do not get replies. The only effective contact is from the opposition or the Greens or the Christian parties. This is why we address the crossbenches. In the last 12 months we have written seven letters to the new minister for the Office of Fair Trading asking for a meeting. People write to the minister, because she is the head, and they believe that she has to review and reassess what happens. But guess what happened. The minister passed the letter to the Office of Fair Trading.

**CHAIR**—Let us continue on our inquiry.

**Senator EGGLESTON**—One of the things you raised was the need for some sort of better dispute resolution.

**Mrs Onorati**—Definitely.

**Senator EGGLESTON**—What would you propose there?

**Mrs Onorati**—An independent—

**Senator EGGLESTON**—An independent statutory body?

**Mrs Onorati**—Statutory body? No, I am sorry, we have a statutory body now. The CTTT is a statutory body. Look at the figures here.

**Senator EGGLESTON**—There is a statutory body, but would you have it varied? How would you like to have its role varied?

**Mrs Onorati**—If the statutory body were an independent council with consumers' representation. We have tried. I have written and I even went to the Attorney-General, who knows me, and I pleaded with him many times when he was for a short time the Minister for the Office of Fair Trading. I requested that somebody from BARG, a consumer, a real independent consumer, sit on this council, but we did not get that.

**Senator EGGLESTON**—You think that consumer input is very important?

**Mrs Onorati**—Yes.

**Senator EGGLESTON**—The New South Wales parliament's Legislative Council General Purposes Standing Committee No. 2 has conducted an inquiry into the operations of the Home

Building Service in December 2007, and it made a comment that it was concerned by evidence of poor consumer protection—

**Mrs Onorati**—Definitely.

**Senator EGGLESTON**—and recommended extended coverage beyond the last resort conditions of these policies.

**Mrs Onorati**—But also they recommended an inquiry. Actually, they did not recommend it, they suggested that an inquiry be carried out into the CTTT, the Consumer Trade and Tenancy Tribunal, but that was also recommended by the Campbell inquiry in 2002, and was never carried out in three years—or, if they did, we know nothing about it—and it was not tabled in parliament. They have carried out two reviews now and a solicitor has provided me with that information. But it is not what we want. We have not been asked what happens in the consumer cases. I have plenty of consumers to prove what happens in the CTTT. It is really destroying families. The money all goes there; it lasts from three years to seven years in the CTTT. They spend their fortune; they do not eat. People are completely bankrupt and destroyed. I have an example—

**Senator EGGLESTON**—I understand what you are saying, but one of the big issues seems to be a lack of transparency about the operation of the scheme.

**Mrs Onorati**—Yes. I had that and took it off, for time. I think it was Percy Allen, or Campbell, that said accountability, responsibility and reliability are the three core things.

**Senator EGGLESTON**—You would agree that we need a lot more transparency in the operation of this scheme?

**Mrs Onorati**—And accountability. You mentioned—

**Senator EGGLESTON**—And accountability and a better dispute resolution—

**Mrs Onorati**—You mentioned this inquiry; we are trying to reopen it.

**Senator EGGLESTON**—system with more consumer protection?

**Mrs Onorati**—Yes, definitely. There are many inquiries. I do not want to criticise the inquiries, because they were very lovely people who were involved. All of them tried to do their best, but the problem is that their recommendations were not implemented. I just found out about this catastrophe. The chairperson of the last law and justice committee, if you read the report, put down all the comments of BARG, and my name in particular, when I addressed them, but I did not even know that that recommendation 14 was implemented until the minister read it. Do you know what I mean? We are living in the dark. All my time is spent just to assist these people, because they do not know their rights and entitlements, and the legislation is not enforced. I will give you an example of the CTTT. A builder did not issue a homeowners warranty in this case—and I think you might get the submission this morning; a couple of people will hand you some submissions. He criticised the builder, but at the end he rewarded him because he said, ‘Okay, it is last resort insurance. It does not matter that he did not issue a certificate, because the

consumer had to bankrupt the builder and disappear; therefore, it does not matter.' Is he condoning the bad conduct of a builder? This builder is out there continuing. In 14 years he never had any insurance. We subpoenaed insurance files of Vero, and he never applied. Come on. What are we doing?

**CHAIR**—Who is responsible for checking whether builders have insurance?

**Mrs Onorati**—The Home Building Service, the Home Building Act, section 106.

**CHAIR**—But the insurance is mandatory; who is supposed to check that the builders have that insurance?

**Mrs Onorati**—Nobody checks, unfortunately. Consumers do not know. There is a lady here who only found out the other day. She did not know, and she did not know what to do. The inspector went to check the house and she was told, 'You have no insurance, so that is it; I cannot do anything for you.' Then he walked out. I said, 'Hang on a minute; the insurance is one thing. The Home Building Service is there to prosecute the breaches of the Home Building Act. That is a serious breach.'

**Senator EGGLESTON**—Should issues like having insurance be a condition of licensing, and do you see licensing as an area that needs reform?

**Mrs Onorati**—Definitely, most definitely. My brain has become like a dictionary, an encyclopaedia. I can quote you chapter and verse of clauses. I know the clauses very well. I forget names sometimes, but I can tell you the clauses in the act. Section 92 is about the insurance. When a licensed builder has a residential contract, it is mandatory that he issues that certificate of insurance. But what is not mandatory is that he provides a policy or a PDS, or product disclosure statement, as now it is called, which people do not even know exists. I did not know; I found out because I asked the person to get the policy, and they told me, 'There is no policy anymore for last resort; there is a PDS.' I said, 'What is this?' I did not know what those three letters stood for.

**Senator EGGLESTON**—Coming back to licensing, would you make licensing for, say, only every five or three years?

**Mrs Onorati**—Every year.

**Senator EGGLESTON**—Annual relicensing?

**Mrs Onorati**—Every year. I am not generalising and saying they are all bad. We have a lot of good builders out there who have suffered, because the good builders are covering the media just as much as the consumers. Some of the builders do not work anymore. One of my friends, this was in the *Sydney Morning Herald*—

**Senator EGGLESTON**—But they still retain their licence, even though—

**Mrs Onorati**—They retain their licence. He does not work because he does not want to put his house and lose it, okay.



**Senator EGGLESTON**—There are builders out there that, once they are licensed, they are licensed forever; is that the situation or not?

**Mrs Onorati**—It should not be, because—

**Senator EGGLESTON**—No, but is it the situation?

**Mrs Onorati**—Well, it looks like that, from what we understand from Lydia's builders, from the builders of all these people here and all the other cases I have. I used to say at the beginning that builders get a licence like children get jellybeans. It has been discovered from ICAC that 94 builders—there was a syndicate that was providing references. I do not know if you are aware of that; I think I covered it here or in my address. All you needed was to provide a reference to get a licence, and they got into trouble. Also, engineers' diplomas were obtained for \$50,000. The evidence is there in the ICAC's report. Licence is the first link, the first foundation, where everything starts to go wrong. Professor Percy Allen, one of my favourites, says, 'If consumers need good homes built, we need good dispute resolution, punishment of breaches and'—what were the three things? Insurance would not be needed. As we saw even in the old BSC insurance, there was \$75 million which was given for the Olympic Games, to do building for the Olympic Games in Australia. What I mean is that insurance is very profitable, especially now. There are no claims at all.

**CHAIR**—Given the HIH episode, we all understand that we do need insurance.

**Senator JOYCE**—Looking through your submission, you also obviously have problems with the Office of Fair Trading and its issuing of licences; that was also one of your concerns. You believe that, of the builders who have been issued licences, you will always have ratbags—

**Mrs Onorati**—There will never be a completely foolproof system. Some of the builders can slip out. We addressed the General Purpose Standing Committee No. 4 on the budget estimates and lodged a submission; that is how this inquiry came about, because we proved—and there is evidence in the transcript; David Oldfield said it—they only check 10 per cent. I do not know if you followed that.

**Senator JOYCE**—Yes, I saw your questions. Mr Oldfield asked questions on your behalf with regard to the examination of how many people had been checked for bankruptcy, criminal records et cetera.

**Mrs Onorati**—Exactly.

**Senator JOYCE**—And they said, 'Yes,' or 'But then we found out it is only about 10 per cent,' or something like that.

**Mrs Onorati**—We have experience, as we provided original documents. I do not ask you to believe me, okay? Please look at the documents.

**Senator JOYCE**—I believe you, because you are under oath.

**Mrs Onorati**—Yes, and I am very strict.

**Senator JOYCE**—Do you feel that the Queensland scheme is a better form of scheme?

**Mrs Onorati**—There is a consensus, isn't there?

**Senator JOYCE**—Yes. So your specific issue is with regard to the New South Wales scheme. You find the New South Wales scheme particularly abhorrent. We are having the hearing here in Sydney and it is filling up the room, so obviously the major concern is in the structure of the New South Wales scheme. The question I am getting to is: if I waved a magic wand and said, 'You are now the boss; you now run the show. But you have to make changes,' what changes would you want? You will want transparency, I can see that. You will want a scheme that is more diligent in how it enforces what builders get licences and also how the claims are brought about. If we just overlaid the Queensland scheme into New South Wales, would that be sufficient or is there more you need to do on top of that?

**Mrs Onorati**—I read the evidence of Mr Jennings, I think it was, and it sounds excellent. What I want to bring to your attention also is the recommendation—and I think it is in my written submission—that the Campbell inquiry made that they wanted an independent commission completely detached, separate, from the Office of Fair Trading.

**Senator JOYCE**—I read in your submission that you believe that the Office—

**Mrs Onorati**—But what happened? The recommendation has not been implemented appropriately. It is like putting Dracula to look after the Blood Bank. We have the same problems, because we have the old people who are so used to it. I do not know why. Are they too busy; are there not enough people? It is a systemic culture; I do not know what to call it. There should be an independent body.

**Senator JOYCE**—I saw that in your submission where you talked about the Office of Fair Trading was the problem, and then the solution became part of the problem, and just infected the solution, so you want the Office of Fair Trading out of the scene. You want an independent stand-alone, completely apart from the Office of Fair Trading.

**Mrs Onorati**—I am sorry for that, because I have a lot of good friends there, but unfortunately I cannot see it working. When something does not work it has to be replaced.

**Senator JOYCE**—I also noted in your submission, and I was very interested in this, the amount that you guys are paying in legal fees. It is absolutely astronomical.

**Mrs Onorati**—Yes, this table proves it. Did you see the table?

**Senator JOYCE**—Yes, I can see that. It looks like the legal fees are about one-third to one-quarter of the costs.

**Mrs Onorati**—A quarter! It is double and sometimes triple.

**Senator JOYCE**—The cost?

**Mrs Onorati**—Yes. For one driveway, a three-day job for a concreter, the homeowner went three years to the CTTT. The system is that they engage senior counsel and solicitors when it is supposed to be a system for consumers, inexpensive, informal et cetera, like the legislation. Legislations are not complying in any form or shape. So the consumer has to match; otherwise, what happens? Then they have strategies, the licence people, and the strategy is to delay. This is why the cost goes up, and that is why we have from three years to seven or eight years in the tribunal. They adjourn; he goes overseas. And the costs for that driveway? Now they are waiting for the award of the costs. The decision has come out; the case of the cross-claim was dismissed. This is a small example. This is why the smallest building repair job is the biggest nightmare of your life and destroys people completely—not only financially. People are destroyed mentally. A lot of people—

**Senator JOYCE**—Yes, I can understand that.

**Mrs Onorati**—I am sorry I use the word ‘mental’. They go and see a psychologist. Intelligent people with tertiary education; a former solicitor, member of the CTTT, a dear friend of mine since I was a teenager—I can see how the personality changes. Not only the pocket is emptied; this is emptied.

**Senator JOYCE**—The question I am getting to is this: do you believe it becomes a tactic of the people in avoiding you to say, ‘We will just drag you through the courts, backwards and forth, backwards and forth, backwards and forth, because we know that you are going to run out of money before I do.’

**Mrs Onorati**—That is right. It is a paper war and money war, David and Goliath—call it what you want. Look at the last case in this. This is an example. It is the last resort, but he is still fighting. He refused to settle in mediation. There was no written agreement signed.

**Senator JOYCE**—On top of that, there would be a lot of people out there who would have a grievance but they will never pursue it because they say, ‘If I go to pursue this, I will just go broke.’

**Mrs Onorati**—Exactly, they are scared. This is what I am saying. People are saying that.

**Senator JOYCE**—‘For the sake of my driveway, I will be bankrupt.’

**Mrs Onorati**—That is what she said: ‘I would have been better off to give him whatever he wanted.’ This person is terminally ill. Each person has a problem here.

**Senator JOYCE**—Obviously you are passionate about it, and the people involved with it are passionate about it. Your political involvement in trying to get this issue pursued is obviously intense and has gone over a number of years. Why do you believe it is now before a federal Senate inquiry? Why has this thing not been resolved at a political level before the state? Why hasn’t someone at the state parliamentary level just said: ‘Let’s rule a line under this and fix it up, finish it off, whatever we have to do. If they want an independent tribunal, give them an independent tribunal or get it out of the way.’

**Mrs Onorati**—In my real honest opinion, if I use the terrible wording that people use, that homeowners use, and there is a brotherhood out there. The consumer is alone. Everybody is fighting for the cause, starting from licensing. I worked it out once. How many do we have—168,000 licensees. How much is the licence? It amounts to billions.

**Senator JOYCE**—There is a mates club working against you.

**Mrs Onorati**—Yes, put it in those words, I am sorry. Everybody is getting money from this poor little honest person that worked all his life or her life to get a roof over their head, and they lose. He does not have a roof over his head with four kids; he is in rental.

**Senator JOYCE**—A couple of years ago I would have said, ‘I think you are embellishing it,’ but after certain things around Wollongong and places like that, you are possibly correct, so we need to check that out.

**Mrs Onorati**—Also, when council issues a demolition order—and I have a few; you will see it in my reference, the orders are there—the Office of Fair Trading does not even take any notice. It does not even prosecute the builder. We have letters, and I think some political people should be asked to step down because it is in writing. It is misleading and deceptive conduct. They are saying that the builder is not responsible because it is the engineer. The builder is blaming the engineer. But, wait a minute—the engineer has been employed by the builder. Even the insurer states clearly in these conditions that if the owner has commissioned the engineer then the insurance does not pay, but if the builder commissions the engineer, and that is in the act, it is clear in all the policies, they should be prosecuted. But the builder has not been prosecuted. He has lost nothing, and the consumers have lost everything. He lives in a caravan in his backyard because he cannot live in his house. The council took him to court because they want him to rectify it. If I had time I would quote cases without names. This is just to give you an idea of how terrible it is, how desperate—

**CHAIR**—We have had many written submissions on cases.

**Senator JOYCE**—And we can see that there is a vast belt of them in the western suburbs of Sydney. I can see that.

**Mrs Onorati**—Everywhere north; I have three—

**Senator JOYCE**—I was talking to people in Tamworth and they also said, ‘If you go down this path you are going to open up a can of worms, because they are everywhere.’ Anyway, thank you very much for that.

**Mrs Onorati**—Can I answer your question?

**Senator JOYCE**—Yes.

**Mrs Onorati**—You asked me: all the other inquiries did not do anything, why should a Senate inquiry help? I do trust and hope that the Senate will make it, because you are the head of all the states and you can see everything and all the people suffering. When you look at what is happening in each state, you will realise that all the other inquiries have spent a lot of taxpayers’

money, cost millions of dollars but did not fix the problem simply because what they said has not been taken into consideration. Even with the amending legislation, they did not want the private insurance to get out of the market. I can quote chapter and verse here; if you read it, it is all highlighted and referenced, but I have no time. I knew I had to try to address you in 10 minutes. I have three volumes there that do not even contain the PDS. I have not covered the PDS there.

**Senator JOYCE**—It is a state government issue which we have to pursue. The federal position on this is that we cannot—

**Mrs Onorati**—But doesn't each state have the same problem? If each state has the same problem, why doesn't the head of the—

**Senator JOYCE**—We can certainly put pressure on—

**CHAIR**—Australia is a federation; we are not actually at the head.

**Senator JOYCE**—Yes, thank you very much for that.

**Mrs Onorati**—I am sorry.

**Senator JOYCE**—No, I am just making sure we get our mind around it.

**Mrs Onorati**—You made me lose my hopes; I feel like crying. I was really trusting and hoping that this inquiry would really address the problems.

**CHAIR**—We will certainly try to.

**Mrs Onorati**—Twenty years I am doing this, okay. Think: why am I doing it?

**Senator JOYCE**—You are certainly—

**Mrs Onorati**—Peter Harvey interviewed me at the Campbell inquiry.

**Senator JOYCE**—We could try to get him to fix it.

**Mrs Onorati**—Yes, he told me: 'Tell me in three words why this is happening?' I said, 'The law is breached and then the perpetrator is not prosecuted.' He was happy. But this is continuing.

**Senator JOYCE**—Our job is to make sure that there is a clear and concise case that we can go forward and help and assist you. It would be wrong of us to guarantee that after this inquiry your problems are going to be fixed because that would be misleading you, and that is something you do not want.

**Mrs Onorati**—Can I hope at least it improves?

**CHAIR**—The Productivity Commission is also looking to this Senate inquiry to make some recommendations, and then that needs to be considered by the various governments. We are certainly taking our task very seriously.

**Mrs Onorati**—Thank you very, very much to all of you. I hope that something will come out of this inquiry. I must hope and trust that it will.

**CHAIR**—Yes, indeed; we all do.

**Senator MILNE**—I apologise for my late arrival. I have flown up from Tasmania this morning, so it has taken a bit longer. Can you comment on how the insurance as it is currently forces builders into noncompliance, and can you comment on the issue of builders having to give bank guarantees and what impact that has.

**Mrs Onorati**—The comment I can make very strongly and very efficiently is that the insurance breach the Home Building Act in many ways. I can summarise what I said before.

**Senator MILNE**—Do not go back over it, because you may have gone into that previously.

**Mrs Onorati**—The insurance policy or PDS is not given to consumers. That breaches the Home Building Act. But they are not monitored like the Home Building Act states, in section 106(e), and nor are they prosecuted. This is why we made that submission that I handed in a copy of. Builders have to guarantee their homes with their home insurance; I cannot understand why building insurance is different from any other insurance. I sympathise with the builders, and builders are put in a position that they have to lie and breach the law by not issuing insurance, and they become also responsible—not all of them. In some of the examples I have—you can see them on the table—they have not issued a certificate, or they promise, ‘Yes, I include the cost of the premium in my quote; I will work it out. It takes time. You will have it in a few weeks.’ Somebody else there was told, ‘You will get it in a few months,’ but they never got it.

**Senator MILNE**—You do not have any figures? We need data. I am just asking: do you have any figures of the level of noncompliance with this insurance or builders being driven into noncompliance because they have to give bank guarantees? If you have any data, we would appreciate any statistics that you have in relation to that.

**Mrs Onorati**—Well, no.

**Senator MILNE**—One other matter that I raise with you is adequate inspection of houses during construction. I believe that you mentioned that briefly in your opening statement. What would be your main criticism of the current arrangements in terms of inspection during construction, and what would you recommend?

**Mrs Onorati**—I do not have any statistics. I am a single person working. All the people on the committee have two or three jobs, and they are victims of a building dispute. They can give so little. We meet at committee meetings to see what we are doing and how we can improve.

**Senator MILNE**—It is not a criticism; it is just asking if you have the data. If so, we would like to have it.

**Mrs Onorati**—No, I am sorry; I would love to, but I do not have it. You can notice that in the table or in the complaints or submissions that we have provided. On the second thing, the inspections, we have council inspections first, and sometimes the council inspector goes down, or the PCA, and the structural plans have not been submitted by the builder. The inspector or the PCA says to the builder, ‘As long as you produce a certificate of compliance by the engineer, we are quite happy.’ I have cases that the house was constructed without structural plans submitted and approved by councils. I gave details in the Campbell inquiry. This is why they tried to change the local government and the private PCAs. In a case that broke my heart—the lady is very sick—the PCA had about 10 complaints to the board against him, but he is still working out there. Why? Maybe the board is biased, people of the same profession. Definitely the critical council inspections are not appropriately carried out, or are not carried out at all. We have houses, as I say, with no inspections at all. I have a lady here, I just remembered, Jasmine, with no DA submitted and no inspection at all. What do you think? The house is for demolition. The council issued, ‘Council inspection, not qualified.’ This is a message. Of course they are not qualified inspectors, plus they see the builders all the time in that area, plus, plus, plus. The Office of Fair Trading inspectors—that is another kettle of fish, similar or even worse. That is the last—how do you call it when you go to hospital? You break your head, you are desperate, you have to fix your head, you know?

**Senator EGGLESTON**—First aid?

**Mrs Onorati**—They fail you, too, because as you can see in the complaints, it is a disaster. I will not mention names, but it is the same inspectors repeatedly. We have sent consumers, and a building consultant that I have named in my submission, appointed by the Office of Fair Trading—and we had a very nice HBS manager at one stage, he realised what I was saying, and he was trying to cooperate; we are very obliged to a lot of people there, but sometimes when you see the whole picture it is a failure—he said that they should be sent back to TAFE. They do not have the qualifications. None of the inspectors have, and, if they have, they do not follow by the book what they are supposed to do.

**Senator MILNE**—Okay. It seems to be a key issue for us, that not only the licensing but also the adequate inspection during construction are a major problem leading into this—

**Mrs Onorati**—But to me now insurance is the most important thing; we are talking about homeowners warranty insurance.

**Senator MILNE**—We are talking about trying to fix the whole system.

**Mrs Onorati**—Yes, but they also are never prosecuted, despite there being so many breaches. They are allowed to carry on how they would like to carry on.

**CHAIR**—Thank you, Mrs Onorati, and other members of BARG for coming in today and for giving us this additional material. It is always useful to hear from people who have actually been involved and can tell us what is going on. Thank you for coming this morning.

**Mrs Onorati**—Thank you very much, senators. Thank you, Madam Chair.

[10:02]

**RENOUF, Mr Gordon, Director of Policy and Campaigns, CHOICE**

**CHAIR**—Welcome back, Mr Renouf. Would you like to give an opening statement?

**Mr Renouf**—Just briefly. Thank you very much, Senator Hurley, and members of the committee for hearing from CHOICE on this matter. We have made a submission, which I refer to you. We are also aware of the submission of the Consumer Action Law Centre to this inquiry and the discussion of this issue in the recent report of the Productivity Commission on Australia's consumer policy framework. We generally endorse the conclusions of both the commission and the Consumer Action Law Centre. As I think the committee is aware, we are dealing with a couple of interrelated issues here; one is the ostensible subject of the inquiry, home building warranty insurance, and the other is how disputes are managed and quality ensured in the building industry for consumers. I will try to talk about each of those separately. CHOICE does not have the kind of extensive on-the-ground experience of building disputes that many of the other people appearing before the inquiry will have, so our information is based on our analysis of some work we have done in the past on the insurance subject and, I guess, our extensive knowledge of consumer complaints processes across a wide range of industries.

Starting first of all with home building warranty insurance, I guess our view is that in 2002 the insurance industry pulled a fast one on Australian governments and Australian consumers. They used a crisis caused by the combined effect of the HIH collapse and international events that affected reinsurance prices to have insurance regulation changed in a number of areas. We had the so-called tort reforms, which, in our view, went too far—that is not your problem today—but also the introduction of the last resort home building warranty insurance scheme. That appears to be one of the problems that we have with us now.

As all involved will know, insurance premiums are paid by builders, but most of the costs are generally passed on to consumers. Consumers can only claim on the policy when the builder is shown to be liable for some failure but is unable to remedy the work and is insolvent, dead, missing and so forth. Effectively we have a system in which consumers are compelled to pay for something which is of almost no value to them, because in addition to it being a last resort scheme, of course, it has a number of carve-outs in terms of what claims can be paid. They pay premiums of \$1,500, \$2,000 but get not much in return.

In its measured language, the Productivity Commission in its report said:

Though a cost for consumers ... HBWI—

home building warranty insurance—

offers little protection to them in most circumstances.

That is a conclusion that is consistent with the work that we did in 2004, which is referred to in our submission. As a result of this, in the past we have labelled this insurance, with some other



insurances, as junk insurance. As the Productivity Commission also implies, no rational consumer would choose to purchase this product in its current form unless they were compelled to take it out. We might talk a bit later about what can be done about that.

I want now to turn quickly to the question of dispute resolution. I preface my remarks by saying that one of the themes that we took to the Productivity Commission inquiry about the whole of consumer protection in Australia was an observation we made which is that we deal with very similar issues in very different ways in different consumer industries. In banking, we deal with dispute resolution in one way; in telecommunications, it is similar; in energy, it is similar; in food, it is quite different; in health, it is quite different; in building, it is quite different; in motor vehicles, it is quite different. We have a range of different ways, and we do not seem very good at learning, across those different dispute resolution systems, what works. Of course, all industries are different and they need to be tailored to some degree, but we can learn from all the schemes in Australia. It is our view that, in the financial services industry, in the last 10 to 15 years, we have had quite a good system for resolving most kinds of disputes through the Banking and Financial Services Ombudsman. There are similar schemes in some of the other parts of the financial services industry. There is a slightly less good scheme in telecommunications. We have much less good schemes in relation to some medical things. And obviously, in most states, there are a lot of problems with dispute resolution in building. I would like us to learn from some of the systems that do work.

What is the fundamental bottom line? Consumers need an accessible system which is effective, and I think the key point here is that it is rapid. If you have a problem with a building, particularly if you cannot live in that building and you were, then you need it to be fixed very quickly. You need to know what direction it is going. It seems, from the evidence that others have put to the Productivity Commission, that having access to independent experts who can come in and look and make a bit of a preliminary call about whether or not there is a genuine problem—backed by some kind of dispute resolution system which is not just mediation but can in fact compel a builder to do the necessary rectification work, if that is what the evidence suggests—is one of the elements of a successful dispute resolution scheme. I am sure the inquiry has and will hear of lots of evidence of people who have really had things drawn out because they have had to go to court—the sort of evidence you have just heard about, the risks involved, the cost barriers to taking a matter to court. I guess if we draw that all together, what we have is a situation where consumers have access to quite good dispute resolution procedures about things of modest value, like their telephone bills or some problem with banking—of course, some of the financial service disputes are also large—but the systems are not working very well for building work, which is, for some people, the most important investment they will make; for others, it is extensions, but it is still a relatively substantial amount of money. So we have this comparison that does not make building dispute resolution look very good.

The final point made by the Productivity Commission, which we would endorse, is that it is useful to have a linkage between building dispute resolution and licensing conditions, so that there is some pressure on a builder who wants to stay in business to respond to determinations that are made that they should do certain work or pay certain compensation. We note that the Tasmanian government has taken some recent action. It has obviously come to the view that the home building warranty insurance is not much chop and that there needs to be improved dispute resolution. We welcome its efforts to improve dispute resolution.

I guess, at the end of the day, it seems to us that there needs to be some kind of way of compensating consumers when builders are out of business. It is a slight mystery to us about the Tasmanian government's logic in thinking that, in fixing dispute resolution, we will not need some kind of compensation arrangement. Whether that is some form of insurance or some form of publicly operated scheme, I do not have strong views, but I think I might lean towards the latter. The principal point here is that there will be cases where builders who have been required to do some work or compensate a consumer are unable to pay through death, insolvency et cetera, and there will be some need for some kind of backup.

I am very curious about what the Tasmanian government thinks is going to happen in those cases. I guess I would go out on a limb and predict that there will be some Beechwood type event in Tasmania where a major builder goes bust and five, 20 or 100 consumers are out of pocket, and there will be a public outcry, and they will reinstitute some kind of compensation scheme. Just to summarise the reforms that we need—and as the chair has mentioned, these are not entirely within the responsibility of the Commonwealth—are some more effective ultimate compensation scheme, much more effective dispute resolution, and a linkage between dispute resolution and licensing, which are the kinds of things that the Productivity Commission mentioned should be covered, which we agree with. All the evidence does suggest that consumers get much better value for money in Queensland, both in terms of the dispute resolution scheme and the ultimate compensation scheme. That has to be a starting point for other governments, I would suggest. That is all.

**CHAIR**—Thanks, Mr Renouf. I would like to go back to the actual insurance. It is an unusual system in that the builder goes out and gets the insurance on behalf of his client, who is then the insured, the consumer of the insurance. As we have heard from Mrs Onorati, the person whose house is being built usually does not know the terms and conditions of the policy and what it covers. Because it is called a warranty insurance, many people think that it covers much more than just those last resort conditions.

**Mr Renouf**—Yes. People obviously are used to dealing with particular kinds of insurance—first-party insurance for your motor vehicle lets you turn to the insurer when something goes wrong, and they will sort it out with the person who you say has done something wrong. That is an expectation that consumers will be familiar with. It is the same with their ordinary household contents insurance or basically any kind of first-party insurance. The only other kind of third-party insurance that I can think of that consumers would be possibly familiar with is third-party property damage insurance on their motor vehicles, given that the third-party personal injury schemes are a different kettle of fish. There is that reason why consumers would have a certain expectation. As you say, with the labelling of it as a warranty, people think of a warranty as when they buy goods and they have a warranty that, if there is something wrong with the goods, the retailer or manufacturer will fix them up. Again, I think you are right in saying that the name of the product is part of the problem, although probably not the most important part of the problem.

**CHAIR**—I think it is also the issue that this is a form of insurance that has caused problems for both builders and their clients. It is onerous for both parties.

**Mr Renouf**—That is right. The insurance company is in the business of managing its risk, and, given that its risk only arises if the builder becomes insolvent, dies, or disappears, then it seems that the insurance company's incentives are to focus on those aspects of the builder's

operations and not on whether they are going to deliver a working house to the consumers who buy the products, so there is kind of this misalignment of incentives going on here in the way we have structured this insurance.

**Senator MILNE**—You said that in 2002 the insurance industry pulled a fast one in relation to this insurance, and it certainly seems that way. You go on to say that ‘consumers are compelled to pay for something that is of no value to them’. In relation to that, do you have a view about who is benefiting if it is not the consumers? If the insurance industry did pull a fast one, how are they benefiting? And do you have statistics as to how much are the commissions, who is benefiting from the commissions—some actual data on that?

**Mr Renouf**—Just to clarify, I said that it would be of almost no value. Obviously there are a small number of consumers who successfully pursue the matters through the various dispute resolution processes in courts and ultimately get paid. The Productivity Commission report certainly contains figures supplied by the major insurer about the number of claims, although it does not contain information on the number of claims paid. It would be useful to obtain that information, because I am sure that committee members know, for reasons that are not at all clear to me but were probably part of the fast one, the Commonwealth government exempted the insurance industry—

**Senator MILNE**—Yes, I was going to come to that in a minute.

**Mr Renouf**—from reporting to APRA on this product. If I can draw a contrast with public policy in relation to some other areas of insurance, during the eighties and nineties there was a lot of debate about the quality of consumer credit insurance, the kind of insurance you get when you take out a loan, which is supposed to insure you if you are unable to pay because of disability, unemployment or death. There was a lot of concern in the consumer movement that this was very poor value insurance. The publicly available figures on loss ratios were very useful in taking it up to the insurer and saying that, unlike with motor vehicle insurance, boat insurance and other insurance where consumers get paid back 85, 90, 95 or even 100 per cent of the money that is paid in premiums, in that particular case only 31 per cent of money paid in premiums was returned to consumers. That sort of prima facie raised the question that the market was not working very well to get the right price. A lot of it was disappearing in commissions to finance companies and car dealers. But we just do not have the figures because they are solely within the preserve of the relevant insurers and not reported.

**Senator MILNE**—Okay. This seems to me to be a really key point, that there is no transparency, that the community has no way of finding out how many claims are paid out and to what extent, how many are still in dispute. We do not know anything about the premiums-to-payouts ratio and we do not have any reporting as far as APRA is concerned. I would like to visit that issue of the decision in 2001—that Commonwealth regulation that was then implemented in 2002—to exempt this insurance from the financial services regulatory regime. Do you know or has CHOICE been told or do you have any evidence as to who sought that regulation? How did it come about? If that were repealed, what changes do you think that might be able to facilitate?

**Mr Renouf**—I am not currently aware of whether CHOICE was involved in that in 2001. I was not with CHOICE at the time. I will take that on notice. There are three things. The first is that obviously, as a matter of principle, this is consumer insurance that is meant to benefit

consumers, so there is no reason at all that I can see to distinguish the way in which it is regulated and reported on from other forms of consumer insurance. I cannot see any justification for that exemption. Secondly, on your question about what would happen if it were changed, if it were changed we would know only that, for the premiums that are paid, a certain amount is returned to consumers. We might have some clues about where the money goes in terms of how much is in commissions and how much is in insurers' profit and how much is wasted through administration et cetera. I think we know enough about the way this works to say that making that information available will not solve the problem.

**Senator MILNE**—No, of course.

**Mr Renouf**—I think we know that there are some structural issues—what I said before about the misalignment of incentives, which is essentially the problem that it is a last resort scheme compounded by the fact that we have long and lengthy dispute resolution processes. Fixing the dispute resolution processes would be a substantial step in the right direction; it probably would not do everything, but it would help a lot, I think. Any future system that involves insurance as opposed to some sort of compensation fund, which I think may be the preferred option, would need to have that transparency, absolutely.

**Senator MILNE**—You have said that you cannot get the actual figures. Have you had any anecdotal evidence as to the size and nature of the commissions that are being paid as a result of these insurance products being delivered—what commissions the brokers are getting?

**Mr Renouf**—We have not, no. If I were to investigate that question, I would first turn to Consumer Action and wonder whether through some of their casework they had seen documentation which revealed that.

**Senator MILNE**—But basically it is reasonable to say that this is a secret of the insurance industry and their brokers, and that it is a multimillion dollar industry for them?

**Mr Renouf**—I think that is reasonable.

**Senator MILNE**—Okay. At the very least we clearly need to get substantial transparency in relation to this insurance. In terms of transparency, what happens with other insurance products? What are they required to divulge?

**Mr Renouf**—They certainly divulge the information that is used by APRA to publish information about their loss ratios. In some areas, there are specific requirements to disclose commissions. The area I am most familiar with is consumer credit insurance, where that requirement has been around. It is in the credit code. I think it was in the previous legislation in New South Wales and Victoria. I am trying to remember what the Corporations Act requires in relation to disclosure in a product disclosure statement, whether it requires disclosure of the fact of the commission or the amount. I am sorry, I cannot remember. I will also take that on notice if you like.

**Senator MILNE**—You said in your evidence that you do not have any figures on the number of last resort insurance claims and a breakdown of outcomes in terms of the numbers rejected because they did not satisfy the conditions, the number rejected for other reasons, the number

accepted in full et cetera. Presumably there is nowhere that you can get that information at the moment?

**Mr Renouf**—The only data I am aware of is what is published in the Productivity Commission report, which suggests 3,500 claims.

**Senator MILNE**—But it does not answer those questions?

**Mr Renouf**—No.

**Senator MILNE**—Finally, do you support the Queensland model?

**Mr Renouf**—Yes.

**Senator JOYCE**—I was having a look in the submission where you support the Queensland model. What you are basically saying is that, in your analysis of this, more or less what you are getting with the home warranty insurance in New South Wales is a form of de facto key man insurance, that if the builder dies or disappears you have a possibility of a payout, but if he is just dodgy you have no hope.

**Mr Renouf**—The comments are not limited to New South Wales. They certainly apply in Victoria and some other states as well. By its very nature, this last resort insurance scheme applies only where (a) the builder has some liability to you—you have shown they have not done adequate work and they should fix it or pay you compensation—and where (b) you cannot recover the money from the builder. So, first of all, you have to go through some sort of process to get a decision that they are liable, and in some states that has to be a court process. Secondly, you then have to seek the money from them, and either they pay you or they do not. If they do not pay you, you have to show that they are insolvent, dead or have disappeared. And only then can you turn to the insurance company.

**Senator JOYCE**—By that point in time, you have racked up a legal bill with your local solicitor that is worth about the value of the house.

**Mr Renouf**—It could well be, and you have also become really frustrated and had all sorts of other social problems and costs to the community and whatever because of the stress in your life.

**Senator JOYCE**—What seems to be clearly pointed out by the previous witness and you is that you want it to be accessible and quick, so I have used the word ‘expedient’, and independent of the Office of Fair Trading as a dispute resolution process.

**Mr Renouf**—I am not familiar with all the details of the on-the-ground issues that people have had with particular regulators in particular states. I am not sure that I agree that there is a structural problem in relation to whether it is in or outside an office of fair trading. You will get the opposite view in Victoria, I think, where building disputes are handled outside the office of Consumer Affairs Victoria, that the body that manages those disputes has come in for some criticism. I think it is more about the quality of the dispute resolution process and the ability of that process to make a determination quickly.

**Senator JOYCE**—Okay. I saw your recommendation that you believe the Queensland model is an appropriate model. I cannot find it now, but you talked about the fact that it also covered you for subsidence and a few other issues. What would you say is the strength of the structure of the Queensland model?

**Mr Renouf**—The strength of it is that you have close feedback between the dispute resolution, licensing and compensation systems—they all work in harmony. If somebody is going through a dispute process and they are not paying, you can say, ‘Do you want to keep having a licence?’ That is an incentive to fix the problem. Similarly, in the home building warranty last resort system, the insurer only cares about that fundamental test of whether the builder will become unable to meet the claim, so their interest is only in that, whereas the compensation scheme is obviously interested in people having quality work, so they can monitor. If they have seven claims from somebody, that can be fed back into the licensing process.

**Senator JOYCE**—In that sort of tripartite arrangement that you are talking about in Queensland, the pressure point is that the body can go to the builder through the process and say, ‘Look, if you keep playing up, we are going to take your licence off you. Then you will have a bit of a problem trying to get a loan from a bank because you will not have a builder’s licence.’ Would we be able to incorporate that process into New South Wales legislation? And for want of a better word, we have used ‘the mate’s club’ before, but let us be more politically correct: do you think there are certain political pressures that would work against having a Queensland model incorporated into New South Wales?

**Mr Renouf**—First, CHOICE is a national organisation, and I do not want to be stuck on commenting on New South Wales, and, secondly, I do not think I am in a position to make that call. Personally, as opposed to through CHOICE, I have some experience just as a citizen of the Northern Territory where I was for 10 years, and the building industry is a very important industry in the Northern Territory—

**Senator JOYCE**—It certainly is at the moment.

**Mr Renouf**—There were a number of situations where builders became insolvent and consumers lost their dough and not much was done to fix that problem at that time in the nineties. There are going to be political pressures in both directions, I imagine, but I do not think I can comment on the substance of your question about New South Wales.

**Senator JOYCE**—You also stated that you find the bank ombudsman is a good process. I agree with you on that. Fleshing it out further, what is the factor in the bank ombudsman process that is effective that you could overlay into this process? This process in New South Wales just seems like a complete dog. It needs to be thrown out and started again. What is the process in the bank ombudsman that you would have in a new board?

**Mr Renouf**—The structure of the dispute resolution in financial services has a number of features. The first is that it is a condition of your licence that you belong to an external dispute resolution scheme. The second is that the external dispute resolution scheme, which industry bodies are free to set up, must meet certain criteria which are set out in the ASIC policy statement 139, and there are six criteria—I will not remember them all, but they are effective,

efficient, fair, accessible, independent and something else. I would refer you to policy statement 139 for the full details; it is not very long. They are reviewed every three years. The features are that they are free to consumers to use and there is a small fee charged to the respondent—bank, credit union, whatever—if a complaint is made.

Another feature is that you have had to have at least a go at working it out with the person you are contracted with, in that case the bank—here the builder—before you take it to the dispute resolution scheme. I am not saying that every feature of this scheme in that industry suits here. Of course, in banking there is a more limited number of industry members, but I would say that it does also work reasonably well for the financial planning industry, the FICS, Financial Industry Complaints Service. They will be merged shortly, but that system deals with a much broader industry of smaller players than the banking one. It also seems to work. They are free to consumers, they are relatively accessible, they are relatively quick, they have internal expertise, there is an industry stake in the running of them—there are a number of features that help. I am not saying that that is the only way you could do it, but I think that is a good starting point. Obviously, in building you have that question of on-site inspection that is going to be much more important than in the banking industry where you can often do things on the documents and what people say on the phone.

**Senator JOYCE**—Okay. Two final questions, and it is a yes or no answer: first, when consumers get themselves tied up in this home warranty insurance program in New South Wales, do they actually get like a CIB, customer information brochure, that someone hands to them and says, ‘This is what you get; this is what you don’t get; you had better read the front page. It says that it is not worth much, but if you take it to the toilet, you might find another use for it.’

**Mr Renouf**—I think my answer is, I do not know the answer to the question, but I am not sure that, for all the reasons we have talked about, the fact that it is the builder who contracts with the insurer and not the consumer, that the insurance company is focused on the risk of the builder going insolvent, not the risk of the builder failing to do the work.

**Senator JOYCE**—None of the actual homeowners actually gets a brochure?

**Mr Renouf**—No, I am saying I do not know, But I am not sure how relevant they would see it, given it is compulsory and, if they did read it, they would find out that it was not really—it is compulsory, they have to do it. You are going to take out a contract to build a house; you are going to spend \$100,000 or \$200,000 or whatever it might be, and the builder says you have to take out this insurance for \$1,500 or \$2,000 and there is nothing you can do about it. How much effort are you going to put into thinking about it (a) given its relative cost in the size of the transaction, and (b) the fact it is compulsory—

**Senator MILNE**—And you could not do anything about it anyway—

**Senator JOYCE**—Well, with CLERP legislation, they became very insistent on your getting customer information bureaus and people knowing exactly what you were offering them—

**Mr Renouf**—Yes, but that is when you had a choice.

**Senator JOYCE**—You had to do a needs analysis of the whole thing, and the first thing you had to disclose to your client was exactly what their insurance meant. If you could not do that, you were liable. The final thing is—and it is sort of backing up what Senator Milne said—does anybody know where this compulsory money has gone? Where is it? Who has it?

**Mr Renouf**—It has to either be with the broker or the insurance company, less whatever has been paid out in claims, and we do not know the numbers for any of those things.

**Senator JOYCE**—That is a very interesting path to follow. Somewhere there is a big bucket of money that somebody knows something about, and we want to know where that bucket of money is and who their mates are.

**Mr Renouf**—You would need to ask the bureau and the Housing Industry Association.

**Senator JOYCE**—We are trying.

**Senator EGGLESTON**—This is just a form of insurance against a defect or a loss. What stops general insurance companies from getting involved in this? Why could not I, as a builder of a house, go along to QBE or SGIO in WA and say, 'Insure me against the risk of defects in this building that I am building?'

**Mr Renouf**—First, this insurance of course is not insurance against the defects; it is insurance against the builder being insolvent and unable to pay a claim.

**Senator EGGLESTON**—But in the sense of failure? I am not using the words very precisely.

**Mr Renouf**—I know what you are saying. Why could you not do that? I guess because, first, there are no insurance companies offering that product, so the question is: why would they not? I guess they do not see a big enough market to develop a product. Again, I guess that is a question that you might want to ask the Insurance Council.

**Senator EGGLESTON**—If it is well known that this home warranty insurance is so shoddy and does not deliver, as it seems not to—it does not provide general cover—why would not the general insurance industry be interested in providing an effective product?

**Mr Renouf**—I think the answer is probably the same answer to the question: if you did not have compulsory insurance would enough consumers take out voluntary insurance to ensure that most of them were protected? I suspect that people probably would not take it out to the same degree. We already have a situation where people are probably a bit underinsured in relation to homeownership. There are areas of insurance that are important to have, and that for many people is one of them, and there are some who do not. There are some issues to do with consumers' perceptions of risk and consumers' perception of future risk. They are choosing this builder because they have some recommendations from friends or whatever—they trust them.

**Senator EGGLESTON**—Yes, they do. But they also have an assumption that the insurance they are offered under HBWI will cover them if there is a problem.

**Mr Renouf**—I think some do have that assumption.



**Senator EGGLESTON**—Most of us are fairly naive about these sorts of things, so if there is insurance we think it covers problems.

**Mr Renouf**—Sorry, I have given you a whole lot of reasons I guess in the context of if there was not HBWI. You are saying if there is HBWI then why would you take out alternative insurance, because you think you have a warranty? I think that is right.

**Senator EGGLESTON**—So is part of the solution to this broadening the access, if you like, for the insurance industry to become involved in providing protection to the consumer—in this case, the person who is building the house—against defective workmanship and failure on the part of the builder?

**Mr Renouf**—There seems to me to be three options. Assuming you fix up dispute resolution, what do you do about the cases where the builder cannot pay the claims? It seems there are three options. There is a system like Queensland's; there is a system like the one we have now but with improved transparency and improved coverage for home building warranty and last resort insurance; or there is voluntary insurance. I think the voluntary insurance would be the worst option.

**Senator EGGLESTON**—Really?

**Mr Renouf**—Because I just do not think that the consumers who need protection will, in sufficient numbers, choose to take out the insurance.

**Senator EGGLESTON**—That is a very interesting answer, because I think people are more aware of the need for coverage than perhaps they have been in the past.

**Mr Renouf**—I guess if Tasmania goes ahead with its proposed scheme we will find out.

**Senator EGGLESTON**—We will. In another context, I know that you are aware of the Productivity Commission's recommendation about Australia considering introducing laws covering unfair clauses in consumer contracts. Would that kind of law, if it were in place, be of assistance in this context? It would appear to me that these are unfair clauses because they are not providing the service that the consumer thinks they are.

**Mr Renouf**—My understanding of unfair contract terms legislation—

**Senator EGGLESTON**—It is on standard contracts.

**Mr Renouf**—On standard contracts—is that it is focusing on the terms of the contract. The problem here is not so much the terms of the contract but the description of the insurance as a warranty, which, as has been pointed out, does not really correspond with the normal consumer understanding of what a warranty is.

**Senator EGGLESTON**—Exactly.

**Mr Renouf**—I am not sure that it would, is my answer.

**CHAIR**—Okay, one final question.

**Senator MILNE**—We are trying to get as much statistical evidence as we can, so I just want to ask you if you have these and if CHOICE could provide them: for example, has CHOICE done any work on the number of building contracts every year, the number of licensed builders and the trend over time, things like—

**CHAIR**—We can provide you with this list in written form.

**Senator MILNE**—It is really these issues of numbers in relation to trends of those buildings, how many people are in noncompliance effectively, and things like the number of consumer complaints as a proportion of building contracts. Have you done any work on compiling—

**Mr Renouf**—We have done that kind of work in some other industries, not in building to date. I would imagine that some of that data was in the Office of Fair Trading and/or building bodies annual reports in the various states. It would be a question of adding up the state-by-state figures that were available. Anyway, I do not have them available.

**Senator MILNE**—But CHOICE has not done it?

**Mr Renouf**—No.

**CHAIR**—Thank you, Mr Renouf. The committee will have a break before we have a submission by teleconference.

**Proceedings suspended from 10.38 am to 10.49 am**

**STOKES, Mr Michael, Private capacity**

*Evidence was taken via teleconference—*

**CHAIR**—Mr Stokes, thank you for coming here this morning by teleconference. Would you like to make any comments on the capacity in which you appear and then, if you wish, make an opening statement?

**Mr Stokes**—I was the CEO of Housing Guarantee Fund, which was the builders warranty body in Victoria. Basically I wanted to make a submission to this committee as well as to the Productivity Commission earlier in terms of why I think that builders warranty would be better away from private hands essentially.

**CHAIR**—Thank you. Are you arguing that the former Victorian Housing Guarantee Fund was a reasonable system that is better than the current arrangement?

**Mr Stokes**—I believe so. It was never perfect, but it was a lot better in terms of consumer protection and processing claims than, from what I understand, the present system is.

**CHAIR**—In what way does the Victorian system work at the moment and how is it unsatisfactory compared with a perfect system?

**Mr Stokes**—I guess the difference between HGF and, I believe, the Queensland model and others that work, compared to today's, is that the term has come to be 'last resort insurance', which is essentially that the builder must be dead, insolvent, disappeared or all three before a claim can be processed. I think that is the significant difference. If a consumer has a problem with a builder, they cannot actually make a claim if the builder is going bankrupt until liquidation has occurred, so they just have to wait. If the builder does not do any of those three and just refuses to go back to the job to rectify or to complete, there are really no avenues other than legal, and they are fairly costly for a consumer to take. With the Queensland system and with HGF, essentially you brought your claim to the fund. The fund would start to investigate it straightaway, regardless of the status of the builder. The builder was always invited to turn up, to respond, to do whatever, but essentially the fund would pick up the claim and begin to process it. I think that is the fundamental difference. It was a warranty body that essentially was the guarantor of the builder's performance, as opposed to an insurer. It just treated it on the basis that there would be claims every year, hundreds of them, and they were a natural part of the industry, so this was the way that it was processed. It is as simple as that.

**CHAIR**—Why was there a changeover?

**Mr Stokes**—I was with HGF until 1992 and then back again in 1997. When I heard that it went to a privatised system I was a bit surprised. I think that there was a parliamentary estimates paper that did in part recommend some competition, that it would be better for it to be not a monopoly. My opinion was that all the time the state had control of that monopoly, it could basically set the fees, make sure it was not too expensive, it could appoint the right people and so forth. Following the line of privatisation to bring in competition, because HGF was quite a

unique body—it was a public company limited by guarantee and it specifically was there to do that task—once it was privatised it was not allowed to be in the arena. There were reasons for that. It had certain tax exemptions to keep it cheap to process. It did not pay company tax. It paid the normal income taxes and the like, but it was a not-for-profit company—that was the point of it all. To be honest, I cannot really explain to you why it became privatised.

**CHAIR**—The current insurance arrangement is not being asked to do what the Victorian guarantee fund is doing. It is a lesser system altogether, isn't it?

**Mr Stokes**—Correct. It will only process the claim providing, as I said, the builder is DID—dead, insolvent or disappeared. Then it will say, 'We now have an insurance claim and we will process it accordingly.' The biggest problem that I see with that is that, in the area of defective workmanship, my memory was that approximately 70 per cent of defective workmanship cases were builders who were still registered and still operating and simply refused to go back. If that is the case still today, then the consumers have no chance. We would make them go back if we had come to the conclusion that it was their problem, and if they simply refused to go back whatsoever we would organise then to have the defect rectified, paid for, and then we would seek financial recovery from the builder.

**CHAIR**—The Victorian dispute resolution system does not achieve that at the moment, you believe?

**Mr Stokes**—All the anecdotal evidence I am hearing is saying no. As a company, we dealt with VCAT—the administrative tribunal—on a quite regular basis and for a consumer to tackle that is not an easy process.

**Senator EGGLESTON**—You say the necessary elements of a warranty system are a licensing authority to check technical competence of builders, adequate inspection of houses during construction, a warranty body to provide cover and process consumer complaints and an appeals mechanism for owners and builders.

**Mr Stokes**—Yes.

**Senator EGGLESTON**—Could you tell the committee for the record how Victoria handles each of these elements at present, and does it do so satisfactorily?

**Mr Stokes**—To my understanding, as far as the licensing is concerned, or the registration, builders are registered with the building commission in Victoria, but I am not certain as to the qualifications they apply in terms of selecting a builder. We did do that as a warranty body, so the builder was connected to his work, connected to his claims. I know that they basically register them at the present moment, but I am led to believe again that they will only do so if an insurer gives them a letter that says they are prepared to insure that builder for his work. If that is the case, I do not see that the registration body is really adding much to the scheme at all.

As far as the scheme cover is concerned, that has been increased through the years. I think it is now approximately \$200,000, and I think that is in both New South Wales and Victoria. But that is a bit smoky because there are various restrictions in it that quite often consumers do not get the full entitlement. As far as the claims handling is concerned, there is a body that was invented

in Victoria, BACV, and that was supposed to handle complaints from owners where the builder was still in business but would not go back. I do not think they have any real power. I am pretty certain that they do not have access to the administrative tribunal and they certainly have no access to the insurers because in those instances the builder is still around. As far as the actual processing of claims at the end of the day, I do not know. I cannot see why insurers would hold that up or do anything untoward in that regard.

**Senator EGGLESTON**—You said there is that cover of \$200,000 in both Victoria and New South Wales. Is that indexed? I do not think \$200,000 is going to cover the cost of many buildings these days.

**Mr Stokes**—It actually does in the sense that what happens is that you will take out, say, a \$300,000 contract with the builder, and you may have paid \$100,000 or \$150,000 on the way through, so you have, say, \$150,000 left in your pocket. If the builder fails, it would be a fairly massive claim for it to be for \$100,000. The insurance body would pay that, but do not forget that you still have the \$150,000 from the original contract. So if it turns out that your house actually costs \$400,000 to complete, in that case you are not out of pocket.

So the \$200,000 is probably not a bad ceiling. However, there are certain restrictions on it in walk-away, where I believe most of them apply a percentage against the contract price. If the contract price is, say, \$300,000, I believe they still have a 20 per cent factor, where they say that the maximum they can pay for a walk-away claim or for a builder failing to return or going bankrupt is 20 per cent. So they would pay a maximum of \$60,000 in that instance.

**Senator EGGLESTON**—Do you think that is a fair arrangement for the consumer?

**Mr Stokes**—We did not do it that way. We would simply pay out. Our limit then was only \$40,000, but that was quite some time ago. If the first owner had a \$35,000 claim, leaving only \$5,000 behind for later claims, then so be it, but at least it got the owner past the first hurdle. I think the percentage could be higher, let us be honest.

**Senator EGGLESTON**—That is one thing, the percentage could be higher. Going back to my first question about indexation, because we have to allow for inflation and things like that, do you think it would be desirable that there should be some sort of indexation of that basic limit amount?

**Mr Stokes**—I do not see that it would hurt, let us put it that way. At the present moment I think that that particular limit is basically enshrined in legislation, so to amend it you would need to amend the legislation each time. But if it is possible to index, I do not see why not.

**Senator EGGLESTON**—I think that is even more worrying if it is enshrined in legislation; it should also include some sort of indexation, in my view, because things do change.

**Mr Stokes**—Yes, I am not arguing.

**Senator EGGLESTON**—Your point 3 is for a warranty body to provide cover and process consumer complaints. There is some criticism of that kind of view in the insurance industry in that there is a moral hazard, it is claimed, if the same body not only provides the cover but also

processes complaints. Would you like to comment on that, or should they be done by separate bodies?

**Mr Stokes**—No, it can be done. I think the difference here is that the way this scheme was funded in this arrangement was that, instead of treating it as an insurance premium, we would work out actuarially how much it was likely this one year of housing would cost for the next 10 and we would collect sufficient money plus future earnings to basically build a fund to say: ‘This is inevitable these claims will arise. It is an inevitable part of the building industry.’ So we took the attitude: ‘This is not insurance. What we are doing is providing cover for people where we know it is going to happen one way or another.’ I think the statistics that we kept said that one house in 10 would finally end up deriving some sort of claim or some sort of process that was required. Bear in mind we were spending our own money and it was collected specifically for that purpose.

We would have experts in terms of assessing the claim. We had our own in-house inspectors, and they were generally all ex-builders, so they knew what they were looking at. But if there was ever any difference of opinion we would also have engineers and various technical experts that we could send to the job and say, ‘Is this just one of those things or is it the result of workmanship?’ And, finally, there was the Administrative Appeals Tribunal, where people could go and appeal it. Let us just say that, in the main, we lost very few cases because we were quite expert at assessing them. So I do not think it is so much a moral hazard; we were not looking for one way or another. I think in the statistics that you may have up there you will see that we rejected about 35 per cent of all claims, so it was not all one-way traffic.

**Senator EGGLESTON**—That is very interesting, but you are still talking about a 10 per cent problem rate, if you like.

**Mr Stokes**—Yes. It is quite high in my opinion.

**Senator EGGLESTON**—It is quite high. Is the answer to that a different kind of licensing regime under which builders who consistently have problems with their work are not relicensed? Should builders be relicensed on a periodic basis of, say, three years?

**Mr Stokes**—One of the problems that I have with the licensing arrangements in Victoria—I do not know about New South Wales—and I certainly had the same sorts of qualms when I was with HGF when it was actually operating, is that it is basically like a golf club: you go through your initial assessment and you are accepted onto the book as a builder, and from then on in, provided you paid your annual fee to remain on the register, you could remain on the register. I ran statistics in the past—and I do not see that they would be any different—where many builders, for whatever reason I do not know, registered as a builder and never built a house but they could always go out and build one tomorrow if they chose to. Some builders were three, four or five years between jobs. I used to think to myself, ‘I don’t know why they can just be allowed to do this.’ It ought to be like a current licence, some sort of annual assessment, in my opinion.

**Senator EGGLESTON**—You would have an annual assessment, and also there should be some criteria that they should be actively building, so if they have not been building for three years they do not get relicensed in one year?

**Mr Stokes**—It could be. Let us assume that somebody has not built for two, three or four years and then suddenly registers a particular job. I would think that in that particular instance you would want to apply a series of close inspections to the work to make sure that it is not just effective but that it is up to date as well.

**Senator EGGLESTON**—How are builders accredited for registration in the first place? What criteria are applied?

**Mr Stokes**—In Victoria, I think the most significant thing is that provided they receive a letter of acceptance from an insurer, the likelihood is they will take the builder on. That is what I believe. When we did it, there was the good repute and character and there was the technical skills. But the other thing we used to do was look at the financial capacity of the builder to actually build, and we would do that on a sliding scale: you appear to have enough working capital to build, say, three houses at any one time—not in a year, but at any one time. We would only license that builder to build three houses at any one time. Once he had registered three, he received no more registration until such time as he completed the work. Later, as he built up capital and built that sort of thing, you would increase the limit.

**Senator EGGLESTON**—Should there be a sort of a checklist against this as criteria every time they reregister?

**Mr Stokes**—I think so, and that is what I say in my paper. When there is the annual renewal process—if that is what happens—there ought to be checks from the licensing body back to a warranty body or the insurers today to effectively say, ‘Has this builder had any claims this year?’ I think that ought to be taken into account. I do not believe that it is at the moment.

**Senator EGGLESTON**—Obviously this problem affects everybody in Australia.

**Mr Stokes**—Yes.

**Senator EGGLESTON**—I come from Perth and I certainly know about problems with buildings there. You say there should be a national scheme. How would that be achieved under a federal system, because building standards and the business of warranty insurance seem to be very much state matters?

**Mr Stokes**—It is. It arose out of state legislation. If you go back to 1984, there were two states, New South Wales and Victoria, that had it and nobody else had it at all. Then it started to come in in different forms because I think it was a state government initiative. What I would like to see, I guess, is something like the game of cricket, that there is a fundamental set of rules established at the national level. It should not be that hard to establish. It would be to do with general qualifications and licensing of builders and there ought to be two types of claim you can have, financial failure of a builder and defects in workmanship. Basically, that should be laid down. And then, to a large degree, the states could run it, provided that the common principles were there.

**Senator EGGLESTON**—Could APRA have role, or the corporations regulations? At the present time the regulation excludes from the disclosure regime insurance entered into for the purposes of a law that relates to building or construction.

**Mr Stokes**—Yes.

**Senator EGGLESTON**—Would reversing that exemption provide a means of national scrutiny of all of this issue?

**Mr Stokes**—I am not quite certain in that regard. APRA is to do with insurance, and HGF was never an insurance body or an insurance company. It was essentially a fund that was created to pay for inevitable claims. The only insurance that we took out was, having established—for the sake of fact of argument—that in this current year maybe \$10 million worth of claims would arise, we would collect sufficient so that, through time, the fund would cover the costs of admin and the actual cost of claims. Just to be safe, we would then go to the insurance world and take out what we call catastrophe cover. The insurers would look at it and say, ‘You seem to have got this pretty well covered, but you are looking for some cat cover, so we might insure for another \$5 million over the top,’ and that meant that we were safe. That is my problem; I just do not see this as insurance.

**Senator EGGLESTON**—Fair enough; I understand that point. But there is that exemption there, and one of the issues, I suppose, is whether that exemption should be removed.

**Senator MILNE**—Mr Stokes, I want to go back to a point you made about Victoria changing to last resort in 2002, and also the decision to privatise. In hindsight, what do you think was driving the process to privatise? We have had CHOICE say this morning that it was essentially a try-on from the insurance industry that worked. What is your take on why it was privatised in the first place?

**Mr Stokes**—I think there was a change of government in Victoria at about that time, in 1993-94, whenever, and I believe that the ideology of that particular state government was to reduce regulation and to privatise where it could, but I think that was a matter of ideology. I think there was a lot of that going on with it.

**Senator MILNE**—What about the move to last resort?

**Mr Stokes**—What happened there, I believe, was this. You essentially had two main insurers in the country. There was Royal Sun, which is today Vero, and they pretty well insured all of the HIA builders. Then there was HIH, which pretty well insured all of the MBA builders in Victoria. I think in New South Wales HIH probably insured a little bit more. The break-up in Victoria was about 35 per cent HIH and 65 per cent Royal Sun, or Vero today. When HIH collapsed, I think that was the big spark, because Vero found itself alone, virtually a monopoly. There were other insurers around, but they were not very big. Vero saw the magnitude of the warranty claims with HIH, and they had had some bad claims experience themselves, and I think what they did—and again this is only my opinion—was that they went to the government and said, ‘If you wish us to remain in this industry, these are the terms and conditions that we want, and it is not really negotiable.’

**Senator MILNE**—Okay, which government are we talking about that they went to making these sorts of claims?

**Mr Stokes**—The present Labor government in Victoria.



**Senator MILNE**—Do you have any idea about the premium to payout ratios?

**Mr Stokes**—No, I do not.

**Senator MILNE**—Not even anecdotally?

**Mr Stokes**—Premium to payout ratio?

**Senator MILNE**—In terms of what—

**Mr Stokes**—Yes, well, anecdotally I have heard that they are collecting an awful lot of money and not paying very much out at all. Yes, I have heard that.

**Senator MILNE**—Okay. What about what the brokers get in terms of the kickbacks, if you like?

**Mr Stokes**—I have heard that as well. I think everybody that is associated with this has heard that. You have got HIA and MBA operating, and most builders are members of one of those associations. As such, they make for very good marketing avenues for either, and that is why I said back then HIH used to do MBA and Vero used to do HIA, although there was some crossover. In the main, that was the set-up. If they are your main associations, and they become your main marketing channels, then I guess it is up to the associations—if they wish to be commission agents, then they can be. I think it is possibly a conflict of interests, but, yes, that is true.

**Senator MILNE**—And we do not know what those commissions are?

**Mr Stokes**—I never knew. I believe that there have been some stabs in the dark, but I do not think that anybody knows.

**Senator MILNE**—Do you know anything about the structure of those housing industry associations? Is there any democracy in them? Do the members actually get to vote for anything?

**Mr Stokes**—I believe so. They are both meant to be peak bodies to represent builders, their interests, political lobbying, blah, blah, blah—all the normal things that those associations are created for. I know they pay the fees. They do a lot of training. They provide an enormous amount of paperwork for the standard builder, so that he has proper, decent contractual arrangements. I believe they can vote, but that is about all I know of them.

**Senator MILNE**—Just to go back to a point you made about the financial competence of builders in Victoria, you said that is something that you used to do.

**Mr Stokes**—Yes.

**Senator MILNE**—Who actually does that now?

**Mr Stokes**—I believe it is the insurers, because the Building Commission, who is the registration body, have no real interest that I can see in knowing any of that information. Either the builder is suitable to build, so he is registered, or he is not, and the key criterion is: can he get insurance? If he can, he is in; if he cannot, then he cannot build, so he would not be registered.

**Senator MILNE**—Basically the insurer determines whether there is financial competence and capability and the insurer is offering the product, and then you get the payback, if you like, to the associations. So it is very much a closed shop, isn't it?

**Mr Stokes**—It would appear to be. I think that the Building Commission does its best with new builders to assess that they do have the necessary skills to get on with the work. But how far it can go with that, I do not know.

**Senator MILNE**—But a consumer has no way of finding out, or any independent verification of, the financial capability, competence or whatever of the builder, whereas, when you were doing it, through the licensing you could make sure that people had the cash flow to cover the work they were doing.

**Mr Stokes**—That is right, although builders went broke with us time and time again; it is just a natural part of the industry. All that we could do at that stage was say, 'We have done everything that we could; the builder has still gone broke, so all we can do now is to basically redress the claims.' That is the way we used to treat it. We had some big failures in our time, and they just happened. There is something that somebody in the committee might want to check on. If you go onto the websites of the respective licensing bodies in, say, Queensland, New South Wales and Victoria, and call up particular builders, I think you will see quite a lot of information in Queensland, including, I believe, recommendations as to whether or not a builder is reliable. I do not think it is so strong in New South Wales, and in Victoria I think it is just, 'This builder is registered,' or he is not, and that is it. That is all you find out. The bodies themselves supply varying degrees of information.

**Senator MILNE**—So once again the Queensland system gives the consumer a greater capacity to make a judgement about which builder they may wish to go and secure the services from?

**Mr Stokes**—That is right. The last time that I did a comparison, which was about four years ago, that is what it seemed to me.

**Senator MILNE**—In the Victorian system, who does the building inspection of the houses while they are under construction, and how is that different now? In your view, is it adequate?

**Mr Stokes**—When we were doing it before the big changes in 1996, the inspection of houses was carried out via the local councils. The houses were built all in their respective municipalities and they would issue the building permit. In other words, they would come to my block and issue me with a planning permit so that I could do this, and then they would issue the building permit. Then they would actually carry out two, three or four inspections as the case might be, and then finally they would issue the certificate of occupancy. In 1996, when it was all privatised, that was privatised as well. In other words, they took that power away from the councils and said, essentially, 'Now we will have private building surveyors, the same as

privatised insurers. They may or may not be attached to the council, but they can actually go out and do this now independently of councils.'

What tends to happen is that builders latch on to a building surveyor, or a couple, if they are a big-volume builder. They do the actual inspections, and report back to the builder. There is no reporting to the homeowner. The inspections themselves are really only for safety—has this house progressed to this stage; is it safe; is it in general okay? When I say 'in general okay', that is what I mean. There is no real inspection for quality and the like along the way. I know that in the English system they do do that. Apart from checking that the house is at a certain stage and the stumps are right and the foundations are correct, and everything else, they do actually look at the quality of it on the way through. If they accept that the house has proceeded to a certain stage, that also becomes the authority for a progress payment. The inspection regime altered dramatically as well.

**Senator MILNE**—Given what you have just said, one of the ways to improve the system would be, in your view, to go back to local council and to make a proper inspection the basis for paying progress payments?

**Mr Stokes**—I think that would be a good idea. But of course, you have to make sure the inspector is reasonably independent of the builder—they are never their employees, but obviously if you are doing a lot of work for one builder the temptation could be there to possibly pass things that are marginal, if you know what I mean.

**Senator MILNE**—Yes, absolutely. What is to prevent that in Victoria right now, since the system has been privatised?

**Mr Stokes**—Nothing.

**Senator MILNE**—Do you believe that that is going on?

**Mr Stokes**—One of the interesting things that we did as a body was when we were in run-down mode, in 2001. When HIH failed, the Victorian government appointed us to handle the HIH claims. They said, 'We will fund it all; we will build a special fund. We will pay you guys; you treat these claims as if HIH was still around. So, stand in the shoes of the insurer and do that.' It was very interesting to see that in a lot of the HIH claims the quality of the work was very poor. In a lot of instances, that work had been passed at different stages by a building surveyor, and in other instances the house had actually been fully complete and that building surveyor had never been back and carried out any inspections at all.

**Senator MILNE**—What was done about that?

**Mr Stokes**—The building surveyors are also registered with the Building Commission. In a lot of instances what had happened was the same as what happened with builders. When we started to make investigations into what we found out, the building surveyor had either gone bankrupt or had just vanished; we could not find him.

**Senator MILNE**—The current situation is that the Building Commission registers these surveyors in Victoria, is that correct?

**Mr Stokes**—Yes.

**Senator MILNE**—Who has oversight of that?

**Mr Stokes**—I believe it is the Building Commission itself. They are responsible to the state government via various legislation.

**Senator MILNE**—Is there any way of checking the relationship between these building surveyors and the building companies? You have said that surveyors are often used by certain local governments.

**Mr Stokes**—No, not to my knowledge. In fact, it is fairly standard practice in Victoria now that technically the owner is supposed to hire the building surveyor and then that building surveyor basically is responsible to the owner for the inspections. Because most owners do not have a clue, what most builders do—and it is quite legitimate to do it—is they sign an agency arrangement when the contract is signed to say that you appoint me as the builder, as you, the owner's agent, and I will organise the building inspections and the building surveyor for you. Most people do it because they do not understand it.

**Senator MILNE**—Okay. That is something we clearly need to pursue with the Victorian government at some point. I just wanted to be clear about that, because it seems to me we would solve a lot of problems if we got proper inspections of buildings all the way through?

**Mr Stokes**—Yes. Everything starts with building codes, which are meant to be saying this is the way you build this house, this is the way you build various components of the house. I think they are trying to make that better and better all the time. But there is another little body of things that I know the Building Commission relies on. I think we invented it, and it has gone along; it is called standards and tolerances. What happens is you have your broad building codes which ensure that the house is safe, it is properly built and the like, but then standards and tolerances are for cases where, for example, there are gaps in the cornice or more than a 3mm-gap around the doors and various other things like that. That is considered to be poor workmanship and the builder needs to fix it. They are like one big book and one small book.

**Senator MILNE**—Finally, it is reported that there is a very poor relationship between Consumer Affairs Victoria and the Building Commission. Is that true, and what do we know about it?

**Mr Stokes**—I have only heard that anecdotally. They are a very big bureaucracy, that is true, and whether owners are able to get any satisfaction through them, I do not really know. That is one of the problems: they are a big bureaucracy and they have to follow the law, regulations and the like. I can only say that I have I have heard that.

**Senator MILNE**—Okay, thank you.

**Senator JOYCE**—There have been discussions about the close relationships between the approval mechanism, the capacity of the builder to hold the licence, and the insurance company, such to say that basically if you play up through the process, we can take your licence off you.

**Mr Stokes**—That is possible.

**Senator JOYCE**—What do you think of that idea?

**Mr Stokes**—That is what the licensing and the registration was supposed to be about, in that if there were sufficient complaints about a builders and the builder was, to use Paul Keating's phrase, recalcitrant in going back, then that mechanism allowed us to say, 'Okay, you will now lose your licence. You cannot build again so we are taking your livelihood away from you.' That is always possible. We had that power, but the other thing we used to do was, if a builder had caused a claim and was a bit tardy in going back to fix it, restrict the amount of work that he could actually do. We used to call it a conditional limit on his work, and say, 'You don't get any more registrations until you've resolved this issue.' So, he kept his licence; he could still operate, but he had a temporary block on him for the time being until he tidied up this particular claim. There are ways and means, but then again, HGF was a monopoly body, so it did do the licensing and it did do the warranty claims—so it did have control over the builders in that regard. At the present moment, as you can gather, it is decentralised. Insurance is done by the insurers; registration is done by the Building Commission or the licensing bodies in each state. I do not think that the coordination between them works very well. The other problem that you have is that there is no register of properties in any state, so that you know what has been built and what the claims are. They are held by the insurers, and you cannot get at them. With us, it was an open document.

**Senator JOYCE**—I heard your discussions with Senator Eggleston, Senator Milne and Senator Hurley that basically covered what I would have discussed with you in any case. You also believe in greater transparency. I am more concerned, as we go through this inquiry, about the transparency of exactly where this money is going. We know that it is compulsorily acquired, but somewhere there is quite a substantial amount of money. You gave evidence that the amount paid out in claims is quite insignificant compared to what is collected. Who is making the money, and what sort of relationship, if any, do they have with people who have authorised the decision for that money to be collected. That is a very interesting question, I think, that we have to get to the bottom of.

**Mr Stokes**—That is right. There are two lots of money, as you know. There is the agency fee to actually sell the insurance in the first place, so I presume that is just a fixed rate and HIA and MBA and whoever else is involved get that. As far as the actual premium finally received by the insurers, I guess it is going there. If they are not paying too many claims then it must be a very profitable product line.

**Senator JOYCE**—However, a couple of people, as you have read in the press, have decided not to front this inquiry. Do you have any reason to think why they would not?

**Mr Stokes**—I guess that they are the main players in the industry. I know what I personally think, but—

**Senator JOYCE**—You have parliamentary privilege, so you can say whatever you like.

**Senator EGGLESTON**—You can say whatever you like to this committee.

**Mr Stokes**—I just think that there is good money being made from the scheme as it stands at the present moment, and good money being made by those two bodies. Essentially, any regulation or reversal of the present system, say, back to a Queensland type model, would seriously threaten that income to the both of them. I guess that is it.

**Senator JOYCE**—Thank you very much for that.

**Senator MILNE**—My question relates to this power that you have referred to. Obviously those two bodies are getting quite a lot of money, but also power. What is your comment about the appropriateness of essentially an insurance industry being able to determine who can and who cannot build? Essentially, that is an enormous power. Is there any comment you want to make about the misuse or use of that power?

**Mr Stokes**—Again, if you look at Queensland and you look at the old HGF model, we were everything rolled into one. If we were going to take on builders, we would only take them on if they appeared to be a reasonable risk. I guess that insurers have the same right, but I do not know to what extent they are exercising it, and I do not know what part HIA play in that role in terms of assessing builders as applicants for insurance. I really do not know. I guess you cannot just say to an insurer, ‘You will take on all risks whether you like it or whether you do not.’ We used to reject builders up front. They would come along but did not have the experience or the cash, or did not have something, so we would say, ‘Look, I’m sorry; go away, sort yourself out one way or the other and then come back in 12 months’ time and see if you make it then.’ That is all I can say to you.

**Senator MILNE**—Did you have to provide reasons, though?

**Mr Stokes**—Yes.

**Senator MILNE**—At the moment it seems like the insurance company can just say to someone, ‘Either you do as we say or we will not give you insurance’, and they do not have to provide reasons.

**Mr Stokes**—No, we did. We would write them a letter and say, ‘We will not be registering you as a builder because of this, this and this.’ If they wanted to, they could come in to that particular arm of the company and discuss it with the manager there, and he would tell them what it was that they needed to make the grade.

**Senator MILNE**—Did you require bank guarantees from builders?

**Mr Stokes**—We did at a later stage, but they were different in terms of their magnitude. I am led to believe now that bank guarantees can be quite horrendous—\$200,000, \$300,000, half-a-million, \$1 million of bank guarantees. We went down that path, but we did it by breaking our builders up into classes of work and classes of claims and saying that on average all builders in this particular class will cost us, say, \$10,000, not hundreds of thousands. We would then apply a bank guarantee against anybody in that class of \$10,000, but it was not the half-a-million and the exorbitant figures I am hearing today.

**CHAIR**—Thank you for giving evidence to the committee today. It has been very useful. I should state for the record that players in the building industry, like the HIA, the MBA and the Insurance Council of Australia, have put in substantial written submissions. The HIA have said to the committee that they do not wish to appear. The Insurance Council of Australia said that they were unable to attend today. There has been no real refusal by those bodies to attend. Thank you, Mr Stokes.

**Mr Stokes**—Okay.

[11.38 am]

**HOWARD, Mr Jerry Anthony, Deputy Executive Director, Master Builders Fidelity Fund**

**CHAIR**—Welcome. Do you have any comments to make on the capacity in which you appear?

**Mr Howard**—I am also the Deputy Executive Director of the Master Builders Association of the ACT.

**CHAIR**—Would you like to make a brief opening statement for the committee?

**Mr Howard**—Yes. For the committee's benefit, I will give some background on why the Master Builders Fidelity Fund was established in the first instance. It was established in response to the crisis that we had when HIH collapsed back in 2002. The industry in the ACT was in a pretty perilous situation at that time in that a lot of small builder members were just about to go to the wall because they could not obtain home warranty insurance. At that time we approached associations in the ACT with similar interests to ours saying that we should drop the whole idea of home warranty insurance. However, the government at that time did not agree to that because we still had an insurance provider that was operating in the ACT. The insurance companies at that time were placing very onerous provisions on applicants obtaining insurance, especially some of the smaller operators who work on very low margins. Essentially, they just could not start work; they just could not commence work. We also had a large number of speculative projects in the ACT, because, if you understand the industry in the ACT, there are a lot of speculative projects that are built and sold on. At that time they probably would have been about 60 per cent.

The master builders at that time had negotiated an arrangement with the authorities that builders could commence work on those projects, but prior to selling those projects they required home warranty insurance so that a certificate of occupancy could be issued in the sale transaction. At that time, coming up to about March, April or May, we had about 300 builders with houses that they could not actually exchange contracts on because they could not get insurance. We were receiving lots of calls from the banks and creditors at the time, because these builders just could not pay their debts. The ACT government would not drop the requirement in their act because they also, I guess, were being lobbied by the insurance providers who had insurance.

We, I guess, went on our hands and knees to the ACT government and said, 'We need to set up an alternative scheme.' We called it the Master Builders Fidelity Fund. From the concept being developed on a whiteboard in our office to inception of the scheme in about mid-June 2002, this process probably took about 2½ months. You can imagine that, at the time, we were under severe pressure from our builder members saying, 'We're going broke.' Believe me, it was a major crisis, because in the ACT—I guess we are different from the other states—we are very close to our builder members, because of the geographic nature of Canberra. They can come and see us. I can remember the very first meeting we had on insurance. We had builders and we could not



actually fit them into our training room. Our training room typically takes about 150 people, so they were down the stairs and they were outside, saying, 'What are you guys going to do?'

It was at that time we approached the ACT government, and I must say that the ACT government, with the Department of Justice and Community Safety, their legal department, pulled out all the stops to get us to the position where we could issue insurance. Master builders itself had to kick in about \$400,000, and we also obtained some funds from some of the larger builders because we could not get the scheme approved unless there was some capital in the scheme, because, essentially, as soon as we started issuing certificates we were quite likely to receive claims from consumers and we had to have the capacity to pay. Of course, we also had to have actuarial sign-off.

We issued the first certificates and, as you can imagine, at that time there was an absolute hoard of builders stomping at our door to get that piece of paper so they could get exchange of their contracts and actually start work. The first day we started, we issued about 300 certificates to builders—that was on the first day. Since then, the scheme has gone from strength to strength. From our point of view, our greatest risk was that, if we had received claims in the early days, it could very well have collapsed and we would have lost our \$400,000. But we have managed our scheme well. It is totally different from an insurance company. We manage it with the consumers and the builders. It is a system that is essentially owned by the builders. Remember that this is an impost that has been placed on industry by the regulatory authorities, and it should be remembered that this was a concept that was never conceived by industry associations or builders. Essentially what we were trying to do was satisfy the regulatory requirements of the old Building Act. That is some background.

**CHAIR**—Thank you very much. That is useful. You mentioned there was one insurer still operating at the time when you set up. Are there other insurers still operating in the ACT apart from yourselves?

**Mr Howard**—Yes. There are about four now that operate in the ACT delivering the same warranty insurance as we do.

**CHAIR**—So they operate at the same time. Is there a separate licensing body in the ACT?

**Mr Howard**—Yes, there is. There is a builders licensing body—the same as in the other states. A builder has to be licensed before they are issued with home warranty insurance. You have companies and individuals. We have probably about 1,400 builders who operate in the ACT at varying levels of work.

**CHAIR**—Is the home warranty insurance that you provide purely a last resort, or do you have other elements in there as well?

**Mr Howard**—It is a last resort under our Building Act, but we do not actually operate it as last-resort insurance. We have had instances where builders have not gone broke or bankrupt or died and we have paid out the claim. Our objective is to help the builders. I do not believe there is any benefit in chasing a builder when he gets into financial difficulty because it is not only the consumers who get affected but also the subcontractors who get affected. Our objective is to help the builders. We provide free financial advice to the builders, and we get an idea if the

builder is in financial difficulty. We have a qualified assessor that assesses all the builders. We bring the builders in to meet with the assessor so they can do a financial management plan for them to get them out of their financial difficulties. Since we started the operation of the scheme, we have had one medium to large builder and one smaller builder go out of business. Some of the other insurers have actually had a few fold.

**CHAIR**—Can you give any kind of ballpark estimate of how many of your builders do run into trouble, in the sense that they need some extra assistance?

**Mr Howard**—I would say from time to time anywhere from five to 10 per cent of the builders do need good advice. I think it is critical to recognise in the early stages when builders are getting into financial difficulty. We pick up this intelligence probably better because we are close to it. The insurance companies—I am not being cynical here—do not care, quite frankly, because they are big insurance companies. But we do, because, if we have a claim of, say, \$300,000 or \$400,000, it severely affects our capital adequacy. We have to meet our capital adequacy requirements under the prudential standards every year, so it is in our interest to make sure that the builders are helped through the process if they have financial difficulty and to provide advice to them rather than letting them trade on and it manifest into a far greater problem. Typically, from my knowledge of the industry and builders, they are always of the view that they can trade out, that there will always be the next job that will get them through, but that is not the case. The problem is simply manifesting, and it can easily manifest over a period of six to 12 months, so we get the signals very early.

The other thing we do that the other insurers do not do is that we actually also do site audits and inspections. We do not rely on local authority inspections, so we inspect at the critical stages in the work. We then get reasonable intelligence from talking to the builder and subcontractors on site as to how the build is going. If we get any inkling that there are difficulties emerging, we talk to the builder. Then we can actually control the number of projects that the builder takes on as well. We do this in the very early stages. We look at their capacity. We just do not look at financial capacity; we look at their experience and their capacity to manage the projects. On that basis, we say, ‘You’re okay; you are capable of doing four projects at any one time to a value.’

We try, in a way, I guess, to hold some control over the builder as well. ‘Control’ is probably a bad word; it is probably for their own benefit in many instances. In times of large work—and I say this to our builders—the hardest thing for you to do would be to refuse work. They take on too much work. They overcapitalise, they overcommit themselves and then they get into trouble. In turn, the consumer gets into trouble and of course the suppliers get into trouble, so there is a chain reaction. It is just not the consumer; it is the chain reaction—small contractors go out of business. It is crucial at this end that we manage it well.

**CHAIR**—Do you ever reject builders completely?

**Mr Howard**—We do, yes. We have rejected probably about 35 builders since it started. We have had builders that have simply had a not so good reputation, and we just do not want to take on that risk. If the insurers want to take on that risk, they can.

**CHAIR**—I think you might have said this in your written submission, but who sets your prudential standards?

**Mr Howard**—The prudential standards are set by APRA standards, the same as the other insurers. They are actually prudential standards under our Building Act, and we have to provide an actuarial report every six months on our capital adequacy to be able to pay claims should they arise. We have claims provisions, and we have an audit report every 12 months. So we have an actuarial report every six months and an audit report every 12 months. That report has to be provided to ACT Treasury. If we refuse a claim, we have to advise our local fair trading authority as to why we refuse a claim, give reasons why. I must say, as yet we have not refused a claim.

**CHAIR**—Obviously the ACT is a reasonably small jurisdiction. Do you think your model could be translated to a larger jurisdiction?

**Mr Howard**—Absolutely. On a regional basis, it could work. It could work very well in Tasmania, because we did actually share our information with the Tasmanians at the time. They were looking closely at setting up a model very similar to ours—Master Builders Tasmania. I think the great benefit of this scheme is that you need to know the industry. You need to be close to the industry. It may not work that well in a large jurisdiction like Sydney, where you have builders essentially all over the state. It would be more difficult to control.

**Senator JOYCE**—Are you aware of ASIC policy 139? You are governed by APRA?

**Mr Howard**—We are not; we are governed by the provisions under the ACT Building Act 2004.

**Senator JOYCE**—Would you say that the Canberra market, as an indicator, is a fair sort of indicator of the way the building market would work in other areas—that is, 10 per cent of builders usually have problems and about 10 per cent of builders generally in other areas have problems? Is there anything peculiar about the Canberra market that would be completely different from the Sydney market?

**Mr Howard**—There is not. I would say that the Canberra builders are probably insulated a bit more because of the types of consumers. This relates back to affordability issues. There are better affordability issues in Canberra, probably, than in the other states. There is a lesser risk, I would say, of the Canberra builders actually going broke than there would be of, say, typical Sydney builders, or typical Brisbane builders.

**Senator JOYCE**—I know that the structure of your entity is different from an insurer's entity, but what sort of payout proportion do you have for premium received?

**Mr Howard**—Our actuary actually does that calculation. We have claims provisions every year. It is difficult to give a precise number, but the actuary works out the numbers based on the number of certificates issued and value of work insured. Again, our market is slightly different, because it is not a dominant contractual market, and the contractual market is the high-risk market. Just to explain the difference, that I said previously, a builder purchases a block of land and builds a house and on-sells it to a consumer. There is no financial risk during the building process for the consumer; they buy the product at the end. There is a risk on the statutory warranty if defects manifest in the work, whereas the contractual situation is very different. I guess this is the one area where we carefully monitor where the insurance companies do not, and I can give you an example.

**Senator JOYCE**—I understand what you are saying. If there is something flawed in the structure itself after he has on-sold the whole project to you then you can go back.

**Mr Howard**—Yes.

**Senator JOYCE**—Just as a rough figure, would someone say, ‘Of 100 per cent of the funds we collect, we probably end up paying out 50 per cent of them’—or 70 per cent of them, or 20 per cent of them? What would be a ballpark figure?

**Mr Howard**—I would not know precisely, because there is a provision made for six years. If you look back through our claims history, if you understand the actuarial provisions, they make provisions for these catastrophic claims that they say that are likely to emerge.

**Senator JOYCE**—Yes, I know that.

**Mr Howard**—Hopefully that will never happen.

**Senator JOYCE**—Hopefully you do not have that.

**Mr Howard**—Say, for example, if we said 20 per cent?

**Senator JOYCE**—Okay. I am just trying to get a really rough calculation. So it is roughly about 20 per cent?

**Mr Howard**—Yes.

**Senator JOYCE**—Are you aware of the warranty scheme that is in place in New South Wales? It appears that they do not really pay out on anything, but what is the difference between what they are supposed to do and what you pay out on? Is there any extension in what you do that is greater than what they do? Could you look at it *prima facie* and say, ‘They don’t pay out on this, and we generally do.’

**Mr Howard**—I think they have a much more complicated system. We purely cover residential building works. They cover outbuildings, garages, swimming pools—it is a far more complex mix than ours. I believe that there should never be a requirement for what we call external structures. I think it is so important to protect homeowners if a builder fails to complete, so they can actually move into their house and get it finished. Who cares if the swimming pool is not completed? I believe they are luxury items. If somebody wants to spend \$40,000 on a swimming pool, I believe that they should do their due diligence and make sure they get a proper pool builder in the process.

**Senator JOYCE**—Okay. What seems to be the evidence we are getting is that they do not pay out—obviously; that is why the inquiry is being held. They might discuss in a vague way a whole range of areas, but actually getting the money out of them is something completely different. How do you actually cover the people, or engage in the marketplace, in terms of insurance or some sort of protection? If I buy a house in Canberra that has been built by a builder and I am the first person to live in it, how do I know that you exist and how do I know what your relationship is with me? How do I find out about that?

**Mr Howard**—The owner, the builder and the local authority get a copy of our certificate.

**Senator JOYCE**—So I get a piece of paper?

**Mr Howard**—You get a certificate of insurance with all the cover on the front and the conditions on the reverse side.

**Senator JOYCE**—And it says, ‘If these things happen, this is who you call’?

**Mr Howard**—Yes.

**Senator JOYCE**—Do you find that that is the point of call and how people find out?

**Mr Howard**—It is.

**Senator JOYCE**—So they say, ‘Hang on, the walk-in wardrobe just walked out, so now I’m going to give you a bell’?

**Mr Howard**—Yes. That is precisely what happens. In the first instance, they will ring, and then we send them a claim form, and we have 90 days to process their claim.

**Senator JOYCE**—You send them out a claim form, and then I imagine they fill it out and you send out an assessor, and the assessor has a look around?

**Mr Howard**—Yes.

**Senator JOYCE**—How do you make sure that the assessor and yourselves put up that professional isolation from the builder so that I am not going down to the pub and having a beer with you that night and saying, ‘Come on, Jerry, mate, fair go; go easy on me’?

**Mr Howard**—They have the option to engage an independent assessor. It is just that we have the expertise in house that does our audit, on a full-time basis, of the builders. The owner puts the claim in; then we do an assessment and say, ‘Yes, this is fair and reasonable.’

**Senator JOYCE**—What are the golden rules of your scheme that you say keeps the public with a sense of confidence in what you do? Are you transparent, independent, expedient, have a dispute resolution process that is independent of you so that if I do not have to turn up and say, ‘Jerry, I think you’re too good a mate with Bob the builder and that is why you are not paying any out’? What do you think are the golden rules of your scheme?

**Mr Howard**—One of the things that we do that is very unique is that when the builder applies for insurance, he has to provide a copy of his contract, so we do an assessment of the contract in the first instance to make sure that what is on that contract is what is being delivered to the owner. I guess we also check to make sure that the builder has actually priced the job correctly. The last thing we want is the builder underpricing the job. That gets us into strife because we are likely to have a claim, and then it gets the owner into strife because they do not get the work completed. That is the one thing that we do that the other insurers just do not do. Clearly the owner also signs the application for insurance, so they know that it is being issued. The other

thing we do is we have clear warnings in our contract for the consumer, just to make sure that they do not actually pay an excessive deposit to the builder—so it says, ‘This is the level of cover we provide if you lose your deposit.’ We run contractual seminars for the consumers as well. That advice is put out at the very beginning.

**Senator JOYCE**—What is your turnaround in dispute resolution? I might turn up and say, ‘I have a bona fide claim; the wall in the lounge room has just fallen over and it shouldn’t have.’ You turn up and your assessor goes out there and says, ‘It’s lucky it didn’t kill somebody.’ How long before some money turns up in my bank account to fix it up?

**Mr Howard**—We will actually organise also the contractors to complete the work. There is an option. We would organise the contractors to do the work or in some instances we would just pay the claim to the people and they have gone on with the work themselves, because in some instances they feel that they can actually do it quicker themselves. So we give them that option. What we say is we will have all claims resolved within 90 days.

**Senator JOYCE**—Claims resolved within 90 days. I imagine there will always be contentious claims; it is just the nature of the world that some people disagree. How often does it end up in a legal battle where someone says, ‘I don’t think so, so I’m going off to court’?

**Mr Howard**—We have not had that. I guess this is again probably—

**Senator JOYCE**—You have not had one person saying, ‘I’m going to take it to court’?

**Mr Howard**—No. I think this again is probably due to the fact that we manage the contractual process up-front, so—

**Senator JOYCE**—You know your rights before you start.

**Mr Howard**—Exactly. The contract is clear on what is included and what is not included in the contract because, in many instances, builders are not the best at completing paperwork.

**Senator JOYCE**—You are telling me.

**Mr Howard**—We get an example whereby we get a price and we look at it for insurance purposes and we say, ‘This is way under.’ Then you get the builder in and he says, ‘But that does not include a kitchen because the owner is doing the kitchen. He is a cabinet maker and he is doing his own painting.’ All of a sudden, there is a \$30,000 difference in the contract. If we take on that risk, there is a \$30,000 extra risk there for us. We are very clear, and in our certificate of insurance we will say, ‘Works not included in this insurance certificate: kitchen by owner; painting by owner’.

**Senator JOYCE**—So it is not just the transparency of how you do the process, but it is also the transparency and full and frank declaration at the start of the process about whose responsibility is what and what is going on.

**Mr Howard**—Yes. I guess again, geographically, you get to know very quickly in Canberra if a builder is doing poor work. We get our intelligence very quickly.

**Senator JOYCE**—I live with a builder in Canberra. I should declare my interest. It is not in a conjugal form! We are actually in the same house.

**Mr Howard**—I think the builders have a sense of ownership over what we did for them too, because we set this up to get the builders out of a hole. If they see a builder who is doing something dodgy, I can assure you I will probably hear about it within a week, and we will have somebody out there to say, ‘Fix this up or next time you won’t get insurance.’

**Senator JOYCE**—You bankrolled that whole thing at the start with \$400,000?

**Mr Howard**—Yes.

**Senator JOYCE**—That is not much money at all.

**Mr Howard**—We did, and it was a major risk for us at the time because we issued those 300 certificates and we could have had a claim within a—

**Senator JOYCE**—Yes, you could have had two claims and it is gone.

**Mr Howard**—Exactly. It could have wiped us out. This was something we had to negotiate with the ACT government, because they said, ‘You’ll need \$1 million in capital to start this.’ We had some of our larger builders actually kick in funds as well. We had actually accredited them for certificates in advance, some of the larger builders. I think we had to have about \$650,000 in net tangible assets before we could issue the first certificate.

**Senator JOYCE**—Please do not answer this question, because I am really doing very simple sums. I am working on about 320,000 or 350,000 people in Canberra; what sorts of funds do you comfortably sit on now, and do you think that sort of covers the whole scope of things?

**Mr Howard**—Our actuary is advising us that, because we carry a statutory warranty, we should reach a capital level of \$5 million.

**Senator JOYCE**—So, \$5 million for 350,000?

**Mr Howard**—Yes.

**Senator JOYCE**—Roughly speaking, we have about four million here, so it is 12 times in Sydney, about \$60 million or something in funds in one in Sydney to do about the same job?

**Mr Howard**—Yes.

**Senator EGGLESTON**—How many builders do you actually have on your books?

**Mr Howard**—I would say we have about 1,400 builders, but not a lot of them do a lot of work. In some instances, because they are also subcontractors, they might build one house and then go subcontracting for two years and then they will come back again. Typically I would say that, of that group of builders, probably 20 to 30 per cent do the majority of the work. We do not have large volume builders in Canberra like they do have in Sydney. Our largest builder in

Canberra would probably build about 80 to 100 houses—that would be a larger builder in Canberra. The majority of the rest are made up of builders that build I would say anywhere from two to five houses a year.

**Senator EGGLESTON**—It seems quite a lot for a small city like Canberra, to be quite honest.

**Mr Howard**—We have had a building boom in the past couple of years in Canberra. We build probably about 2,500 to 3,000 residential units a year, and not a lot of those require warranty insurance because warranty insurance is not required for multistorey above three storeys, which is the same as New South Wales.

**Senator EGGLESTON**—How many of these builders do you insure?

**Mr Howard**—I would say, from my last reckoning, we probably have about 65 per cent of the market. When we started we probably had about 80 per cent. We are probably about 65 per cent now.

**Senator EGGLESTON**—Why has it dropped to that?

**Mr Howard**—It has dropped because some of our builders did not meet our access to the fund requirements and they went to other insurers.

**Senator EGGLESTON**—What sort of other insurers are they going to?

**Mr Howard**—It could be any of those HIA insurance services that are run; there are a couple of others as well. As I said previously, we have had a loyalty from our builders because of what we did. They are willing to stick with us rather than go across, even though there have been some attractive premium propositions put to them from time to time.

**Senator EGGLESTON**—That is another area to get into, because the insurance industry I understand believes that returning to first resort cover would require premiums to increase.

**Mr Howard**—I do not think so.

**Senator EGGLESTON**—You do not agree with that at all?

**Mr Howard**—I do not agree with that from the ACT's perspective because, quite frankly, I could not care because our attitude is that the builders that are on our system, we will make sure they do the work properly, and if a claim or a dispute does arise we can actually deal with it.

**Senator EGGLESTON**—It seems to be quite a good model, I must say. I am surprised it has not been taken up elsewhere around the country.

**Mr Howard**—I think it probably would have, but you have got the interests of the large insurers that put a lot of pressure on governments by saying, 'We are delivering a great service, so why should you let smaller providers into the market?' That is just my opinion.



**Senator EGGLESTON**—That is an interesting view. We are growing to the point of view that the larger insurers are not really providing a particularly satisfactory service to consumers, so alternative models need to be looked at.

**Mr Howard**—With respect, the regulatory authorities gave way to the insurers. We should not blame the insurers totally for this. The regulatory authorities caved in.

**Senator EGGLESTON**—Through the exemption clauses?

**Mr Howard**—Yes. As I said, we can very easily blame the insurers, but the insurers did a deal and the regulatory authorities agreed, and they harmonised insurance across the states, and they have brought in this ‘last resort’ and consumers have obviously been affected by it. I guess there are two issues here: the role of the regulatory authorities in licensing and in monitoring the builders. I think that, again, we do this well with our local regulatory authority because I can pick up the phone and talk to our construction occupations registrar or he will ring me and say, ‘Look, we’ve got problems with this,’ and we will sort it out together.

**Senator EGGLESTON**—I suppose that is a function of a smaller jurisdiction. Licensing is another area that has also been drawn to our attention as an area where there are some problems, in that people are not being reviewed and their licence seems to be for an indefinite period without any kind of checking, in many cases, of their ongoing capability to maintain their operations as builders.

**Mr Howard**—Yes, and their financial capacity. That is a yearly check for us as well. We do not want to be a regulatory authority, but I think we work well with the regulatory authority to deliver the best outcome. I think licensing should not be purely about qualification; it is about business, and we do provide business training for our builders. What we are planning to do as surpluses emerge in our scheme, and we have approval from the minister for this, is that those surpluses will be used to provide training for consumers and builders in the industry. So if our actuary tells us tomorrow that we have met our capital requirements, then all surpluses will not go back to an insurance company but back into the industry for training. That is something else that we are going to do.

**Senator EGGLESTON**—That is a very positive approach, I must say. Are there any other general comments you would like to make about your scheme in relation to other schemes around the country?

**Mr Howard**—There has been a lot of negative comment about insurance companies and probably rightfully so. But, as I said, in some instances they are not totally to blame. Warranty insurance is something that has been imposed on the industry by the regulatory authorities. It started probably in about 1989 and there were some voluntary schemes, but then we had builders going broke and some horror stories of works not being completed. Then the Building Services Authority set up their own scheme here and they did not pay out lots of claims, I understand, at that time, and created some massive surpluses. Then we had the privatised scheme to go across the country, and Queensland is now probably the only state that has a government backed scheme. Then we had the collapse of HIH, and then the whole industry changed again.

It has now settled back down again to where the insurance companies, because of the lower risks, I guess, that they have with the last resort insurance, are making hay while the sun shines; hence, this inquiry into how valid or not valid this type of insurance is. It has to again be clearly understood that this is being imposed by the regulatory authorities to protect consumers. If you drop it tomorrow, that is fine; then consumers will have to be far more diligent in their selection of builder, and consumers typically build one house in their lifetime. I believe the critical area they need protection from—and this is my view—is when the builder actually goes broke, disappears or dies because they do not have any control over those three elements, whereas in the selection of a builder for quality building work they do and in the selection of the price to do the job they do. But some of those other areas are outside their control.

**Senator EGGLESTON**—I suppose the criticism with the insolvency, disappearance or dying approach, which you have just said consumers do not have any control over and need protection against, is that there are other issues which the consumers need to be protected from, such as faulty workmanship and all these sorts of things—

**Mr Howard**—Yes.

**Senator EGGLESTON**—and they are not getting that kind of protection. Would you envisage some different sort of approach which encompassed your three basic points plus?

**Mr Howard**—That is very much a regulatory authority issue. Again, there is just not one magic bullet for this. The councils are just pulling out of doing inspections because of liability issues. We have private building certification because authorities have moved away from the liability of inspecting building work. Local authorities do not want to take responsibility; they want to shift it back to industry. The quality of workmanship is something that New South Wales have actually been trying to address and they have had several inquiries into the quality of building work in New South Wales. They license just about everything that moves, but regulation in itself does not fix quality of work issues.

We in the ACT do not have an overburdened regulatory system. What we do have is a pretty good system of managing the building certification process from inception to completion of the building work. The other thing we do, which I neglected to mention, is that we ensure that the actual project is completed and a certificate of occupancy is issued. The insurers do not care about that. In the ACT, they do not follow up that certificates have been issued, whereas we get generate reports constantly to make sure that the owners have their certificate of occupancy because if they come to sell that house and they do not have a certificate of occupancy they cannot sell in the ACT. They are things that we do that the consumers probably do not even know we do, quite frankly, but it is all about not just doing one thing; there are lots of factors in this quality of work issue. Certainly I believe it starts with ensuring that the builder has priced the job correctly in the first instance. That is why we ask for the key parts of the contract to ensure that the builder has actually priced it. We have a typical unit rate for work, and if we know the type of project we know what it is going to cost. There is no point in our knowing and issuing a certificate that has a builder entering into a contract with you but we know he will not be able to complete that work. It will disrupt your life and it will disrupt others. What we have tried to do is stop the builder at that point. The builder, of course, has the right to go off to other insurers and get insurance, but at least we feel that we are doing the right thing at that point.

**Senator EGGLESTON**—You mentioned other groups have been concerned about liability insurance. Could we say that was a by-product of the limitations of the home warranty scheme?

**Mr Howard**—Yes.

**Senator EGGLESTON**—Could the committee draw that conclusion?

**Mr Howard**—Yes.

**Senator MILNE**—I am very interested in this issue of the risk and financial assessment before admission to the fund being carried out by an independent auditor, and I am interested in the fact that you said you started out with about 85 per cent of the builders and that has gone down to 65 per cent. Presumably that 20 per cent has gone off and got admission to another insurance product, so we can conclude from that that the assessment of the insurance companies, compared with your assessment, is considerably less rigorous.

**Mr Howard**—I would agree, absolutely. We know from building starts that builders whom we have refused get insurance from others. I think it started off in 2002 very diligently, requiring bank guarantees from very small business operators that were quite happy to work on small margins but would never go broke. We have builders like that; they are quite happy to make five per cent, and they will never go broke. But they would not meet the eligibility requirements back then for insurance. Yet they would pass through with flying colours under our system because we look at their capacity to do the work and their margin. You are right in what you say, that the insurance market, for want of a better term, has loosened up a lot. This is my take on it: they are purely interested in volume.

**Senator MILNE**—To address this issue, it seems to me that the critical component here is the independent audit assessment of the risk and the financial viability before you are able to get access to a fund or insurance or whatever, to make sure that at least the fundamentals are in place.

**Mr Howard**—Yes. You mention two elements. One is financial, but I think there is another critical one that we do, and that is the builder's history in the industry and his history of doing quality work. You can have a builder who can actually get through in flying colours on the financials, but he might not meet our standard of work criteria as well.

**Senator MILNE**—Sure. I think that is an important thing for us to consider, in terms of verifying that before we start. In terms of the bank guarantees, do you ask for bank guarantees?

**Mr Howard**—No. Initially we did ask for directors' guarantees. I believe that if you have to ask for bank guarantees, firstly, they should not get through in the first instance. Why try to prop them up with a bank guarantee? That is just going to help us; it will not help the consumer. If a builder has a bank guarantee and the builder goes broke and he cannot finish the consumer's house, it is of no benefit to the consumer if he has a bank guarantee. That is only a benefit to the people providing the insurance. They can probably seek recovery to finish the work. I guess I had an issue with bank guarantees because we had lots of our builders through previous insurance schemes that still have bank guarantees that are not being paid back. This is despite the fact that the statutory warranty period is long past. I just had a personal issue with this whole

issue of bank guarantees. What we can do, and what the insurance companies cannot do, is limit them to a number of projects.

**Senator MILNE**—I understand that. I just want to follow up on what you just said, that you know of people who have given a bank guarantee and it has been refused to be paid back to them.

**Mr Howard**—Yes. With one our members, probably about two weeks back I just happened to ask him: ‘Have you still to get that bank guarantee back?’ He had had to put up a bank guarantee for \$25,000 back in 2002.

**Senator MILNE**—This was with an insurance company?

**Mr Howard**—Yes. The statutory warranty has long since expired and he is still struggling to get his bank guarantee back.

**Senator MILNE**—Can you say which insurance company?

**Mr Howard**—I cannot, no. But I know which one it is.

**Senator MILNE**—You are under parliamentary privilege here; you can say—

**Mr Howard**—I do not want to.

**Senator MILNE**—If you do not want to, that is fine. I am just saying you can without—

**Mr Howard**—Why I am so close to this one is that he was one of our younger builders at the time and we had provided him with insurance. He wanted to do a project in New South Wales and we did not offer insurance in New South Wales. He had to put up a bank guarantee. That put some severe financial stress on him at the time. Since then he has moved on, but he is still saying he has not got that back, and he makes quite regular contact with them, even though the warranty period is long expired.

**Senator MILNE**—The criticism from a lot of the builders is essentially they are being required to insure themselves by virtue of these bank guarantees and that it is grossly unfair.

**Mr Howard**—I agree.

**Senator MILNE**—Do you want to comment on that?

**Mr Howard**—I agree. If you look at the definition of insurance, surely it is about taking risk. You take a premium from a builder, you are taking that risk. You should not have to ask the builder to actually sell his soul to get the insurance. We would never, never go after the personal assets of a builder if a builder got into trouble because we believe that that is just not on. We take the risk.

**Senator MILNE**—If I can go to the question that Senator Hurley asked in the first place, in terms of the latent defects and so on that you cover, which makes you not a last resort because

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you cover the defects, does that cover the defects without the person dying, disappearing or becoming insolvent?

**Mr Howard**—Yes. We have paid claims out even though we do not have to under our Building Act. Our Building Act clearly states, as do other building acts, that we do not have to pay a claim until the builder has disappeared or died.

**Senator MILNE**—That is what I was just trying to get at. So under the ACT scheme you would cover defects but, legally, only in the case that the builder has died, disappeared or become insolvent. In fact, you do pay the defects out even while the builder is not insolvent, but that is your choice, that is not your legal requirement?

**Mr Howard**—That is our choice, yes.

**Senator MILNE**—That is important. Do you have a limit to the claim that you would pay out? How does that work?

**Mr Howard**—Yes, \$85,000 under our Building Act. It is \$85,000 in the ACT.

**Senator MILNE**—You would pay that out on defects even if the person was not insolvent or dead or disappeared or whatever?

**Mr Howard**—Exactly, yes. I could not see much point, quite frankly, in chasing a builder that we quite clearly knew did not have the financial capacity to actually finish the work. There was little point in us forcing that builder into bankruptcy, because it is not going to help the builder. We have had builders that have, through no fault of their own, got into financial difficulty, but they make us aware of it and we will actually help them through.

**Senator MILNE**—Senator Eggleston asked you about the issue of premiums, and I just want to be clear about what you said. How do your premiums compare with the last resort insurance? You offer a better product in terms of what the consumer can get, but I would like to know how much more expensive the premiums are or whether they are more expensive.

**Mr Howard**—They are more expensive.

**Senator MILNE**—Relative terms?

**Mr Howard**—We have different scales, but I would say—I could have got this precisely for you—

**CHAIR**—You can probably provide it to us later.

**Senator MILNE**—Perhaps you could provide it to the committee, because it would be very interesting for us to see in relative terms.

**Mr Howard**—Yes. I would say that when we started in 2002 we tried to match our premium rates to our competitors, but since that time we have not actually raised our premiums, but the

others certainly have dropped their premium rates. In a typical house with, say, a new home, ours probably would be about \$300 to \$400 more expensive. That is just on that element.

**CHAIR**—Presumably if the consumer is aware of the extra protection they might prefer to have that, but you still deal through the builder and the consumer does not really have any say?

**Mr Howard**—But we are certainly under severe pressure from the insurance providers because we know that they are trying to canvass our members. This is an issue I have raised with our actuary, because our actuary also sets the premium rates for us. We do not have a lot of control over that. We cannot allow insurance companies to say, ‘Okay, we will drop our rates and we will just get all this revenue in.’ We cannot do that. We have to be very careful because of our small pool and our capital requirements. The actuary actually sets the premium rates, and the actuary also has an actuarial review that approves those premium rates. We cannot drop our premium rates without the approval of the actuary.

**Senator MILNE**—That is reassuring to me, I have to say. In terms of the scale, you said that one of the advantages of your scheme is that it is a relatively small area. The businesses are known to you, the builders are known to you and so you can make judgements accordingly. Therefore it is not replicable to Sydney or Melbourne, but it would be replicable on a regional scale?

**Mr Howard**—Yes.

**Senator MILNE**—If there were half a dozen regions that got together, implementing at a regional level but with one pool, then you could probably operate more cost effectively, is that right?

**Mr Howard**—Yes, and we actually did try this. We spoke to the New South Wales government people and said that we would actually offer our fidelity fund outside to regional areas like Yass and Goulburn. Unfortunately we did not succeed in getting that up. We did write to the New South Wales minister at the time; I believe it might have been John Della Bosca at the time.

**Senator MILNE**—Basically it was a political decision not to allow that to happen.

**Mr Howard**—Yes.

**Senator MILNE**—I am just seeing if technically it was possible?

**Mr Howard**—Absolutely. It would have worked perfectly in Tasmania and probably in South Australia—South Australia was also interested in our model. But since that time, I guess the whole insurance market—and again, this is probably due to the environment they are in now, why it is a last resort—has been able to offer insurance, and there is no need for somebody like us to actually do anything else.

**CHAIR**—Thank you very much, Mr Howard, for appearing today.

**Mr Howard**—Yes, thank you very much.

[12.33 pm]

**LIM, Mr Michael, Manager, Investor Protection Unit, CFSD/Markets Group, Department of the Treasury**

**WALKER, Ms Caroline Rosemary, Senior Adviser, Insurance Access and Pricing Unit, Department of the Treasury**

**WILKINSON, Ms Vicki, Manager, Insurance Access and Pricing Unit, Department of the Treasury**

**CHAIR**—Good afternoon, and thank you for coming in. Ms Wilkinson, I believe that you have an opening statement.

**Ms Wilkinson**—Yes, I do, thank you. Treasury would like to make the following opening statement. Treasury acknowledges that home builders warranty insurance has been a contentious issue for many years and notes that numerous reviews and reports have been undertaken. Treasury's role in the existing regime, however, is limited, given that states and territories regulate the building industry and determine whether and in what form to mandate home builders warranty insurance.

As the committee is aware, there are different approaches in different jurisdictions. For example, Queensland mandates first resort home builders warranty insurance provided by a government agency. New South Wales and Victoria mandate last resort home builders warranty insurance provided by private insurers in a competitive environment. Tasmania, in contrast, has recently decided to no longer mandate home builders warranty insurance and to allow the market to determine whether first resort insurance, last resort insurance, some other type of insurance product or no insurance is provided.

Treasury has been specifically asked by the committee to comment on Corporations Regulation 7.1.12 (2). By way of background, section 761G(5) of the Corporations Act requires providers of certain home building insurance products to certain clients to meet the requirements of the disclosure regime set out in that act. Regulation 7.1.12 of Corporations Regulations 2001 defines for the purposes of section 761G(5)(b)(ii) what forms of home building insurance products should be included in the disclosure regime provided by the act. The regulation excludes from the disclosure regime insurance entered into for the purposes of a law, including a law of a state or territory, that relates to building or construction work in relation to a home building. Therefore, mandated home builders warranty insurance is excluded from the Corporations Act disclosure regime.

However, providers of mandated home builders warranty insurance are still required to meet other relevant requirements of the Corporations Act, such as the licensing requirements. This exclusion is consistent with the treatment of other state mandated insurance products such as workers compensation and compulsory third party motor vehicle insurance. The reason for these exclusions is that, if a state or territory law mandates a certain type of insurance, in the Commonwealth's view, the state or territory law should also be responsible for outlining what

disclosure and/or other consumer protection measures need to accompany the insurance. If the Commonwealth also regulates in this space, there is a risk of duplication and/or inconsistency between Commonwealth and state/territory based regulation which may well increase the overall regulatory burden and result in increased insurance costs.

To summarise, as a result of the corporations regulations, providers of home builders warranty insurance do not have to meet the disclosure requirements of the Corporations Act if they operate in states and territories where home builders' warranty insurance is mandated. However, this does not mean that home builders warranty insurance providers are unregulated, as the private or commercial insurance providers have to comply with the remaining requirements of the Corporations Act, other Commonwealth legislation including, most importantly, the prudential regulation contained in the insurance act, and obviously any relevant state and territory legislation. If a state or territory does not mandate home builders warranty insurance, such as Tasmania is proposing—and I think that legislation is before the Tasmanian parliament at the moment—

**CHAIR**—It has passed.

**Ms Wilkinson**—It has passed. If they no longer mandate insurance, then the corporations regulations relating to mandated insurance do not apply, and providers of home builders warranty insurance will have to comply with the full disclosure regime under the Corporations Act if the other relevant conditions are satisfied. These other conditions include that the purchaser of the insurance is an individual or the insurance is being purchased for use by a small business. The rationale for this is that if there is no state or territory legislation requiring the insurance, then there is no alternative legislative framework that the insurance provider must comply with. As a result, there is no justification for excluding the providers from the disclosure regime contained in the Corporations Act.

However, it should be noted that, even where the disclosure regime under the Corporations Act applies, disclosure occurs to the purchaser of the insurance policy—that is, the builder. Treasury agrees there is merit in considering options for improving the awareness of consumer, the person having the house built, around issues associated with home builders warranty insurance and other aspects of the building industry, but we consider that the Corporations Act may not be the appropriate vehicle for achieving this.

We note that the Consumer Action Law Centre's submission suggests that, because of the corporations regulation, there is no comprehensive reporting of the premiums earned and number and value of claims being made in relation to home builders warranty insurance by the Australian Prudential Regulatory Authority. The corporations regulations, however, are not relevant to any data collection, so we just wanted to correct that.

The relevant Commonwealth legislation which empowers APRA to collect premiums and claims data is the Financial Sector (Collection of Data) Act 2001. Following a request from the Australian government in 2003, APRA established the National Claims and Policies Database in consultation with the insurance industry and other stakeholders. The objective of the NCPD is to provide insurers, the community and government with a better understanding of professional indemnity and public liability insurance. However, following consultation with stakeholders, home builders warranty insurance was excluded from the National Claims and Policies Database



as it has a different policy period, premium earning pattern and cause of loss to normal liability business, and therefore a separate data collection would be required. Obviously, a separate data collection would potentially impose additional financial and reporting burdens on the insurance industry, and really the benefits of that need to be assessed against the costs.

With respect to the other specific matters the committee has been asked to report on, Treasury notes that the final report of the Productivity Commission's *Review of Australia's consumer policy framework* was released on 8 May 2008. We note that recommendation 5.5 addresses home builders warranty insurance. The Council of Australian Governments has set a deadline of October 2008 for developing enhanced national processes to improve the consumer policy framework, including legislative and regulatory structures, drawing on the commission's final report.

In relation to comments made by the Productivity Commission in relation to home builders warranty insurance, we agree that it would be useful to look at the means of improving consumer awareness of what home builders warranty insurance does and does not cover and at the case for rebadging the product to more accurately represent its coverage to consumers—that is, the people purchasing the houses. As previously noted, however, Commonwealth legislation may not be the most appropriate way to do this. Treasury also agrees with the Productivity Commission's comment that the form and scope of home builders warranty insurance needs to be considered in conjunction with other aspects of the building industry, including licensing requirements and dispute resolution mechanisms.

Finally, while agreeing that there is merit in the committee considering potential reforms that may lead to appropriate consumer and builder protection and to improved housing affordability, Treasury notes that the cost of home builders warranty insurance is only a small proportion of the total cost of housing and that any reforms are unlikely to significantly impact on overall housing affordability. Thank you. We are happy to respond to any questions you might have.

**CHAIR**—Thank you. Going back to when you were talking about the Tasmanian situation and saying that, even where the disclosure regime under the Corporations Act applies, disclosure will be to the purchaser of the insurance, namely the builder, and it most certainly is the case that the builder takes out the insurance on behalf of their client, is there any particular reason why the consumer themselves could not decide who they insure with and what level of insurance they take out?

**Ms Wilkinson**—No, there is no reason why that could not be the case. The only reason is the state regimes and the mandated requirements for insurance. So there is no reason, and I guess in a sense there is no reason why, if that sort of insurance was a profitable line of business and consumers had a demand for it, insurers could not already be offering that in addition to what is mandated at the state level. So there is no technical impediment to that other than whatever might be in the state legislation.

**CHAIR**—And in that case, the disclosure regime of the Corporations Act would apply?

**Ms Wilkinson**—Yes, potentially—if the nature of the product that the consumer was buying fell within the definition in the Corporations Law as it currently stands. The starting point for the Corporations Law, in terms of disclosure, is to divide products that are being offered to

wholesale clients and those that are offered to retail clients, and then it defines who a retail client is. For a general insurance product, that definition is based on the nature of the product. There are specific products defined in the Corporation Act. One of the products is home-building insurance, and, in some circumstances, depending on the way that the policy was worded, that policy that you are speculating about could well fall under that definition and be considered to be therefore being offered to a retail client, and all those disclosures in the Corps Law would flow. We have had a brief look at the Tasmanian product that was previously mandated. Where a product is designed to cover both construction and occupation, technically our advice is that it falls within the retail definition. If a product was designed purely for the construction phase, it would not fall under the retail definition as it currently stands. There are some technical issues around that.

**CHAIR**—If the state mandated that the consumer rather than the builder took out the insurance, would the same circumstances still apply?

**Ms Wilkinson**—The current Corporations Act says that, where the insurance is mandated by the law of a state, the purchaser of that insurance is not considered to be retail under the Corps Act. So as things currently stand it would be considered to be a wholesale product and those disclosures would not flow.

**CHAIR**—So then it would be incumbent on the state government to make the necessary disclosure regime around that.

**Ms Wilkinson**—Yes, that is right. They could certainly do that.

**Senator JOYCE**—For the benefit of the audience, when you talk about Treasury, you mean the federal Treasury.

**Ms Wilkinson**—Yes.

**Senator JOYCE**—At this point in time, through your analysis and summary, there is not a Commonwealth oversight on this issue—there could possibly be, but there is not at this point in time?

**Ms Wilkinson**—It depends on how you describe the issue. The Commonwealth does not regulate the building sector. That is our starting point. The Corporations Act and the financial regulation mean that we regulate financial products in some circumstances. Home builders warranty insurance mandated by states and territories is outside Commonwealth disclosure, but not prudential. We prudentially regulate the private insurers that might offer it.

**Senator JOYCE**—So you prudentially regulate it, but the disclosure is outside the Commonwealth?

**Ms Wilkinson**—Yes.

**Senator JOYCE**—In precis, if the evidence that has been presented is correct—and I strongly believe it is—the current scheme is more than ineffective; in ways, it is deceptive, and it has no capacity whatsoever to deal with the concerns that have been brought forward at this committee.

If that means that the Commonwealth have to increase their role, or at least threaten to increase their role until the state government pull up their socks, is there any possible amendment to federal legislation that would bring this home warranty scheme under our jurisdiction?

**Ms Wilkinson**—Obviously I cannot comment on your lead-in to this topic. I have read a few of the submissions, but I am making no judgement about the merits of anyone's case, obviously. In terms of the Commonwealth's role, to the extent that the Commonwealth regulates the provision of financial products and services, the Commonwealth regulates the provision by the provider of the insurance to the purchaser of the insurance. The Commonwealth do not mandate that anyone takes out insurance and would not have the constitutional power to mandate that consumers started to take it out.

**Senator JOYCE**—I can understand that.

**Ms Wilkinson**—To the extent that someone else—that is, a state—mandated that different parties took out insurance, I suppose the Commonwealth can look at who the provider of the insurance is and who the recipient of the insurance is. And if we were going to do anything, we could probably do more in terms of who is buying the insurance. However, as we have said and as is clear to you, I am sure, where the states already have a regulatory regime in place, the Commonwealth does not step into the territory for fear of overregulation and increasing costs. You would have to assess those sorts of things.

**Senator JOYCE**—Okay. The issue is not so much about overregulation as about a complete avoidance of regulation. Under CLERP, there is a duty of disclosure, is there not? If I sell insurance I have to give a customer an information brochure. I have to say, 'This is what I am selling you; this is the product. Have a read of that.' Once they are happy with that, there is a contractual relationship between the purchaser of the insurance and the seller of the insurance. We have heard evidence today that people are definitely paying for the insurance, but there has been no transparency in simple English terms of exactly what they are purchasing. There has been no proper disclosure of the product that they are purchasing.

**Ms Wilkinson**—When you say there is no proper disclosure to the purchaser, are you referring to the builder or to the home owner?

**Senator JOYCE**—The home owner.

**Ms Wilkinson**—The way that the Commonwealth regulation of financial products works in general is that all the disclosures built into the Corporations Act are disclosures between the provider of the product and the intermediary—like a financial planner or an insurance broker and the purchaser of the product—

**Senator JOYCE**—Which in this case will be the builder.

**Ms Wilkinson**—It will be the builder. In the same way that if a lawyer buys professional indemnity insurance, the customer of the lawyer does not get disclosure other than if they ask the lawyer or there is some requirement at state level for the lawyer to reveal. It is not dissimilar to any of the public liability and professional indemnity insurance products. It is between the

insurance provider and the professional—or the builder in this case—that the disclosures occur. It is not to the third-party beneficiary.

**Senator JOYCE**—If there was a move to say that since ultimately the whole purpose of this product is to protect not so much the builder but the person for whom the builder is building the house, therefore they should have some right of transparency—of knowing exactly what they are doing—and know how to prosecute a claim should they have one, would there be a capacity for us to put that requirement into federal legislation?

**Ms Wilkinson**—At the federal level, we could not force the builder—that is, the purchaser—to disclose onwards because we do not have constitutional jurisdiction over builders, unless they were corporations, when we might look at a constitutional power. All we could do, I suppose, is to mandate that the insurance provider somehow disclosed to the end consumer—the home builder. I think there would be practical difficulties there, because the insurer who is selling the product to the builder but then trying to disclose to all the different beneficiaries might have no knowledge of their existence. So, again, from our perspective, if you want that flow from the builder to the home owner, it is probably better mandated at state level because the state has the power, through the whole building regime, to force that on-flow.

**Senator JOYCE**—Do you see the point I am getting to?

**Ms Wilkinson**—I can.

**Senator JOYCE**—Obviously a lot of people have some very serious and genuine concerns. They see federal senators turn up and they say, ‘You beauty, there’ll be a resolution to the problem.’ Obviously there is, by reason of this, political pressure we can put on players and we can certainly kick up a stink and try to drag people in here. And if they do not want to turn up, I suppose we could subpoena them. But, really, the aspect of the law that we can change to bring about a resolution at a federal level is not there.

**Ms Wilkinson**—Yes; it is very, very limited.

**Mr Lim**—I look after that part of the Corporations Act. The problem there is with the powers we have under that act. That act is an agreement between the Commonwealth and the states, and it is limited to financial services providers. If the relationship was between the insurance company and the home owner we would not have a problem stepping in under that legislation. If, however, the problem lies between the home builder and the consumer we cannot, because we do not have the power to enforce regulations on home builders.

**Senator JOYCE**—I was talking to some good ladies at the door a second ago and they said, ‘Well, fix it so that you do have the power.’ To fix it so that we do have the power, you would have to go to COAG and get the states to cede those powers across to the Commonwealth, and then the Commonwealth would have to accept those powers, and you would have to go from there. You would need the New South Wales state government to say, ‘We want to give these powers up.’ They would have to want to say that. It is very unlikely that they will because they do not want people to see what has gone wrong. The states would have to cede the powers, the Commonwealth would have to accept the powers, and then we would have to implement the laws to deal with the issue. If we did bring that about, it would not be retrospective. We would

not be able to go back into the past and say, 'We are also going to look after these things that happened in the past.' We would only be able to look after things from that point forward. Would that be right?

**Ms Wilkinson**—I think that is right. I think the other issue if you were contemplating that sort of referral of power is: what would be the scope of the power you referred? To the extent that I have looked at some of the submissions, there has been this discussion not just about insurance but about a holistic approach to the building regulations. You make the insurance work more effectively if it is built within a whole building regulation environment. I guess if you were contemplating some referral of power to achieve the end goal that you really want, the breadth of it might be that you were then referring all building regulation to the Commonwealth government. That would obviously be a significant task, and you would have to analyse the pros and cons of that more.

**Ms Walker**—I guess what I would add to what Vicki is saying here is that, from the Commonwealth's perspective, you would want to think in-principle why the Commonwealth could do a better job regulating the building industry, and I would have thought that there would be a lot of local issues—

**Senator JOYCE**—There would be a lot of suggestions as to how we could, after today's evidence.

**Ms Walker**—I think you would want to think about there being a lot of local issues in the building industry that local government and state government are better placed to address than the Commonwealth government.

**Senator MILNE**—We do have a COAG process. It is not beyond us. The Commonwealth can set principles and require the states to implement them.

**Senator JOYCE**—Yes, I stated that it would have to go to COAG. ASIC policy 139 has been brought up as a pro forma of a certain type of scheme that would give a better transparency and a better process to this. I would be very surprised if you were aware of it. If you are, can you please give me a description of how you would think it would work? If you are not aware of it, can you take it on notice and get back to us?

**Ms Wilkinson**—I think we will take it on notice.

**Senator JOYCE**—Under any CLERP legislation, are there any referrals to acknowledgment of transparency of information to be given to third parties?

**Ms Wilkinson**—No. I think all third-party beneficiaries have some cut-through rights to reinsurers under the Contracts Act, but that is at a totally different point and not pertinent to what you are saying.

**Mr Lim**—The only thing I can think of is where financial planners, for example, need to get professional indemnity insurance, and we have required them to disclose some information about those arrangements to the consumer. But we can do that, because under the Corporations Act powers, we can regulate financial planners, and they stand in the stead of the home builders

in this case. We do not have the same powers over home builders, which is why, as Vicki explained, we would not be able to do it.

**Senator JOYCE**—With regard to financial planners, would there not ipso facto be a case that the people who sold the home warranty insurance are in a form selling a financial product, because they would have to be covered by APRA legislation, would they not?

**Ms Wilkinson**—It depends on who sells it. The product provider, yes, if it is a private insurer, would be APRA regulated for prudential—

**Senator JOYCE**—HIA is flogging this insurance around the traps; they would have to be covered by Corporations Law. They are definitely a corporation—I would put my house on that. They would also be covered by APRA legislation, wouldn't they?

**Ms Wilkinson**—They would be prudentially regulated by APRA as an insurer because they are a product provider. To the extent that they were the intermediary that sold the product to the builder, they would be covered by the Corporations Act; however, if the product was sold by an insurance broker, then the insurance broker would be regulated under the Corporations Act.

**Senator JOYCE**—They would have to have capital issues to cover possible claims that would come against them?

**Ms Wilkinson**—The product provider, yes.

**Senator JOYCE**—The question that has been raised today is: these compulsory funds go off to them and there is an apparent lack of claims coming back in the other direction. There is an assertion—and I am making it—that there is this big pile of money somewhere that is a very nice little earner on behalf of the warranty insurance provider with little money being paid out. Can we get any access to exactly how much they have collected and how much they have paid out?

**Ms Wilkinson**—I think you would have to talk to the individual insurers about that.

**Senator JOYCE**—The answer will be very short.

**CHAIR**—Just to clarify again, the Commonwealth is not in a position to collect that kind of data, and certainly not the Treasury.

**Ms Wilkinson**—The Australian Prudential Regulation Authority collects certain data to perform its prudential regulatory function. I do not know if the specific data that you are referring to would be collected but, to the extent that that sort of data is collected, there are secrecy provisions in the APRA legislation that would limit their ability to disclose that.

**Senator JOYCE**—But APRA would be able to go in and say, 'We want to know how much,' and even though they do not disclose it, they could go in and say, 'We want to know how much you have collected and how much you have paid out.'

**Ms Wilkinson**—I do not know. It would go to whether that was significant for prudential supervision. That question we could either take on notice or APRA could respond to it, if they are appearing. They may have ability to do that but, as I said, there are quite strong secrecy laws that govern their passing on of that information to anyone.

**Senator MILNE**—Could I pursue that particular point, please? You have said in your statement here that, ‘Following consultation with stakeholders, APRA decided to exclude home builders’ warranty insurance from the National Claims and Policies Database,’ blah, blah, blah. Whilst APRA does collect this information for everything else, it seems that it does not collect it for this particular insurance. Have you got any idea which stakeholders APRA consulted and who advised them that this would be a bad idea and, as a result, they advised government, and that seems to be the only insurance that is not collected?

**Ms Wilkinson**—National Claims and Policies Database goes to liability insurance, so it is not all the insurance. That database is not set up for every type of insurance product; it is limited in that way. In terms of APRA’s consultation, I was not personally involved, so I can only speculate, but they would have, I assume, consulted with the insurance providers and other stakeholders. The National Claims and Policies Database was set up post-HIH collapse by the states and the Commonwealth in an attempt to provide increased information, so the stakeholders would have been probably the insurance industry. It may well have been state and territory and Commonwealth governments who had an interest in that data being available.

**Senator MILNE**—I want to pursue this because in your statement you say that following consultation with stakeholders, APRA decided to exclude home builders’ warranty insurance in relation to this data collection. You go on to say:

A separate data collection could potentially impose additional financial and reporting burdens on industry and the benefit needs to be assessed against the cost.

That clearly is a position that the industry would take; it is not a position necessarily that consumers or the public interest would take. I want to find out where the committee can find out about who APRA consulted and where there are notes about those consultations, and can they be provided to this committee?

**Ms Wilkinson**—I think that would best be directed to APRA, because APRA consulted—

**Senator MILNE**—APRA is under whose—

**Ms Wilkinson**—It is under the Treasury portfolio, but they are an independent regulator. The committee may want to request APRA to either appear or to provide that information.

**Senator MILNE**—But surely Treasury can require it of APRA?

**Ms Wilkinson**—I suppose we can take it on notice, if you want to go via Treasury.

**Senator MILNE**—Essentially it is the Treasurer who has responsibility for the Financial Sector (Collection of Data) Act 2001, so I suppose APRA is under Treasury.

**Ms Wilkinson**—They are, but they are an independent regulator. If you would like to direct us, we can ask or you could go directly to APRA, whichever.

**Senator MILNE**—I would like to ask you to provide all that information around the consultations where that decision was made to exclude it, and whether there ever was a cost benefit analysis of how much it would cost to collect that data.

**Ms Wilkinson**—Yes, we will take that on notice.

**Senator JOYCE**—You have to ask them to ask APRA to provide that.

**Senator MILNE**—Yes, that is what I am asking.

**Ms Wilkinson**—Yes, that is fine.

**Senator MILNE**—The second thing I wanted to ask about was the COAG process. They have set a deadline of October for developing enhanced national processes to improve the consumer policy framework, including legislative and regulatory structures that will be based on the Productivity Commission's report.

**Ms Wilkinson**—Yes.

**Senator MILNE**—Is Treasury feeding into that process?

**Ms Wilkinson**—Yes.

**Senator MILNE**—And, of course, we can feed into that process as well, presumably. Essentially, through that process, this whole regulatory area can be looked at.

**Ms Wilkinson**—It can be. I note that the Productivity Commission in its report, when they spoke about home builders' warranty insurance, recognised that the Senate inquiry was underway.

**Senator MILNE**—And they recommended that there should be some sort of national system, and this obviously provides us with the opportunity through this COAG process being finalised in October this year?

**Ms Wilkinson**—I am not sure if it is finalised, or whether they are responding.

**Senator MILNE**—It says a deadline of feeding into it by October, so essentially the regulatory framework within which this insurance is regulated and the whole issue of builders and the home warranty could be dealt with through the COAG process underway.

**Ms Wilkinson**—Yes, if the committee and COAG were of that mind.

**Senator EGGLESTON**—I wondered whether there were any other examples of mandated insurance underwritten by the purchaser? Can you think of any examples of that? We are saying



here that in this case the builders are required to have the insurance, and in effect that creates a situation in which the purchase of the builder provides the insurance companies with the capital to provide the cover, does it not?

**Ms Wilkinson**—They pay a premium.

**Senator EGGLESTON**—Yes, and that provides the capital, part of which I suppose claims are met?

**Ms Wilkinson**—The premium purchases the product and then, yes, the insurance company takes that premium and invests it along with all other premium and does what it does.

**Senator EGGLESTON**—Are there any other examples of mandated insurance?

**Ms Wilkinson**—Motor vehicle insurance and workers compensation. Other examples of mandated insurance are workers compensation, motor vehicle and home builders' warranty. Again, in different states and territories, those schemes operate in different ways: sometimes with private insurers; and sometimes state backed. The same pattern that you see in builders' warranty happens in the other mandated classes. The Commonwealth does not mandate any insurance.

**Senator EGGLESTON**—That is what I wanted to know. In your statement, you said that the Treasury agrees with the Productivity Commission's comment that the form and scope of home builders' warranty insurance needs to be considered in conjunction with other aspects of the building industry, including licensing requirements and dispute resolution mechanisms, which I suppose implies that you see that there is a problem with this warranty insurance issue.

**Ms Wilkinson**—From our observations—and we have seen the press reports and the concerns that have been raised at various times—it spiked, obviously, post-HIH, but it has a history before that. So, yes, we have obviously observed press and people writing to federal ministers, and we have seen those concerns.

**Ms Walker**—I think the point we are trying to make there is that you cannot just look at the insurance issues in isolation; you have to look at the whole system.

**Ms Wilkinson**—Again, we are not experts on this area, and the previous speaker obviously was talking about a system that involved an insurance claim part way through an entire process that all tried to build a strong outcome for home builders.

**Senator EGGLESTON**—I think this committee would agree with you that there are other issues such as licensing and dispute resolution mechanisms which need to be looked at, but obviously the mandating of this home warranty insurance and the fact that the builders are the people who are the purchasers of that insurance seems to be a particular problem from the consumers' point of view because obviously the consumers, from the evidence we have received, are not receiving a product that is particularly useful to them. It is far too limited in its scope. One of the other issues that were raised earlier this morning is the capacity for general insurers to be permitted to get into some sort of provision of insurance for defects in building and covering this same ground. Would you have any comment about that?

**Ms Wilkinson**—Again, I guess we have not done a lot of research into that, but at the moment I do not see any structural impediment to the general insurance industry, if they thought there was a market, offering something beyond home builders warranty. Home builders warranty carves out this particular niche area—

**Senator EGGLESTON**—For those three grounds.

**Ms Wilkinson**—And they are mandated, but if you are suggesting that the insurance industry could cover different space, I do not think there is anything that would prohibit that at the moment. So I think it would be an interesting question to ask: ‘Why isn’t that being offered?’ Is there an end consumer demand and is there a general insurance market? I suppose that would drive where there is a market there. Beyond the DDI insurance, there is nothing that prevents other insurance being offered at the moment, no structural problem.

**Senator EGGLESTON**—Because it was not mandated, it could be under the regulation of the federal authorities.

**Ms Wilkinson**—Again, to the extent that it is provided by private commercial insurers, it will always be prudentially regulated under the Insurance Act. In terms of disclosure to the purchaser of the product, that retail-wholesale definition comes into play in the Corporations Act. If the product that was being offered fell within that retail description, then the consumer would get the disclosure; if it did not, as the law currently stands it would not. I suppose if there was a product that was being developed where everyone thought the disclosure should flow to the consumer as a retail client, then we would look at that.

**Senator EGGLESTON**—The wholesaler would be the insurance agent, wouldn’t it?

**Ms Wilkinson**—No. The way the Corporations Act works in respect of general insurance, there are a whole lot of products listed and if those general insurance products are being sold to an individual or for the use of small business, then that individual or the small business is considered to be a retail client. Typically, those products are motor vehicle insurance, home building and contents insurance, travel accident and sickness—those sorts of things. If you are selling that to an individual or small business, they are automatically retail products and you get all those disclosures. If you are selling something like public liability, that is not on that list, so the consumer of that, whoever it is, would be considered to be a wholesale client, and they would not get the product disclosure.

**Senator EGGLESTON**—I have public liability insurance for my office; do I then become a wholesaler?

**Ms Wilkinson**—A wholesale client for the purpose of that product. Then tomorrow, if you go out and insure your car, you would be considered to be a retail client for that product.

**Senator EGGLESTON**—And the agent would be the wholesaler, is that right?

**Ms Wilkinson**—No, the agent is just the financial intermediary. They are selling you the product. They are the ones that might have to disclose to you in some circumstances, but they are not considered the wholesaler.

**Senator EGGLESTON**—I understand this now. If there was a general insurance product for defects in building, the homeowner who purchased that product would be the consumer, and disclosure could occur to that person.

**Ms Wilkinson**—If that product met the existing retail definition in the law. If it did not, then you would have to look at whether it should, and if it should and it did not, you would have to amend it.

**Ms Walker**—In a sense, even if you are a wholesale client, you can still ask for the disclosure, but it is not mandated that it has to be given to you at the time of purchase. But you are still in a position where you can ask for it.

**Senator EGGLESTON**—The other general issue is that professions like lawyers, doctors, accountants have professional indemnity insurance. Are there any analogies to be drawn here with the builders warranty?

**Ms Wilkinson**—Yes, I think there are in some ways, in that for those professions that insurance is sold to the professional, the builder equivalent, but the claim on the policy occurs when a third-party beneficiary loses out for some reason. In the case of accountants, lawyers and others, it is not restricted to when the professional dies, disappears or becomes insolvent.

**Senator EGGLESTON**—Exactly, so it is broader.

**Ms Wilkinson**—That is right. Similarly, for those professions there is often some regulation at state level. Insurance is not mandated for doctors, for example, by the state medical boards, because they choose not to, but the state medical boards set the conditions and things for doctors. It is analogous in that sense. The legal profession is guided by state legislation that governs the legal profession in each state and mandates various things. I do not know off-hand the extent to which they mandate insurance for those professionals.

**Senator EGGLESTON**—As part of this mix of solving the problem that we are dealing with and which is the subject of this inquiry, you have talked about including licensing requirements and dispute resolution. Could part of the solution also be to come up with a form of professional indemnity insurance for builders which was broader than the three current points that builders warranty insurance covers?

**Ms Wilkinson**—Certainly I think state legislation could mandate whatever product they want.

**Senator EGGLESTON**—Not mandate it—but go on.

**Ms Wilkinson**—Well, you could mandate it; then the issue becomes that a private insurer would have to see whether it was commercially viable to offer that product. At the same time, from the consumers' perspective, it will cost something. In an unmandated environment, if there was a market for something that is broader than the currently mandated product, there is no reason why at the moment both the general insurance market and the end consumer could not be seeking that product and buying it. Obviously the factors that drive that from the insurer's point of view are whether it is commercially viable and a risk that they are capable and willing to

undertake, and from the consumers' point of view is whether it is a risk they are willing to cover at the price at which the insurance company is willing to offer it.

**Ms Walker**—There is a third element as well in that, from a prudential regulation perspective, it would have to be a prudentially sound business transaction, otherwise there would be concerns if insurers were offering products that were not considered to be prudentially sound.

**Senator EGGLESTON**—Given all of those things, the situation here seems to be that the consumers are being deceived into believing that they have an insurance policy cover that covers the building that they are having built by the builder, when in fact the scope of that insurance is severely limited and does not really provide the consumers with the protection against bad workmanship, defects in building and various other things that they presume warranty insurance implies.

**Ms Walker**—Obviously that is your observation.

**Senator EGGLESTON**—Yes, I am making an observation. So a broader kind of insurance genuinely providing indemnity to builders for incompetence, deficiencies and so on would be a better product to be offering to the consumer, it seems to me.

**Ms Wilkinson**—It may be, if the consumer wanted that and could pay whatever the price of that was.

**Senator EGGLESTON**—I suspect it would be in the public interest to provide it?

**Ms Wilkinson**—It may be in the public interest to provide it, but a commercial insurer will underwrite a product if it is commercially viable.

**Senator EGGLESTON**—I agree with that.

**Ms Wilkinson**—You may be edging into something that is not—

**Senator EGGLESTON**—What I am really saying is that builders' warranty insurance seems to me so woefully deficient that it is not meeting the public interest in terms of the requirements of the average consumer.

**CHAIR**—That is an observation, I think.

**Senator EGGLESTON**—That is an observation also.

**CHAIR**—One final question: if the states imposed any kind of levy that would go into a fund to provide for consumers, what is the status of that under the Corporations Act; is there any impact?

**Ms Wilkinson**—If it were a state-run sort of insurance? No, it would be something operated within the confines of a state. Again, if a state were to do that, then presumably it could set the standards for disclosure, et cetera, for consumers, but it is not within the constitutional register, the Corporations Law, nor would it necessarily be appropriate.

**CHAIR**—Even if the fund were operated by something like a Master Builders Association or an HIA?

**Ms Wilkinson**—The first issue would be: was whoever was doing it carrying on insurance business as defined under the Insurance Act? That act determines from a prudential point of view whether the Commonwealth legislation applies, and there are a few things. First of all there is the threshold of: are you carrying on insurance business as defined? Secondly, insurance business that is carried on within the confines of the state, again, is not an area where the Commonwealth legislation reaches, although a state might voluntarily comply. That is the prudential side. I suppose the next thing would be for Corporations Act to start to look like it would apply, whether someone was carrying on a financial services business as defined.

**Mr Lim**—And if they were providing sort of a straightforward insurance product, it fell within those definitions that Vicki mentioned—or the government decided to change those definitions to make sure that whatever was being provided would fall under it—and the purchaser of the product was the end consumer, the owner of the home, then the Corporations Act would apply.

**CHAIR**—Thank you. Thank you for appearing here this afternoon. The committee will adjourn and resume at 2.00 pm.

**Proceedings suspended from 1.21 pm to 2.05 pm**

**McCARTHY, Mr Greg, Chair, NSW Home Warranty Insurance Scheme Board****GRIFFIN, Mr Stephen, General Manager, Home Building Service, NSW Office of Fair Trading**

**CHAIR**—Welcome. I understand, Mr McCarthy, you have an opening statement.

**Mr McCarthy**—Yes, if you do not mind. Thank you for inviting us here today. Much of the criticism of the scheme operating in New South Wales in recent weeks has been ill-informed and unhelpful. Mr Griffin and I are here today to present to the committee an accurate account of the home warranty scheme as it operates in New South Wales today. There are a couple of main points I wish to bring to the committee's attention.

Firstly, I ask the committee to note that the New South Wales scheme is vastly different to the private home warranty insurance schemes that operate in other states and territories. Unlike in other jurisdictions, the New South Wales scheme has an independent scheme board responsible for the monitoring of the operation of the scheme. All insurers in the scheme are required to enter into an industry deed with the government over the operation of that scheme. Prior to operating in New South Wales, an insurer is required to be approved by the minister and abide by the conditions of approval introduced in 2004 that guide the conduct of insurers operating in New South Wales. The insurer must also be authorised by APRA under section 12 of the Insurance Act 1973 to carry out an insurance business in Australia or must be a Lloyd's underwriter permitted to issue policies or undertake liability contracts of insurance in Australia under the Insurance Act 1973.

Similarly, market practice and claims handling guidelines have also been developed and implemented to regulate the conduct of insurers. A complaints handling mechanism is also in place, where consumers or builders aggrieved by insurers' noncompliance with its obligations under either the market or claims handling guidelines can be dealt with. Insurers are required to provide the Office of Fair Trading with premium and claims data on a quarterly basis. This information is made publicly available on Fair Trading's website.

The scheme board has a memorandum of understanding with APRA to formalise information sharing and reporting arrangements. The scheme board has now appointed an independent actuary to assist it with the financial oversight of the scheme and the scheme board has in place a stakeholder consultation process to provide feedback on all issues affecting the scheme, and particularly when changes are required. I tender for the committee's information and attention copies of the various approval documents, guidelines and protocols in operation in New South Wales along with the last four quarterly data reports available for 2007.

**CHAIR**—Thank you.

**Mr McCarthy**—Since the inquiry into the operation of home warranty insurance in New South Wales was conducted by Mr Richard Grellman in 2003, the home warranty scheme in New South Wales has undergone substantial change that clearly sets it apart from the private schemes operating elsewhere in Australia.

The Home Warranty Insurance Scheme Board, which I chair, was established and commenced its work in December 2003. The scheme board is independent of the Office of Fair Trading and reports directly to the Minister for Fair Trading. The role of the board, amongst other things, is to monitor the operation of the home warranty insurance scheme in New South Wales and make recommendations to the minister on improvements that can be made to the scheme. The board is comprised of five independent persons with insurance backgrounds, appointed by the minister. The Commissioner for Fair Trading is also a member of that board.

One of the main initial objectives of the board following its establishment in December 2003 was to establish conditions within the marketplace that would allow builders greater access to home warranty insurance cover and improve transparency of the scheme while simultaneously bringing about lower premiums. I am pleased to say that we have achieved these outcomes.

There are currently six insurers licensed to provide home warranty insurance in New South Wales. Developments in New South Wales have seen a return of competition to the market, which has led to improved access for builders and lower premiums charged to builders, a saving which is actually passed on to the consumers.

Whilst the New South Wales scheme is different to schemes operating elsewhere in the country, I am not suggesting that the scheme as it operates in New South Wales is perfect. The board and I have shifted our focus in recent years to enhancing the value of the scheme to the consumer. In keeping with this new focus the government accepted the board's recommendations to increase the minimum level of cover in New South Wales from \$200,000 to \$300,000. This change was introduced on 1 March 2007. Further enhancements to the scheme reducing the onus on the consumer to prove the disappearance of a builder were introduced on 1 October 2007.

In more recent times, the board recommended that the New South Wales government, and it has accepted this recommendation, introduce to the scheme a further trigger for a consumer to lodge a claim under their home warranty insurance. It was clear to the board that consumers were at a severe disadvantage in being required to spend significant amounts of money to file winding-up or bankruptcy proceedings in the legal system in order to access home warranty insurance. Accordingly, the board has proposed to the government that it introduce an additional trigger to the home warranty insurance. This trigger would be suspension of the license of a builder by the Office of Fair Trading for a builder's failure to comply with a money order of the Consumer, Trader and Tenancy Tribunal or a court. Suspension of a builder's license would provide the trigger for the homeowner to lodge a claim with the builder's home warranty insurer. It is the board's view that the introduction of this additional trigger will substantially improve consumer access to home warranty and reduce time delays currently being experienced by some consumers. The government has accepted this recommendation and I understand it intends to introduce a bill into the New South Wales parliament in the near future.

The board recognises that further enhancements and reforms to the scheme are required. The board is currently considering a further range of issues, including home warranty coverage for high rise residential properties. The board will continue to monitor the performance of the scheme and its impact on stakeholders and make recommendations for enhancements beyond those currently being reviewed when and if required.

I note that the committee to date has received some 61 written submissions. Of particular interest to me was that only 14 of those publicly available on the committee's website relate to the New South Wales scheme. Notwithstanding, I wish to draw to the committee's attention the need to clearly distinguish between issues involving the current scheme and issues involving the scheme as it operated prior to 1 July 2002. Many of the complaints about home warranty insurance made to the scheme board and I, and no doubt this committee, by either builders or consumers relate to the previous scheme either government or privately run. I simply make the point that these need to be separated from the issues relating to the current scheme so that a clearer and accurate assessment of this scheme can be made.

I wish to stress to the committee that the home warranty insurance should not be viewed in isolation. It would be wrong to do so, as home warranty is part of a much larger consumer protection framework. In order to make an accurate assessment of the efficacy of home warranty insurance it must be viewed within the wider context of other consumer protection mechanisms. For example, in New South Wales the Home Building Act 1989 contained statutory warranties that oblige a builder to rectify any defects for a period of seven years. Where builders fail to comply with their statutory obligations, consumers are able to lodge a complaint with the Office of Fair Trading. The Office of Fair Trading, often via the use of its building inspectors, conducts on-site mediations, which can result in the issue of a rectification order to the builder. Failure to comply with rectification orders can result in the builder losing his or her license. Reports provided to me by the Office of Fair Trading show that this process is extremely successful in resolving any impasse between the builder and the consumer. Where a dispute is not able to be resolved by Fair Trading's dispute resolutions process the consumer has access to the Consumer, Trader and Tenancy Tribunal. The tribunal is then able to make rectification and money orders in favour of the consumer, thereby resolving the dispute with their builder.

All home warranty insurance schemes, whether they are underwritten by government or by the private sector, are designed to ensure that a builder does not avoid his or her responsibilities. Home warranty insurance forms part of the consumer protection framework that kicks in when a builder is incapable of fulfilling their responsibilities. Accordingly, the operation of home warranty insurance needs to be assessed within this broader framework.

As I mentioned earlier, there is much ill-informed criticism of home warranty insurance, particularly in relation to premiums collected, claims paid and scheme profitability. One of my principle reasons for wanting to appear here today is to address the misinformation and provide this committee with an accurate account of the operation of the scheme in New South Wales.

In New South Wales the scheme board, with the assistance of the Office of Fair Trading, has worked hard to improve the transparency of the scheme. One of the main mechanisms for achieving this outcome has been the collection of data from insurers and the release of this information to the public. I wish to draw the committee's attention to figures from these reports for the 2007 calendar year. During that period, the total premium collected in New South Wales, inclusive of fees and charges, was \$45.4 million. By the end of 2007 a total of 1,252 claims had been made upon the scheme, with a total of \$16 million in claim payments and a further \$7 million in estimated future payments on those claims which have been accepted.

Despite information from other ill-informed sources, insurers are not making super economic profits from the scheme. Claims are being made and paid and consumers are benefiting from the



scheme. It would be my submission to the committee that, for every complaint you receive about the scheme from a consumer, there would be many more who are happy with the protection provided to them by home warranty insurance. I am sure that these people do not consider home warranty to be junk insurance.

The final point I wish to make before taking questions is about the failure of detractors of the scheme to recognise the long tail nature of the scheme. A policy written at the very commencement of this scheme on 1 July 2002 remains open to this very day. Policies written under the scheme provide protection to consumers for six years. Accordingly, premium collected in 2002 could still be drawn down by claims made this year. As a result of this characteristic of the scheme, the fact is that we do not know the true profitability of the written premium in 2002 and will not until at least the end of 2009 or possibly 2010. It is for this very reason that observers of the scheme should not make comparisons with other classes of insurance available in the marketplace.

In summary, the data on the operation of the scheme as it has operated in New South Wales since July 2002 clearly shows that it is delivering protection for consumers. Despite the ill-informed commentary suggesting that home warranty is junk insurance, claims are being made by consumers and they are being paid. Access to home warranty cover for builders has improved dramatically since the collapse of HIH and FAI. The scheme board has received no complaints from individual builders or industry stakeholders that builders are having difficulty today getting cover for home warranty insurance. The level of protection for consumers in New South Wales has been increased and further enhancements to improve access to making a claim are on their way.

These are the facts on the operation of home warranty insurance as it operates in New South Wales. Once again, I ask the committee to recognise the unique characteristics of the New South Wales scheme and the efforts made in this state to improve the value of home warranty protection to consumers.

**CHAIR**—Thank you. Mr Griffin, do you want to make a statement at this stage?

**Mr Griffin**—No, I have no statement to make.

**CHAIR**—Mr McCarthy, the Home Warranty Insurance Scheme Board, of which you are chair, was set up in 2003. Why was that set up? Can you explain a bit more about who operates the board, who you report to and who is on the board?

**Mr McCarthy**—The board was set up out of the findings of the report provided to government by Richard Grellman to instil more transparency into the scheme and to provide oversight of the running of the scheme, similar to other statutory classes of insurance that operate in Australia today such as workers compensation and compulsory third party personal injury motor vehicle schemes.

**CHAIR**—So any of these mandatory insurances are now covered by a board?

**Mr McCarthy**—That is right. Certainly in New South Wales, both the workers compensation scheme and the compulsory third party scheme have independent boards that oversight the

management of those schemes. It was set up to provide that oversight. It was set up independent of the department of fair trading as an insurance scheme board, with the expectation that the people on that board would have experience in insurance, to report to the minister. Its immediate challenge was to overcome the difficulties that builders in the scheme were having in obtaining home warranty insurance. It immediately set about trying to introduce greater competition into the scheme and developing the industry deed that insurers entering the scheme would have to operate by. The guidelines for the various operations of the scheme were also one of its immediate objectives.

**CHAIR**—So the immediate objective was to assist the builders, as such. What responsibilities does the board have to consumers?

**Mr McCarthy**—Since achieving its objective of overcoming the difficulties that builders had, the board's focus has now shifted towards the consumers. It has been that way probably for the last two years now. I have outlined some of the changes in the submission in respect of giving consumers greater access to making claims within the scheme. As I have outlined, we have provided a set of recommendations to the government which they have accepted. As I understand, bills are being prepared now, such as that additional trigger that I spoke of in the paper, which will avoid the need for consumers to go to the time and expense of winding up a builder before they can actually make a claim.

**CHAIR**—Can you tell us a bit more about your recommendation for that trigger?

**Mr McCarthy**—There have been some examples in the scheme where consumers have been delayed significantly and incurred significant cost and, I guess, personal irritation over the time that it has taken for them to get to a stage where they could lodge a claim. The board was of the view that this was not appropriate and has gone about developing this new trigger. It has taken quite a bit of time to get that into place because we go through quite a formal stakeholder consultation process to do that. We have been through all of that. The insurers, the building groups and the stakeholder groups have all been consulted. That has all now been completed and as I understand it—and I can defer to Mr Griffin on this—the bill is being drafted.

**Mr Griffin**—Yes, that is correct.

**CHAIR**—You mentioned already that in October 2007 there had been some similar provisions about disappearance of builders.

**Mr McCarthy**—I will defer to Mr Griffin on the detail of that because they were responsible for carrying out that work on the board's behalf.

**Mr Griffin**—The changes made in relation to the disappearance of a builder came about as a result of some issues that consumers were bringing forward about the lengths they were being asked to go to by an insurer to prove that a builder had disappeared. Our view and the scheme board's view was that that was not a role to be played by the consumer and it did not fit well within the normal consumer protection framework that Greg has outlined. The view was that the consumer should be coming to the Office of Fair Trading to try to resolve or mediate the dispute. As part of that process, Fair Trading would make attempts to locate the builder. If the builder could not be found by Fair Trading, Fair Trading would provide a letter to the consumer and that

was what the insurers would then accept as proof that the builder had indeed disappeared. This in no way affected the insurer's right to go and do its own search and inquiries, but it certainly prevented the insurer from going back to the consumer asking them to provide further information about what levels of search and inquiry they had undertaken. As a result, the claims handling guidelines that guide the conduct of insurers were amended and reissued to reflect this change in protocol.

**CHAIR**—Typically, how long would the Office of Fair Trading spend in trying to find a builder that seemed to have disappeared?

**Mr Griffin**—Our guarantee of service in terms of mediating a dispute is 40 days, so it would be less than two months in terms of completing the dispute resolution process. It would only be a matter of weeks to do those searches, inquiries, accessing various databases and so forth and then coming to a determination that we could not locate the builder and providing a letter to the consumer which would enable them to access home warranty on the basis that the builder had disappeared.

**CHAIR**—Did the change in the limit from \$200,000 to \$300,000 require legislation or was that simply a regulatory change? How did that happen?

**Mr McCarthy**—It was as a result of recognising that since home warranty insurance was introduced the escalation and cost of building had moved on and that we should turn our attention to addressing that.

**CHAIR**—It was simply a board decision, was it?

**Mr McCarthy**—That is right. The board made a recommendation again to government which they accepted. I also should stress that \$300,000 is a minimum. If people wish to take out more insurance, they can.

**CHAIR**—Okay.

**Mr Griffin**—It actually did require a change to the regulation, the Home Building Regulation 2004.

**CHAIR**—Does anyone take out further insurance other than the minimum provided through the home warranty insurance?

**Mr McCarthy**—Not that I am aware of, but it is there if they wish to avail themselves of it.

**CHAIR**—In your opening statement you said that a failure to provide rectification of services could lead to a loss of licence by the builder, and that is from the Office of Fair Trading. Is there any thought to working that in with the home warranty insurance at that stage as a kind of early trigger about a claim, or is that going to happen much further down the track still?

**Mr Griffin**—That is somewhat problematic, in that it is probably somewhat unfair to the builder at that stage. At that stage a decision has been made by an inspector in terms of a mediation result and the builder really has to be given the opportunity to make good the defects

to the home. So to activate a trigger at that early stage, from our point of view, would perhaps be unfair. It would seem much fairer for the issue to have gone right through the dispute resolution process to afford the builder some procedural fairness and natural justice in a court or a tribunal before that point was reached.

**CHAIR**—At what stage do you feel that some sort of trigger should be reached? Does it not happen until there is an actual loss of licence? At some point would you actually consult some of the clients of that builder? Do you ever work proactively like that or is it up to the client to contact you if there is no work or faulty work being done with the building?

**Mr Griffin**—The process is that the consumer contacts us, and they do, very often. The mediation process is very successful; around 90 per cent of those issues are mediated by Fair Trading. The others end up in the tribunal situation. The trigger that is being proposed is in relation to the very end of this resolution process. There is a spectrum of dispute resolution, from telephone intervention by a Fair Trading officer to involvement of a building inspector. If all of those things do not work, at the end of the dispute resolution process is the tribunal. At the very end of the process when a money order is made is when we think it is prudent to have a suspension of the builder's licence for failure to comply with that money order. At that point, all those processes have been dealt with, the builder has had ample opportunity to put forward their case in terms of natural justice, and that is where the builder really needs to be able to fulfil their responsibilities or the consumer be able to access home warranty insurance.

**CHAIR**—How does a builder get his or her licence and for how long is that licence period?

**Mr Griffin**—They get a licence through a process of obtaining a qualification. On 1 January 2006 we changed our licensing requirement to be a pure qualification pathway. Prior to that, the qualification pathway was by years of experience. There was a qualification requirement but you could also come into the building industry through having 20 years experience, being assessed by a training provider and given a certificate to show that you were qualified. But from 1 January 2006 the entry requirement for a builder in New South Wales is all qualifications under the Australian training framework, that is, a certificate IV level, plus two years experience. In addition, there is a fit and proper person process to ensure that the person is not a bankrupt or an undischarged bankrupt for the last three years and has no significant criminal history in terms of fraud and other activities. These licences are up for renewal on either a one- or three-year period, so builders at the moment can either opt for a three-year or a one-year licence.

**CHAIR**—Do you have any register of whether a builder has perhaps repeatedly failed or done poor quality building? Is that able to be taken into account?

**Mr Griffin**—Yes, it is. We have a public register of all the builders and trade contractors that we license in New South Wales. They are on a public register and complaints that are substantiated against them are recorded on a public register.

**CHAIR**—Senator Joyce, do you have any questions?

**Senator JOYCE**—Thank you very much. Your presentation sounds like there is a big misunderstanding. To clarify that, can you, as members of the board or with your involvement in the board, describe to me what you believe are the issues that are held as points of concern with

regard to the public's view of the home warranty insurance scheme? Even if you believe they are misplaced, what do you believe are their concerns?

**Mr McCarthy**—I think some of the concerns are around the level of premium and profitability of the insurers. There are some concerns around issues such as commissions that the insurers pay to brokers and the like; the board is discussing their appropriateness at the moment. Other concerns are the time that it might take to have a claim considered and some of the aspects that consumers might have to go through in order to have a claim. Many of the issues that we had with builders have been addressed, such as the access to insurance. I think there are still some concerns by builders around deeds of indemnity. We are investigating that aspect at the moment to find out where they apply, particularly within the current scheme. I have to say that the board at the moment is only responsible for the current scheme; when we get issues that relate to prior schemes we pass those through to Fair Trading to deal with.

**Senator JOYCE**—I might add a couple to those, just from what I have heard today. One is that they believe they are covered when they are not. That is probably the big one. People believe the insurance that they pay for covers certain issues and there is obviously a different view by the insurer, who believes they are not covered. When people employ the builder, they know the builder is covered by insurance and possibly the reason they come to this conclusion is because no document is actually ever handed to the owner of the house or the owner of the building. Maybe under law they do not have to be handed the document, but they believe that a clear, concise document clearly outlining what their position is and what their obligations are and what they have to pay for is not there. I see you have just grabbed a document. Are you about to tell me there is such a document, Mr Griffin?

**Mr Griffin**—Yes, it is. In actual fact it is a legal requirement for builders who enter into a contract with a consumer to give the consumer the *Consumer building guide*.

**Senator JOYCE**—The consumer in this case being the owner of the building; not the builder, but the owner of the building?

**Mr Griffin**—Being the owner, the builder. If you are talking about third party, it is the person who they are contracting with.

**Senator JOYCE**—Therefore that insurance agreement refers to the actual owner of the building—is that what you are saying?

**Mr Griffin**—There are a couple of things. In relation to section 7A of the legislation—and I do not want to go into sections of the Home Building Act of New South Wales—there is a requirement first of all for a builder who is entering into a contract to give the other party, the consumer, the owner of the property, the *Consumer building guide*, and I will tender that for you.

**Senator JOYCE**—That would suggest to me that he is acting as an agent in referring that insurance contract on.

**Mr Griffin**—I will get to the second part in a minute. There is a checklist in the *Consumer building guide* for the consumer to concern themselves with and inform themselves prior to entering into the contract.

**Senator JOYCE**—All I need to know is: the builder refers the details of the insurance contract in a document to the owner of the building, therefore he is referring the insurance contract on to the party, being the consumer, who he says is the owner of the building. Now, that would start to suggest that it is covered by APRA and ASIC.

**Mr Griffin**—That is given as part of the contractual arrangements. At the same time the contract is signed, the builder receives the five per cent deposit under the contract and is required to give the consumer a certificate of insurance from the insurer.

**Senator JOYCE**—You ask them to do that?

**Mr Griffin**—It is the law.

**Senator JOYCE**—That is interesting because then it becomes an arguable position as to whether he is acting as an agent.

**Mr Griffin**—That is the requirement of section 92 of the Home Building Act in New South Wales.

**Senator JOYCE**—Do you check to make sure they are actually doing that?

**Mr Griffin**—We do. We conduct compliance programs to make sure that they do that.

**Senator JOYCE**—You have oversight over that. I want to refer you to a media release that was put out by Richard Amery, state member for Mount Druitt, in 1995, because it talks about the sentiment of your organisation. Mr Amery said that Labor's reforms for the building industry will ensure—and this is about the body, you remember—that at least 50 per cent of the members of the home building advisory council represent consumers. Can you please tell me who on the board represents consumers' interests?

**Mr McCarthy**—You were talking about the advisory council not the board. The advisory council does actually contain representatives from consumers. It is a separate body.

**Senator JOYCE**—Just tell me who represents consumers on your board.

**Mr McCarthy**—The board was not designed to represent consumers; it was designed to set up an insurance board. There is an advisory council that works independently of the board to advise the minister on matters related.

**Senator JOYCE**—Who represents consumers on that advisory board?

**Mr Griffin**—In terms of the names, we will have to take that on notice.

**Senator JOYCE**—Is there anybody on the board or the advisory committee who represents builders' interests?

**Mr Griffin**—Yes, there is.

**Senator JOYCE**—Who are they?

**Mr Griffin**—Again, I would have to give you the names of the builders involved on notice. I am able to give you a complete list of those people and their placement on the board and I will take that on notice.

**Senator JOYCE**—You have said that people get the bare minimum but if they want more with regard to insurance cover, they can get it. How do they know what the bare minimum is and what it represents? How are they made aware of that? Do they go through a needs analysis with the consumer? Do they sit down and say, ‘This is what you’re buying but this is what you probably will need’?

**Mr Griffin**—I have tendered the document. The *Consumer building guide* contains information about what the policy covers so the consumer is aware upfront what the insurance policy provides.

**Senator JOYCE**—Roughly, what is the cost of the insurance policy? What do you see as a ballpark figure for that product? Does it cost hundreds or thousands of dollars?

**Mr McCarthy**—From our data, the average premium, including charges, per project certificate for builders is \$749 as at December 2007—that is the average cost.

**Senator JOYCE**—Let’s say that is the average cost. At what level do you think—let’s say it got to \$1,000 or \$3,000—it warrants someone sitting down at the kitchen table with the person to whom you are selling the policy and clearly explaining to them exactly what is in it? In my unfortunate earlier life, I owned an insurance agency and it got to a point where I actually had to sit down and tell people what was in the insurance policy before you sold it to them.

**Mr McCarthy**—I would have thought that perhaps any money that you are spending might warrant somebody explaining to you what it is about. That opportunity actually exists for consumers to have that dealt with.

**Senator JOYCE**—How do they get that opportunity?

**Senator MILNE**—How?

**Mr McCarthy**—By speaking to the insurer.

**Senator JOYCE**—You said in your presentation, Mr McCarthy, ‘We’ve had problems, we acknowledge problems, we are going to fix problems up in the future.’ That is a good position for you to have because there obviously are concerns out there in the public. The other issues that have come through again and again today are that of transparency, of consumer knowledge of the product and as to where the money goes. I heard you said it brought in \$45 million in premiums. How does the consumer know about the product if someone does not actually sit down with them? The builder is going to sit down with them, one on one, and say, ‘Where do you want your robe; where do you want your toile; where do you want your lights; and what sort of carpet do you want?’ Where is the section where someone sits down with them and says, ‘This is the premium that is being paid and by default paid by you. These are your rights and

obligations. Do you have any queries to ask on that? Or, is it just that a customer information brochure is handed across, with the builder saying, 'You'd better have a look through that some time too'? There are question marks as to whether everybody is getting one of those brochures.

**Mr McCarthy**—There is no requirement for that to take place.

**Senator JOYCE**—I think a requirement like that would sort out a lot of the aggravation and problems.

**Senator MILNE**—Can I follow your questioning on compliance? Senator Joyce just asked a minute ago about whether there is any requirement for the consumer to be shown the policy by the builder and have it explained to them. You said, 'Yes, there is. We have compliance requirements in place to make that occur.' We heard this morning—and we have seen a lot of submissions—that that is not the case, that the consumer never saw the policy, never had any idea what the builder had signed them up to and they just made assumptions about it. If you are saying the compliance is there and it happens, how can it be that all these people are saying it did not happen? What are your compliance procedures?

**Mr Griffin**—Yes, certainly. Apart from getting complaints, investigating them and taking action against builders for not complying with various legislative requirements, we conduct compliance campaigns where 30 or 40 officers go to building companies throughout the state to check the records, checking that they have supplied home warranty insurance and the consumer guide to builders. We ran a large compliance campaign last year and one earlier this year. Our compliance campaign showed that the majority of the big builders are doing the right thing. It did show a higher level of noncompliance with subcontractors—people who just do concreting only or carpentry only; they were the people who were less likely to be complying with the requirement to provide home warranty. There are tough penalties in New South Wales for not doing that.

**Senator MILNE**—You are mixing up two issues. One is compliance of having home warranty and the other is the builder, having taken out the insurance on behalf of the consumer, informing the consumer about what it is they are actually buying. You are mixing up the two in your answer. I heard you just say that you have run some compliance campaigns and you have given material to builders. Have you run any kinds of surveys? Have you interviewed any people who are the consumers of this product and said, 'Did the builder show it to you; did the builder explain it to you?' Have you done anything about compliance at that level?

Have you run any kinds of surveys? Have you interviewed any people who are the consumers of this product and said, 'Did the builder show it to you, did the builder explain it to you?' Have you done anything about compliance at that level?

**Mr Griffin**—No, we have not conducted any surveys.

**Senator MILNE**—So you cannot say there is compliance because you do not know.

**Mr Griffin**—There are requirements that we can check on in terms of compliance. The requirement of the builder is to supply the consumer information guide, and we check on that, because that is the information the consumer gets about the product and what it covers. We also



check that the home warranty insurance certificate has been provided to the consumer as part of the transaction process. They are the main tenets of the legislative requirements. There is no requirement as it currently stands for the builder to sit there, as Senator Barnaby Joyce is suggesting, and explain the insurance product to the consumer.

**Senator MILNE**—Sorry, Barnaby, I just wanted to clarify that.

**Senator JOYCE**—It is part of CLERP legislation in so many other areas of insurance, though. That is exactly what you have to do now: you have to sit down with the person and explain to them. There were some times where it was quite nauseating actually, because they would be buying something that is quite simple but you had to sit down and explain the components of the insurance so that if they wanted to upgrade they had that opportunity. People do not know to upgrade their insurance when they do not know what they are getting in the first instance.

I just want to go through the collection of money. You said you collected about \$45 million in premiums last year and you paid out \$16 million—I just jotted this down about five minutes ago, so correct me if my memory is wrong—and you said there is a tail out there, that other claims may come in in due course. I acknowledge that that might be the case, but I would say that they are substantially less than they would be in the first instance. This scheme been going since 2003—is that right?

**Mr McCarthy**—2002.

**Senator JOYCE**—So the insurance companies would be starting to build up quite a corpus of funds. Is that a greater proportion of collection to what they are having to expend than with other forms of insurance? How does it compare across the insurance industry?

**Mr McCarthy**—Our data is too immature to comment on that at the moment. The reason we are collecting the data is so that we can make those sorts of comments in the future.

**Senator JOYCE**—I know the insurance is compulsory, but how many people can provide this home warranty insurance?

**Mr McCarthy**—There are six insurers in New South Wales at the moment that can provide it.

**Senator JOYCE**—Is there good market knowledge? Do people know they can get a cheaper premium than what they are offered? Do people know that, if all they are buying is if a person drops dead on them that someone is going to finish the building off, they can get a cheaper premium elsewhere?

**Mr McCarthy**—I think we would say yes to that because we have seen the premiums dropping in the last several years as a result of their ability to be able to shop around.

**Senator JOYCE**—How do they get that ability to shop around? If the builder is just handing the cost across to the consumer and the consumer is ultimately paying for it—

**Mr McCarthy**—It is the builder that is purchasing the insurance, though.

**Senator JOYCE**—So it is the builder who makes the decision, not the consumer that makes the decision. Can you not see that there is a bit of a disjoint there? The person you are trying to fix up if something goes wrong is the consumer; the person who is making the decision about what insurance policy they are going to buy is the builder. They are two different people.

**Mr McCarthy**—That could be the case.

**Mr Griffin**—If I could just add that, as Mr McCarthy said at the beginning in his opening statement, it is a different type of product. It is purchased by a third party; it is a third-party product. And the same as in other jurisdictions, including Queensland, it is done by the builder on behalf of the consumer. The consumer ultimately pays, that is correct. That is the situation.

**CHAIR**—I should point out that that is the requirement under legislation. It is not the people here who have decided that; they are only administering the scheme.

**Senator JOYCE**—I can understand that, but what I am pointing out is that it is a flaw in the legislation because obviously the builder is going to buy something cheap and nasty because it does not really worry him—it is not his house.

**Mr McCarthy**—However, it is a statutory cover, so the policy conditions would be the same regardless of whoever they are buying it from. That is right, it is the builder who is buying the insurance. It is there to provide protection to those people he builds a home for, so that, should the circumstances eventuate that the policy covers eventuate, the consumer will be protected. As I say, it is the builder's insurance. It is providing protection to the consumer.

**Mr Griffin**—Can I just add something to Mr McCarthy's answer, Chair?

**CHAIR**—Yes, Mr Griffin.

**Mr Griffin**—The market practice guidelines that insurers are obliged to abide by in New South Wales require them to have available to any consumer the information in respect to that policy. If the consumer is concerned about the level of cover, once they get a certificate they are able to contact the insurer and the insurer is obliged, under the market practice guidelines, to provide the consumer with that information.

**Senator JOYCE**—Mr Griffin, it is a circular argument because the consumer does not know that he should be concerned. He has not found out that he should be concerned. The evidence that we are hearing is he does not have enough knowledge of exactly what he is buying before he buys it. If he knew what he was buying he would probably buy more to cover himself more appropriately for the problems that obviously come about.

**Senator MILNE**—That is the point I just want to follow up on.

**Senator JOYCE**—I will let that go, then. You have many recommendations coming forward, Mr McCarthy, and I can understand possibly some of the impetus and the reasons why, because it is a very emotive issue and that is self-evident in the room. Are you able to tell us of any of the recommendations you are going forward with at the moment?

**Mr McCarthy**—I have talked about the new trigger that we have introduced. The board is still considering the issues in terms of further recommendations. At this point it is too early to state those publicly until it has had an opportunity to properly discuss those issues.

**Senator JOYCE**—Finally, regarding duty of agency, if I have made representation to you that you are buying a certain thing and you fully believe that and you go out and buy it, then, regardless of what is in the document, what I represented to you is what you are able to go back and ask me for. If this is being moved on to someone else who is obviously acting as an agent because he says, ‘Here’s the policy and here’s the CIB,’ then what does that do? If he says, ‘What this does is it covers you so if the place falls to pieces you’ve got the right to get it fixed up,’ that is a representation and I am bound by that, regardless of what is in that document.

**CHAIR**—Thank you. Senator Milne.

**Senator MILNE**—I just want to follow up on the line of questioning that Senator Joyce was talking about. You said earlier that consumers can go out and get more insurance if they wish to have more insurance but, as we have established, it is the builder who buys the insurance and then the consumer may or may not ever know what they have actually purchased. But isn’t it true that the builder buys the policy based on the contract value?

**Mr McCarthy**—In terms of the pricing of the policy, yes, it is. As you know, there are some contracts that are greater than \$300,000 and it is in that instance that I am referring to the fact that someone could purchase a greater level of cover if they desire.

**Senator MILNE**—Yes, but what is very clear to me is the builder would go and get this insurance based on the contract value, the consumer is not even told about it in a lot of cases and does not know what they have got. The likelihood of anyone going and getting more insurance is remote. So I would suggest that it was a fairly disingenuous suggestion that there was even the opportunity to do it.

**Mr McCarthy**—I can just say to you that the opportunity does exist.

**Senator MILNE**—The opportunity does exist to protect people and to protect consumers, but we are not, frankly, seeing a lot of it. Regarding the graphs and tables that you handed out, you said earlier that in New South Wales it is transparent that the last resort home warranty exists and the insurance companies have to provide the information, and it goes up on your website. So can you tell us what is the current claims-loss ratio for last resort builders warranty insurance in New South Wales?

**Mr McCarthy**—I pointed out to Senator Joyce a moment ago that our data is too immature to provide that information at the present point in time.

**Senator MILNE**—How long have you been collecting this data that is going up on your website?

**Mr McCarthy**—Twelve months.

**Senator MILNE**—Only 12 months.

**Mr McCarthy**—We had to start somewhere.

**Senator MILNE**—Why did it take you this long to get to that point?

**Mr McCarthy**—There is quite a lot involved in going through the data specification requirements that can be applied across all of the insurers that supply data to us. We had to engage external consultants to work with the insurers to get the data specification programs in place. It is no different to any other statutory class of insurance when you are trying to get these processes into place; they just take time.

**Senator MILNE**—Regarding commissions, you said the board is now talking about the commissions that are being paid. Since you are talking about it, you have got some idea of what they are. What sorts of commissions are being paid?

**Mr McCarthy**—We are talking about it because we want to investigate what are the levels of commission. At this point we do not know. We are looking at introducing some processes into the scheme that will enable us to identify the level of commissions that will be paid.

**Senator MILNE**—When you say you are talking about it—

**Mr McCarthy**—It is being discussed at board level.

**Senator MILNE**—The problem is being discussed at board level?

**Mr McCarthy**—The issue is being discussed at board level.

**Senator MILNE**—But no-one has got any idea at this point except the insurance companies, and HIA presumably, exactly what the commissions are that are actually paid?

**Mr McCarthy**—That would be correct and that is why we are looking to introduce a policy to enable us to understand that.

**Senator MILNE**—Can I go on to the issue of the system in New South Wales of inspecting building works when it is under construction.

**Mr McCarthy**—I will have to defer to Mr Griffin on that.

**Senator MILNE**—We have heard quite a lot of evidence about that this morning. Can you tell us what is required under the law in terms of building inspections during construction?

**Mr Griffin**—Whilst this is not part of Fair Trading's role it is part of the Department of Planning and the Building Professionals Board so I can give you some generalities. The Environmental Planning Assessment Act 1979 in New South Wales requires critical stage inspections of homes and a greater level of inspection of high-rise buildings during the construction process. Those inspections can be carried out by either a council building inspector or by a private certifier who the consumer engages to do those inspections on their behalf. Those stage inspections are required to be lodged with local councils as part of the development application process.

**Senator MILNE**—How can it be that buildings can be completed before there has been any real inspection going on?

**Mr Griffin**—If that is occurring, that is a problem with the building inspection process.

**Senator MILNE**—Where would a consumer go to complain about that?

**Mr Griffin**—To the Department of Planning.

**Senator MILNE**—How long would it be before their complaint was dealt with?

**Mr Griffin**—I cannot answer that; you would have to ask the Department of Planning and the Building Professionals Board to give you a response on that matter.

**Senator MILNE**—I will pursue that in another arena. I will go back to the payouts that are made under this last resort insurance. Is it true that the insurance companies are engaging in what can only be described as litigation for harassment, where they offer a settlement which is wildly under what could be expected and then the consumer is left with having to take it through the courts and probably lose everything? The insurance company can offer an absolute minimum and bankrupt someone in order to secure more.

**Mr McCarthy**—I can only comment on the current scheme. Within the current scheme, the board is not aware of any complaints on that issue. I cannot comment for prior schemes.

**Senator MILNE**—You are saying that there are no complaints at the moment from anyone, that the insurance companies are paying out and that nobody is complaining?

**Mr Griffin**—I think the complaints that do exist relate to the issue of quantum and arguments over quantum in terms of insurance claim payout. They do exist. Those matters currently get determined by the Consumer Trade and Tenancy Tribunal in New South Wales. That is the forum that makes a determination on whether the offer of payment by the insurer is fair under the policy.

**Senator MILNE**—What is the time frame on this? How long is the consumer left out there fighting this? Is there any time line under law whereby they have to settle something or something has to be heard by the tribunal or can this go on for years?

**Mr Griffin**—The tribunal does have benchmarks. I cannot speak on behalf of the tribunal but I am happy to take that on notice and get that information back to the committee.

**Senator MILNE**—The tribunal has benchmarks; one of those benchmarks you are seeming to suggest is a time line.

**Mr Griffin**—They do have time lines for lodging, having first hearings and trying to have matters resolved within the tribunal process, yes.

**Senator MILNE**—Again, we have received lots of evidence from people saying that this goes on for a long time. We have also had evidence, of which obviously Mr McCarthy is not aware, of

people who say that the insurance industry is offering them minimal amounts and forcing them into a litigious process that is a warning to other people. Essentially, if you take people through a litigious—

**Mr McCarthy**—If you are asking us to comment on whether we have had any of those complaints made directly to the board, we have not. They may be being dealt with by Fair Trading, and that is why I deferred to Mr Griffin on that issue.

**Senator MILNE**—Mr Griffin, you are saying that Fair Trading is not aware of any of that kind of complaint?

**Mr Griffin**—No, I did not say that at all. I actually said to the contrary, that there are people who have complained not only about the current scheme in terms of the time and effort. I know this committee has received submissions from an individual in New South Wales and there have been others in the gallery here who have had long protracted matters through the courts and tribunals. Again, this is one of the principal reasons for us to bring in this additional trigger, to subvert the need for consumers to go through that long, costly, time-consuming process before they access home warranty insurance and hopefully to resolve the matter before it gets into a long, protracted legal battle.

**Senator MILNE**—Given that this trigger is going to address that, what about all the people who have suffered before?

**Mr Griffin**—Unfortunately it is one of those situations where it could not be made retrospective, Senator, because the policies have been written and matters have been dealt with in the appropriate forums.

**Senator MILNE**—I appreciate you cannot make policies retrospective but there are a lot of people affected by the time lag that it has taken Fair Trading and anybody else to recognise the problem. Given that that is the case, apart from bringing in the trigger, is there any other legislative recompense or mechanism to deal with these legacy issues?

**Mr Griffin**—I would have to take that on notice and give you an answer out of session on that issue. I am not aware of any off the top of my head. There are always opportunities for people to make ex gratia payment claims from government where they think that the processes have let them down. Those ex gratia claims are dealt with on a case-by-case basis. At the moment, off the top of my head, I am not aware of any other mechanism for resolving those issues.

**Senator MILNE**—When is your expectation that the trigger will be legislated and in place?

**Mr Griffin**—We are hoping to have it in the spring session of state parliament this year. That is my understanding of where it sits at the moment, Senator.

**Senator MILNE**—Thank you.

**Senator EGGLESTON**—I was just looking at the report of the New South Wales state parliament's General Purposes Standing Committee No. 2 on these issues. One of the issues that

they were concerned about was poor consumer protection offered by the current home warranty insurance scheme. They say:

We consider it highly desirable that coverage be extended beyond the 'last resort' circumstances of a builder's death, disappearance or insolvency. We are similarly concerned by reports that the current scheme leads to the escalation of disputes rather than their early resolution, and that payouts are sometimes inadequate while the consumer costs associated with exhausting other avenues before claiming on insurance can be exorbitant.

Some of those issues have been covered already. What would you say about the statement that the current scheme leads to the escalation of disputes—do you think that is the case?

**Mr McCarthy**—No, I would not.

**Senator EGGLESTON**—In short!

**Mr Griffin**—If I could add to Mr McCarthy's answer, it is important to view the current scheme in the context of the current consumer protection framework, which, I might just add, has really only been in place since 1 July 2003. The current scheme is an escalation process in the sense that you obviously start off with the dispute with the builder and you try to deal with that through the client-builder relationship. That would then escalate to a report to Fair Trading, who would try to resolve it through telephone contact and approach. If that did not work, that would escalate to the involvement of the building inspector from the Home Building Service. If that approach failed, then obviously that would escalate to the Consumer, Trader and Tenancy Tribunal. So there is an escalation in a sense, if that is what you are suggesting. Certainly from our point of view, from the statistics we have maintained there has been a reduction in the number of complaints that have come to Fair Trading since the beginning of the process. Of course, economic factors are involved in cause and effect there. But certainly there has been a 30 per cent reduction in matters that have gone before the tribunal that were going there prior to the commencement of dispute resolution in New South Wales.

**Mr McCarthy**—That was the reason for my answer.

**Senator EGGLESTON**—That paragraph concludes:

The fact that both consumer and industry representatives highlighted these deficiencies attests to the weight of the problem.

Are you in effect saying that is just not the case, that there is not a real issue about poor consumer protection?

**Mr McCarthy**—Nobody is trying to suggest that this scheme is perfect, and I think I said that in my opening address. We are continually monitoring the scheme for how we can improve the consumer issues in relation to consumers, hence the introduction of the new trigger. We would be foolish to sit here today and suggest that we will never identify other mechanisms by which we can improve consumer protection. We are not trying to sit here today and suggest that this scheme, as it stands, requires no further improvements. But our role as the scheme board is to identify what those issues are, take on board what the various stakeholders say and move that forward over time.

**Senator EGGLESTON**—You are intending to continually improve it and accept the deficiencies at the moment or the problems that are there. The other question I would like to ask you follows up on Senator Joyce's comment that the consumer, the purchaser, could be engaging the builder and thereby the builder becomes his agent in a legal sense. That was a question which I had thought of putting to the Treasury officials in the previous section. Can you take that question on notice?

**Mr McCarthy**—I was just going to say to you that I would not like to try to respond to that question without some advice. I would like to take that question on notice if I could.

**Senator EGGLESTON**—It really does have some implications in terms of the right of the consumer to be informed about the contents of insurance and various other things.

**Mr McCarthy**—I understand the point of the question and I would like to take that on notice and we will have that investigated.

**Senator JOYCE**—He or she believes they are buying the product, they believe you are selling it to them and they believe you are the representative of the sale of the product to them, therefore entailed in that relationship is a relationship of agency.

**CHAIR**—As there are no further questions, thank you, gentlemen. It has been very useful because we have got some hard information from you that has been difficult to get from other sources, even though it is relatively limited. If we have got any follow-up questions, particularly in response to the questions you have taken on notice, would you be able to take those questions from the committee in writing?

**Mr McCarthy**—Certainly.

**CHAIR**—Thank you for appearing here this afternoon.

**Committee adjourned at 3.08 pm**