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STANDING COMMITTEE ON ECONOMICS

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

WEDNESDAY, 17 SEPTEMBER 2008

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**SENATE STANDING COMMITTEE ON
ECONOMICS**

Wednesday, 17 September 2008

Members: Senator Hurley (*Chair*), Senator Eggleston (*Deputy Chair*), Senators Bushby, Cameron, Furner, Joyce, Pratt and Xenophon

Participating members: Senators Abetz, Adams, Arbib, Barnett, Bernardi, Bilyk, Birmingham, Mark Bishop, Boswell, Boyce, Brandis, Bob Brown, Carol Brown, Cash, Colbeck, Jacinta Collins, Coonan, Cormann, Crossin, Ellison, Farrell, Feeney, Fielding, Fierravanti-Wells, Fifield, Fisher, Forshaw, Hanson-Young, Heffernan, Hogg, Humphries, Hutchins, Johnston, Kroger, Ludlam, Lundy, Ian Macdonald, Marshall, Mason, McEwen, McGauran, McLucas, Milne, Minchin, Moore, Nash, O'Brien, Parry, Payne, Polley, Ronaldson, Ryan, Scullion, Siewert, Stephens, Sterle, Troeth, Trood, Williams, Wortley and Xenophon

Senators in attendance: Senators Cameron, Eggleston, Furner, Hurley, Joyce, Milne and Pratt

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.

WITNESSES

GOODWIN, Mr Shane, Deputy Managing Director, Housing Industry Association Ltd..... 1

LAMONT, Mr Chris, Chief Executive, Policy, Housing Industry Association Ltd..... 1

SILBERBERG, Dr Ronald, Managing Director, Housing Industry Association Ltd..... 1

**SIMPSON, Mr Glenn Ives, Senior Executive Director, Legal Affairs and Corporate Services,
Housing Industry Association Ltd 1**

Committee met at 4.16 pm**GOODWIN, Mr Shane, Deputy Managing Director, Housing Industry Association Ltd****LAMONT, Mr Chris, Chief Executive, Policy, Housing Industry Association Ltd****SILBERBERG, Dr Ronald, Managing Director, Housing Industry Association Ltd****SIMPSON, Mr Glenn Ives, Senior Executive Director, Legal Affairs and Corporate Services, Housing Industry Association Ltd**

CHAIR (Senator Hurley)—I declare open this public hearing of the Senate Economics Committee. The committee is inquiring into home warranty insurance. I welcome everyone 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.

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 witness concerned before doing this. The Senate can also order publication of confidential evidence. Do you wish to give an opening statement, Dr Silberberg?

Dr Silberberg—I should like to, Chair, thank you. HIA has made two written submissions to the inquiry, which we will take as read. Certainly some people have shown a keen interest in what we have submitted. HIA has been involved in promoting insurance services to the housing industry for more than 20 years. One of the insurance products provided through HIA Insurance Services Pty Ltd, a company owned jointly by Aon Ltd and HIA Ltd, is home warranty.

In 2007, HIA's last completed financial year, the amount of income attributable to home warranty was an estimated \$2.35 million, representing 2.6 per cent of total consolidated revenue of \$88.5 million. The amount of income attributable to home warranty broking services distributed to HIA Ltd was about \$2.5 million in 2006 and \$2.7 million in 2005.

HIA Ltd is a not-for-profit association and does not pay dividends to members. All revenue raised by the association is under the control of HIA's board of directors and is utilised to provide services for members, of which there are more than 40,000 Australia-wide, including about 1,700 members who are active on HIA committees. For the sake of good order, it should be affirmed that no HIA staff person or HIA member has any shares in HIA Insurance Services Pty Ltd. While two staff of HIA are directors of HIA Insurance Services, neither receives any payment or benefit for being a director of that company.

Much of the turmoil surrounding home warranty emanated from the collapse of HIH and FAI in March 2001. HIA never promoted the purchase of home warranty insurance from either HIH or FAI on the advice of our then broker. When HIH collapsed many builders were left stranded. It was a particularly difficult time for a period of 18 months to two years, as builders who had

been with HIH moved from a non-rated environment to financial testing. Today about 70 per cent of builders are in the top-rated categories and enjoy lower warranty premiums as a result. One of the features of the Victorian and New South Wales schemes is that builders can qualify for lower premiums because of their track record, levels of capitalisation and organisational capacity.

In Victoria the all-inclusive warranty premium on a new house valued at \$300,000 ranges from \$380 to \$2,300. In New South Wales the all-inclusive warranty premium on a new house valued at \$300,000 ranges from \$450 to \$3,500. In Queensland all builders are charged the same premium, regardless of their capacities. On a new house valued at \$300,000 the premium is \$2,326 in Queensland.

HIA is not in favour of a monopoly situation in home warranty or any other sector. When HIH collapsed there was one underwriter left standing, Royal and Sun Alliance, now Vero. HIA recognised that such a situation was not tenable and worked with Aon Ltd to encourage additional suppliers of home warranty into the New South Wales and Victorian markets. Today home warranty is provided by Vero, QBE, CGU, Lumley and Calliden.

Home warranty premiums paid are higher in Queensland relative to New South Wales and Victoria moreover, whereas the average warranty premium paid in New South Wales and Victoria has declined by about 36 per cent in the past four years. In Queensland home warranty premiums have increased markedly by more than 45 per cent over the same period.

The main reasons home warranty premiums have declined in New South Wales and Victoria have been the force of competition keeping individual underwriters on their toes, and builders have improved their category rating to qualify for lower premiums. Whereas private underwriters pay company tax, the Queensland Building Services Authority is income tax exempt.

Every builder in Queensland is required by legislation to provide a personal guarantee so that, in the event of a building company failure, the Queensland Building Services Authority can pursue the personal assets of directors of the building company. In New South Wales and Victoria about two per cent of builders have to provide a personal guarantee or bank guarantee. It would be worthwhile asking underwriters how much lower premiums would be in Victoria and New South Wales if all builders had to provide a personal guarantee, as applies in Queensland. If builders in New South Wales and Victoria do not like the service from their underwriter or broker they have some choice. They can change their broker and/or underwriter. In Queensland there is no choice. HIA has prepared a table that summarises the Queensland and New South Wales home warranty schemes, which we would like to provide to the inquiry.

The level of consumer protection applying to new homes and major renovations should be consistent across Australia. In other words, regardless of where a consumer has a new home or major renovation undertaken, they should enjoy the same levels of consumer protection. There are differences in the statutory warranties between states, which emerged in the aftermath of the collapse of HIH.

Seven years on, it would be appropriate for the New South Wales and Victorian governments to consider amendments to the home warranty schemes. The principal enhancement to the New

South Wales and Victorian schemes should be a completion guarantee based on the original contract, instead of a capped proportion of the contract price. Should the builder fail while a house is under construction, the home owner should be able to terminate the contract and make an insurance claim for the house to be completed. Had this provision applied in New South Wales the delays that occurred following the collapse of Beechwood Homes could have been avoided.

Because home warranty involves a substantial and long-term financial commitment on the part of underwriters, it is essential that providers of home warranty should be subject to the capital adequacy tests required by the Australian Prudential Regulation Authority. Undercapitalised warranty providers should not be accredited to offer consumer insurance. Thank you, Chair.

CHAIR—Thank you, Dr Silberberg. We appreciate HIA coming in today. You have put in a substantial submission and responded to various submissions that have come in. But you would know, of course, that HIA has been mentioned in a number of submissions and in hearings, so it is a good opportunity for us to address the issues that have been raised and it is very important, in order for us to give a balanced report, that we do have these kinds of responses.

Senator MILNE—We have had a lot of evidence that suggests that last resort home warranty insurance does not provide adequate consumer protection. Can you name any organisation or any stakeholder group, apart from HIA and the Insurance Council, that supports current last resort arrangements and can you give us any references to their statements or documents to support that? Could you cite anyone at all?

Dr Silberberg—In Western Australia and South Australia, from the inception of their home warranty schemes, which dates back to about the 1980s, those schemes have been last resort warranty, and I am not aware of any consumer backlash in those states. I will ask my colleague Glenn Simpson to respond to your question.

Mr Simpson—I possibly should start by mentioning the working party of the Standing Committee of Officials of Consumer Affairs. In November 2002 they reported to all consumer affairs ministers in relation to home warranty insurance and they endorsed a scheme of last resort insurance, coupled with a scheme of improved dispute resolution. It is that report, in my submission, that state governments are continuing to act on. That is the latest official scrutiny of the scheme, if I can put it that way, and state governments have not seen fit to publicly consult, either through an inquiry or through the state and Commonwealth ministers for consumer affairs, in relation to this particular scheme. Your question related to private organisations—consumer organisations—as I understand it. I am not here to speak for any organisation this afternoon other than the Housing Industry Association.

Senator MILNE—No. It is just that we have been unable to find anybody else except HIA and the Insurance Council who thinks that last resort does provide adequate insurance cover. I wanted then, Mr Simpson, to particularly go to you. In the submission that HIA made to the inquiry in relation to corporate regulation 7.1.12(2), you said that HIA strongly lobbied in favour of APRA regulation, which would have, of course, kept the product as a retail product and not a wholesale product, and so the exemption from APRA et cetera. I have gone back to the submission that you cited in that. I understand it is the home warranty insurance and mutual fidelity fund submission, 17 July 2002.

Mr Simpson—Yes.

Senator MILNE—7.1.12 is not mentioned at all in that document.

Mr Simpson—7.1.12 was not something which was on our radar at the time. We thought it was appropriate for APRA to regulate it. We did not have our attention drawn to this particular regulation. Indeed, we were completely unaware that it had been altered until it was brought to our attention in relation to this inquiry.

Senator MILNE—In your document you say that you lobbied strongly in favour of APRA regulation, meeting with the then Treasurer, APRA and the Insurance Council of Australia on this point. You say that you are not aware why the submissions were rejected and this regulation made, but there is nothing, as I said, in your submission that even refers to wanting to keep APRA oversight in relation to this product. Can you cite for me any document at all? You say you went to the Treasury, APRA and the Insurance Council on this point. Could you table to the committee any document at all where you lobbied in favour of APRA regulation.

Mr Simpson—I was not with HIA at that time and I was not personally involved. That may be something we will need to take on notice.

Senator MILNE—Thank you. I would appreciate HIA taking that on notice and I would like anything in writing that suggested you wanted that. I take it from your response that you do not know why the government at that time decided to bring in this regulation to exempt you and, given your strong support of it, you would have no objection to the repeal of this regulation. Is that right?

Mr Simpson—I think we are on record to say that. Our submission at page 9 says that ‘based on the above, HIA considered the funds should be subject to full APRA scrutiny and compliance with the above reforms introduced under the General Insurance Reform Act.’ That was in relation to the ACT and Tasmania. That was on the basis that we understood that APRA would apply to all of these insurers and in relation to this business. So far as I am aware, from my own personal knowledge and through HIA documentation and discussing this matter with HIA staff, we were not aware of this regulation even having been made.

Senator MILNE—So did your 10-point plan—which coincidentally was implemented post the striking of this regulation—require this change for the regulation to be able to be implemented?

Mr Simpson—Absolutely not.

Senator MILNE—Thank you. I would appreciate getting any documentation showing your position on it at that time, where you lobbied any of those. I would like to now go to the Beechwood collapse. I wonder if you would comment on the comparison of the handling of the Beechwood collapse in New South Wales and the Real Property Constructions collapse in Queensland. We understand that in Queensland, after 87 days, 70 per cent of affected consumers had their houses completed or the deposits refunded. How many days is it now since the Beechwood collapse and what are the equivalent figures for Beechwood?

Mr Simpson—We do not have official figures. It is not a matter that we would have official figures on. In relation to the Beechwood matter, while it was a collapse, it was not a collapse that involved calling on the insurance. It was a case where the business of Beechwood Homes was sold. It is true that the New South Wales government's handling of this and the handling of this by insurers is something that they will have to answer for. We were not involved. We do not say that they did a good job or a bad job.

We note that it has taken some time to resolve the situation with Beechwood Homes, but that is because, in my opinion, the issue was: could it be sold as an ongoing concern? That would have had implications for subcontractors and other creditors, as well as for clients of Beechwood Homes.

Mr Goodwin—I think there are some lessons to be learnt from that episode, and hence the recommendation that Dr Silberberg put to the committee concerning a completion guarantee. Conceptually, that involves a change in approach. It would involve the insurer becoming responsible for managing the completion of the project rather than the consumer having to make a claim, organise builders and then recover compensation.

Fundamental to that proposal would be some legislation which would enable a consumer to terminate a contract in cases where the builder had become insolvent. That would enable the asset, the house, the contract, to be outside of the hands of the receiver and would enable the insurer to step in and finish that project in the quickest possible time. Also conceptually, it is inherent in that proposal that there would be no cap on the cost of completing that dwelling. The obligation would be on the insurer to mobilise other builders and contractors to finish the house under the contract which had been on foot with the insolvent builder.

Senator MILNE—I asked you to comment on how the situation with the Real Property Constructions collapse in Queensland was handled compared with Beechwood. Would you not agree that in the Queensland case consumers would be a lot happier than they are with the current state of Beechwood in New South Wales?

Mr Goodwin—I cannot speak concerning the Queensland matter. I am not familiar with the facts of that situation. But in relation to the Beechwood matter, if our proposal had been in place things would have been resolved, in my view, a whole lot quicker.

Dr Silberberg—Comparable with what happens in Queensland.

Mr Goodwin—Indeed.

Dr Silberberg—We have developed some proposals in respect of this issue, which we are happy to table to the inquiry, because I think it goes to the heart of how the New South Wales and Victorian schemes could be enhanced to provide the opportunity for consumers to expedite a claim in the event of insolvency or failure of a building company. In Queensland consumers can terminate the contract in the event of insolvency. In New South Wales and Victoria essentially they wait their turn whilst the administrator tries to recover as much margin as possible out of the contracts that have not been completed. We do not think that the situation in New South Wales and Victoria is satisfactory from a consumer protection point of view.

Mr Simpson—There is also an additional point to be made in relation to Queensland, and that is that the Queensland Building Services Authority knew 12 months in advance that Real Property Group was going to go into liquidation and during that period they managed down, to the best of their ability, their insurance liabilities. During that period a lot of people, a lot of consumers, contracted with that company because they had no knowledge of its financial situation. While there may be consumers who are happy with the outcome in Queensland, there are also consumers who have been put in a position of having a contract with Real Property Group on foot that they may not have entered into had they known what the Building Services Authority knew. So there are swings and roundabouts in these matters.

Senator MILNE—I understand that, but I am glad that you concede that in Victoria and New South Wales people do not have adequate consumer protection with the last resort insurance arrangements that are currently in place.

Mr Simpson—I think we said that in our submission.

Mr Goodwin—It is more a question of the way the insolvency law operates, that the contract and the house become an asset in the hands of the receiver. What we need to do is get it out of the hands of the receiver and then compel the insurer to come in and finish the house. To do that, you need a mechanism in the contract to enable the consumer to terminate the contract with that particular builder. That is the mechanism that exists in Queensland.

Dr Silberberg—Were those circumstances to be picked up in New South Wales and Victoria, the relevant underwriter would have a strong financial incentive to get on and have the houses completed, because the longer they sit out there in a state of being uncompleted the more the damage and deterioration that could occur. So in our view it is a fairly straightforward set of amendments to the New South Wales and Victorian statutory schemes that could put them on a compatible footing with the consumer protection provisions that apply in Queensland.

Senator MILNE—Further to the issue of Queensland, you say that ‘any form of first resort insurance will be expensive, potentially prohibitively so.’ Do you think that the Queensland rate of \$7.90 per \$1,000 of project value for first resort cover is prohibitively expensive? If so, why? And do you have any evidence that Queensland consumers are dissatisfied with this cost?

Dr Silberberg—The average premium on a typical new house in Queensland is more than double the average premium for a comparable house in Victoria and 77 per cent more expensive than a comparable house in New South Wales. In view of the fact that your terms of reference involve considerations of housing affordability, could I respectfully suggest that that is an important issue.

Senator MILNE—Isn’t the difference here that they are offering first resort? We are talking about the first resort.

Dr Silberberg—No, I do not think the Queensland scheme is necessarily first resort. I think it is second resort. The Queensland Building Services Authority, as the licensing agent and essentially insurer, can place builders in a situation where, in the event of a consumer complaint, the Queensland Building Services Authority can effectively coerce builders to rectify, failing which a builder’s licence could be in jeopardy. That is potentially a very big stick. There is too

much reliance, in our view, in the QBSA scheme on the quality of management of that agency and there is the possibility of a lack of transparency in the way in which disputes and claims are dealt with.

Interestingly enough, back in 1993 Commissioner Dodds did a review of the then New South Wales Building Services Commission, which was a scheme similar to that which applies in Queensland, and recommended firmly against the licensing authority also being the insurer because of a potential for conflict of interest and the possibility of moral hazard. There was no shortage of complaints from our builder members about the capricious behaviour of the then Building Services Commission in New South Wales and similarly with the Housing Guarantee Fund Ltd in Victoria.

Arguably, the presence of private sector arrangements in New South Wales and Victoria provide a sort of brake on excess power being exercised by the Queensland Building Services Authority. The authority in Queensland is empowered significantly by legislation. That the QBSA does not necessarily operate today in the manner that it did some years ago arguably reflects their awareness of the political pressures from having private sector arrangements in New South Wales and Victoria.

Senator MILNE—It is interesting that you should talk about builder members being dissatisfied, because we have had, almost in the hundreds, submissions from builders dissatisfied with the current last resort arrangements.

Dr Silberberg—Can I respond to that? We survey our members regularly and we have in excess of 40,000. We ask them what are the issues that occupy their minds, that keep them awake at night. Home warranty has dropped off the radar. For many builders it is a past issue. You might recall I mentioned that today 70 per cent of residential builders in New South Wales and Victoria are in the top-rated categories, so they enjoy the lowest premiums. Go back to 2001 when HIH collapsed: less than 10 per cent of builders were in the top categories as rated by Royal and Sun Alliance at that time, so there has been a significant shift by the industry.

It has not always been comfortable, and back in the nineties and prior to the collapse of HIH there was one underwriter that was truly underwriting builders, and that was Royal and Sun Alliance. HIH and FAI did not exert any underwriting standards. They underpriced the product, and for five years we were told that HIH and FAI would collapse. That is why we did not promote our members to purchase the warranty product from HIH and FAI. A lot of builders at that time were not as well capitalised as they are today. Royal and Sun Alliance, now Vero, and other underwriters do underwrite builders and they have a premium rating structure that reflects the different organisational capacities and levels of capitalisation of those builders.

I would argue that it is in the interests of consumers that we have better rated builders. It has meant that long-term capital has come into building companies. You used to hear that the building industry was chronically undercapitalised. Today that situation is quite different because builders typically have to have a real stake in their building company in order to get a worthwhile rating from the private underwriters. That is helpful to consumer protection.

Senator MILNE—Can I go back to the line of questioning that I was pursuing here. There was one question in relation to the bank guarantees which I will come to in a minute, but first

back to Queensland. I was asking you about any dissatisfaction with the cost in Queensland, because there has not been any as far as we are concerned, so I wonder if you could name any stakeholder groups or references to statements from stakeholder groups suggesting there is any dissatisfaction with the Queensland model. Also, you said in your submission to the Productivity Commission that it is not true that the Queensland model of state run home building warranty insurance is generally seen to be working well. So could you name for me any other organisations or stakeholder groups in Queensland who you can cite as having said it is not working well.

Dr Silberberg—I cannot cite any other organisations in Queensland that are saying that it is not working well. I can say that our Queensland builder members overwhelmingly have told us through surveys that they would prefer to have a rating system wherein better quality builders would enjoy lower premiums. In Queensland you have no choice, so if you are dissatisfied you cannot vote with your feet. You cannot go to an alternative provider of insurance; you have to cop it. I do have builder members in Queensland who are complaining about the current level of premiums as being too high.

Senator MILNE—So when you made your statement to the Productivity Commission that it is not true that the Queensland model is generally seen to be working well, you have no evidence for that except, you are telling me, the survey from your members?

Dr Silberberg—I cannot recall the Productivity Commission submission, to be honest.

Senator MILNE—It was your submission to the Productivity Commission. That is all. Several of the builders have complained to us that they cannot get bank guarantees cancelled, even after the possibility that there will be any related liability has ended and that this prevents them from shopping around for different insurers. Is it true that this situation arises? If it is, can you tell us why that is so?

Dr Silberberg—We were advised by HIA Insurance Services that about two per cent of builders in New South Wales and Victoria require bank guarantees or personal guarantees. So 98 per cent do not. Do you find it interesting that in Queensland, by legislation, by statute, every builder has to provide a personal guarantee? It would be interesting to ask Mr Ian Jennings, the General Manager of the Queensland Building Services Authority, if he advises builders in Queensland that their personal assets would be on the line in the event of a building company failing and having a deficiency of funds in that company.

Senator MILNE—Dr Silberberg, you are here to answer our questions. I was asking you particularly in relation to this issue—

Dr Silberberg—I responded.

Senator MILNE—of the bank guarantee standing after any related liability is over, because we are being told that people are being forced into illegally building or out of the industry because of this issue of bank guarantees. What I would like to know—and you did not answer that in your response to me—is if it is true that some builders have been unable to get their bank guarantees cancelled after the possibility that there will be any related liability has ended? Can

you tell me why this is so, with logic suggesting that a guarantee should be valid only as long as there might be a claim under a related insurance policy. So is it so? If so, how do you justify it?

Dr Silberberg—I am not trying to justify it.

Senator MILNE—Is it so?

Dr Silberberg—I do not agree with it.

Senator MILNE—Is it true that there are builders who cannot get their money back?

Dr Silberberg—We have, through our broker, made efforts to have guarantees extinguished. We do not condone the practice of holding guarantees after the liability has extinguished, but we are not the underwriter. Our broking arm is there as a supplicant for its customers and where its customers want assistance in lobbying underwriters to have the guarantees removed HIA Insurance Services has fulfilled that service. But I cannot tell you what the incidence is in respect of guarantees still on foot where the liability has expired. I do not know.

Senator MILNE—You mentioned your member surveys and I am interested in the membership of HIA, because I understand that you are a private company.

Dr Silberberg—No, we are a public company.

Senator MILNE—A public company. Do all your members have equal voting rights? Are they able to vote on policy? What is the status of your members?

Mr Simpson—Because HIA is a member-driven organisation and it has 44,000 members all around Australia, it is in a little different position to a public company that has shareholders and a shareholders meeting once a year. We do not operate on that basis. We have a collegiate electoral system, which is set out in our articles of association.

There are elections for elected officials in every HIA region annually. There is a regional executive in every HIA region, with regional committees supporting that executive. There is the National Policy Congress which formally meets annually, which consists of representatives from all of those regions. They are the final arbiters on HIA policy.

So a typical policy would start at a grassroots level, it would be endorsed by local members, local committees, endorsed by the regional executive, considered by National Policy Congress and adopted. All of these people are HIA members or volunteers. None of them are HIA officials. Typically, there are 20 or 30 policy items on our National Policy Congress agenda every year. That includes policies on home warranty insurance, and NPC has considered that on a number of occasions and has voted on it. The matters in relation to home warranty insurance necessarily have been widely debated within HIA.

Senator MILNE—I have been told—and you can confirm whether it is true or not—that members of HIA tried to call a meeting to discuss home warranty under section 249D of the Corporations Act, with the required number to have a meeting, and they were told that they were

not voting members of the organisation. Is that true or not? Who in the organisation has no power out of these 44,000 members?

Mr Goodwin—That is not correct. A petition was presented at the time of 88 people, if my memory serves me correctly, or thereabouts, of which the minority were members. Each of those members was contacted and the majority of those members who had signed that petition did not know what the petition was about. The national president of the day either rang or spoke to each of the people who signed the petition. So he either spoke to them or wrote to them and explained the situation, explained what HIA's policy was and how it came about. That is a matter of record.

Senator MILNE—But were they told that they were not voting members?

Mr Goodwin—They are voting members. Because of our collegiate system, every member has a vote in their particular region.

Senator MILNE—So no members were told they had no voting rights?

Mr Goodwin—I cannot recall what was on the correspondence. I would need to refresh my memory. But members do have voting rights. I do not agree that they do not have voting rights.

Senator MILNE—On what basis do you say that people did not know what they were doing when they signed a petition?

Mr Goodwin—Because when they were asked, they said, 'We were just asked to sign a petition.' They did not realise what the petition was calling for.

Senator MILNE—That is a pretty sad reflection. If you are suggesting that people presented with a petition do not read what it is about and then get a phone call from the organisation offering to educate them on what the organisation thinks, doesn't that smack of standover tactics?

Mr Goodwin—Not at all. A great number of the people who signed the petition were not members. Those contacted said, 'Well, we've had difficulty with insurance,' or words to that effect. 'We didn't realise what we were signing, what we were asking for.' The petition was calling for a number of things and it was explained to them what they were. 'Well, that's not what we thought we were signing on for.' In any event, there was not the requisite number of members to call a meeting. Notwithstanding that, in any event the issues which were raised in the petition did get discussed at National Policy Congress in due course.

Senator MILNE—Thank you.

CHAIR—Senator Eggleston, do you have any questions before you go?

Senator EGGLESTON—I have a series of questions about builders' complaints but I have to go quite soon. So perhaps I should leave them to somebody else to ask.

CHAIR—Okay. In that case I will ask some questions about builders. We have had evidence that some builders have complaints about the system. HIA, of course, represents builders and

one of your areas of revenue—and you have said that it is a very small part of your revenue and I accept that—is that the insurance company may be engaged in disputes with builders. We have heard evidence that some builders therefore think that the HIA does not represent them properly. What is your response to the fact that you may have some conflict of interest there and that you are getting revenue from the insurance arm representing builders?

Dr Silberberg—HIA has a half-equity in HIA Insurance Services Pty Ltd. It is truly an insurance broking operation. It is not an agent of the underwriter. So its responsibility is to try and find the best product on the best possible terms for its clients, who are builders. On lots of occasions HIA Insurance Services staff are involved in discussions and negotiations with underwriters in order to try and achieve the best possible terms and conditions for their customers.

I am bemused by the observation that HIA has some conflict of interest which prejudices its objectivity in looking at this or any other matter. Our National Policy Congress took a decision to support voluntary home warranty. If we were solely guided by some sort of financial motive, why would HIA support a policy of voluntary home warranty in the states outside of Queensland?

We took that proposal to the New South Wales, Victorian and Tasmanian governments, and the Tasmanian government did adopt a form of that. The New South Wales and Victorian governments were not interested. We also were quizzed by underwriters as to why we would possibly be advocating a voluntary home warranty scheme, and we thought it was appropriate to do so where consumers would benefit from a public education and awareness program about their rights and entitlements under the home warranty schemes and could make an informed judgement about whether they wanted the home warranty or otherwise and were prepared to carry the cost for that. That is my response.

CHAIR—It was a bit of a diversion, but I think this is a critical issue about education of consumers. I think we heard some evidence that, because people think that nothing is going to go wrong with their home building in the beginning, they are unlikely to choose to take out insurance. So I can understand why the New South Wales and Victorian governments may not want to go to voluntary home warranty insurance, because if something does happen to the builder, then they are in great difficulties.

Dr Silberberg—That did not seem to deter the Tasmanian government from adopting that scheme.

CHAIR—We will see how that develops. I understand that the Tasmanian government are looking at other options.

Dr Silberberg—Fair enough.

CHAIR—Do you have any ideas about how people might be better educated or better informed about the kind of insurance it is? One suggestion is, of course, a name change for the insurance, to take away any suggestion of a warranty. We had evidence that some brokers and/or some insurance companies automatically send a copy of the policy to the home builder, as well as to the insured, who is the builder.

Dr Silberberg—That is right.

CHAIR—Could you comment on those aspects?

Mr Lamont—Firstly, I think that the name probably is not appropriate. If changes are made in the sense that Dr Silberberg is suggesting, with completion guarantees, then a name change that reflects something of that description would appear to be appropriate. In respect of consumer education, I think it goes hand in hand that, firstly, a greater awareness of the need for appropriate building contracts should be established up-front. Mr Goodwin referred to sections and amendments to contracts that could assist consumers in terms of their rights in respect of a builder who may go into insolvency or become bankrupt and their options in that particular respect.

I think a consumer education campaign that advises of their particular protection cover under whatever warranty scheme we are talking about would be of assistance. Secondly, I think the contractual aspects of home building would also benefit from further explanation for consumers. It is the practice of some underwriters to provide copies of the premium and the insurance cover to both the consumer and the home builder, but I do not believe it is all underwriters who provide that service.

CHAIR—That seems to be one of the bases of the problem. The person who takes out the insurance is the builder.

Dr Silberberg—That is right.

CHAIR—And the person who contracts the builder might not necessarily know what that policy holds. Whether or not they actually go into it and are aware, at least they should be given the opportunity to be aware of what is signed more or less on their behalf by the builder.

Dr Silberberg—That is right, because the underwriters are essentially providing a financial guarantee. They are not underwriting the consumer; they are underwriting the builder. In those circumstances, I do not think underwriters would respond favourably to underwriting consumers direct, so they have to evaluate the capacities of the builder over which they are providing a financial guarantee. I was under the impression that the consumer is the insured. The builder signs on, but the certificate will be in the name of the householder.

Mr Goodwin—I think if we moved to a completion guarantee, we fundamentally change the whole equation. The insurer is compelled to step into the shoes of the builder. The insurer has a real interest then up-front in educating the consumer, the ultimate beneficiary of the policy.

Dr Silberberg—Perhaps one of the reasons the New South Wales and Victorian schemes have been mandatory is that there might be a view that consumers go into the new housing market maybe once in their lifetime and, in order to gather information about the reliability or otherwise of builders, the search costs would be impossibly high. If we mandate, then you have some sort of level playing field in terms of consumer protection.

Under the proposal we advocate, there would be a requirement for the public sector, as well as the private, to shoulder responsibility, to ensure that consumers were aware of their rights, entitlements and obligations in respect of home buying.

CHAIR—In terms of the consumer terminating the contract, that would require changes to the law around receivership, would it not? It would be complex.

Mr Goodwin—It could be done in the home building acts, implying a term into every home building contract that, if it is not written in the contract, it is implied that a consumer could terminate in the event that a builder became insolvent, in which case the right to complete the contract is not an asset in the hands of the receiver. It is a fairly simple legislative amendment, in our view.

CHAIR—I'll take your word for it! In terms of terminating contracts, there is insolvency of the builder and there is death of the builder, which is more clear-cut, but then there is also the suggestion, which I think the HIA has also made, of the licence being cancelled if a builder has been found to be not completing the work. You cover that in your submission, and that does seem like a reasonable way to go, but you mention also—I think it was your submission—that the builder should have some rights of appeal against that licence suspension. In view of some of the evidence we have heard, the committee would be concerned about how long that appeal would go on and what involvement the consumer would have. Do you have any ideas about how that might work?

Mr Simpson—The delicensing of a builder is a severe step, because you are taking away an occupational licence and a person's livelihood. It is not something that builders will willingly allow to happen. As a trigger for an insurance policy, it has the desirable feature that it is definite and it is legal. We would have thought that providing such a trigger would, in effect, have some influence on the willingness of builders to complete. Where the builder is in fact simply unwilling to complete, then the loss of licence would be appropriate, because they are in breach of an order by a tribunal to do the work. If they have breached an order and they have been delicensed, it is an appropriate trigger for the insurer then to step in. Insurers are not in the business of settling disputes. Insurers need some sort of hard and fast event that can be identified as the trigger for the insurance policy.

So far as taking someone's livelihood away by way of appeals, it is something that may involve some delay, but it is equally something whereby the builder needs to have their rights preserved, because the dispute may be over workmanship issues whereby the builder is in fact in a reasonable position to say, 'The workmanship was as per the contract.' The client may disagree, but where the insurer is being called in to do the rectification work, it needs to be properly identified.

It is one of those areas where you simply cannot get away from the need to have a proper inquiry. In our view, they would be few and far between. In most cases where a builder is unable or unwilling to rectify, it is appropriate for the insurer to come in and do it through the completion guarantee. The reason they are unwilling or unable to rectify is because their business is going down the tube and the loss of licence is only one of the things that are falling in on them at the time.

CHAIR—If the trigger were that there were some sort of tribunal or court order—

Mr Simpson—It would be an order from the licensing authority, and there are mechanisms that already exist for that, including appeal mechanisms.

CHAIR—So you would be beyond the appeal stage, because that tribunal or court would have already gone through that stage.

Mr Simpson—Yes.

CHAIR—So that is the stage at which the insurer could come in.

Mr Simpson—Improved dispute-settling procedures would mean that, where there has been—I will not call it a quick and dirty investigation—a simple, cheap, quick investigation, where there is an order for the builder to do work and the builder fails, then the next logical step would be to suspend that builder's licence, because they are clearly in breach of their obligations under the licensing scheme, which is to comply with the disciplines in that scheme.

CHAIR—You are looking at the licence trigger; you are looking at a completion guarantee rather than a particular monetary cap.

Mr Simpson—Yes.

Mr Goodwin—Rather than compensation, because then the consumer has to go out and find a builder and get prices and satisfy the insurer. What we are saying is: compel the insurer to step into the shoes of the failed builder and finish it. It becomes the insurer's problem to find a builder. You find that with storm damage they have a stable, a panel, of builders all ready. They would have a panel of builders to finish off this work. That would take a lot of the delay out of the whole process.

CHAIR—Then a general education program around exactly what people are insured for if the insurance is compulsory?

Mr Goodwin—Know your rights and know what your cover is.

CHAIR—What about the building contract? As I understand it, the HIA, the MBA, various people have standard building contracts. What does that look like across Australia? Are there different contracts for each of those groups in different states? How does that all work?

Mr Simpson—Every state has its own home building legislation. HIA for many years has been lobbying states in an attempt to align them so that we can produce a single contract that would be acceptable to all the states. Sadly, this has not been possible. Every state has its own idea of what is invented here and what is not invented here. HIA produces separate contracts for new home buildings in every state. Each contract is different and each contract has to reflect changes as they occur to legislation in those states. They say that master builders associations all do the same thing. They are state based organisations. The architects, the Royal Australian Institute of Architects, do the same thing. In some states the consumer protection agency has its

own model contract. There are major advantages for consumers and builders in having industry standard contracts. That has been widely recognised.

CHAIR—For a complete layman, what would an industry standard contract look like? Obviously in somewhere like the Territory where you have different building requirements because of cyclones and so on, you would have different—

Mr Simpson—The contracts look different because the legislation requires them to include different warnings. There are different legislative schemes for at what stage progress payments can be taken and different percentages. There are different opt-out provisions. In some states you have to have a legal practitioner assign a certificate saying what are the consequences of not adopting the schedule of progress payments. You need to understand this, so you have to have legal advice before you can opt out of the mandated legislative scheme. There are a lot of differences.

In terms of actually building things, that comes in the plans and specifications which are annexed to the contract. They generally speaking follow the Building Code of Australia and there is a lot of similarity. So the legal mechanisms that the contract needs to contain and the statements that it has to have in it do vary.

Mr Goodwin—Even so, the processes inherent in the contract reflect the building process: you have to get the plans ready, then you have various stages throughout the job where you can claim a payment. It is a milestone and you get paid. There are mechanisms if you want to change something, if there is inclement weather or delays in products: you can extend the time for completion and you can reduce or increase the price. Those things are fundamentally the same wherever you go. It is the legislative changes to some of those processes which Glenn has—

Mr Simpson—The differences that have no practical purpose, that are just differences for no obvious reason, are of concern to us. Where there is a genuine reason for a state based difference, possibly because of builder licensing, we could understand and accommodate that. But sometimes one state requires a wording in this form and another state requires a wording in that form but they are both trying to convey the same information to consumers. That is the problem.

CHAIR—Yes.

Mr Simpson—I hasten to add that every state consumer affairs agency is in active dialogue with HIA about its contracts. The contracts are produced by member committees. The states offer suggestions. They put pressure on us to change aspects of the contract. We try to produce balanced documents and, generally speaking, we believe we have been successful in doing that because we sell a lot of contracts. Our builders use them and they understand them. We run courses on contract administration, as does the Master Builders Association. People know how the contracts operate. As Shane said, the principles are much the same from state to state, but you have to be careful that you have ticked all the boxes and crossed all the crosses that need to be done, otherwise you will not get paid if you are a builder. The usual consequence of failure to comply with the act is that you cannot get paid, so the minutiae of contract differences are extremely important to our members.

CHAIR—I will give you an example of my experience with home warranty insurance. We signed the building contract and found that there was not, in fact, last resort home warranty insurance because the council, which was the person that had to ensure that it was in place, was not finally notified by the builder that the building had taken place. Is that, for example, different interstate? I was told by the South Australian consumer organisation that in Victoria that would have been a different, stricter requirement.

Mr Simpson—It is different from state to state. In my understanding, New South Wales is the only state that does not have it as a legislative obligation that the builder take out a policy of home warranty insurance before applying for a building permit.

Mr Goodwin—But I think you cannot get your plans released until you produce to the council evidence of the insurance.

Mr Lamont—It is a discretion of council.

CHAIR—That is where it fell down.

Dr Silberberg—But it should not be a discretion of the council is the point we would make. It should be mandated in state legislation so that it is not at the discretion of the local government authority to require sighting of a relevant warranty policy as a condition precedent to approving a building application. It ought to be mandated.

CHAIR—That is the kind of thing you are talking about, where you would like similar contracts across the states. Or are you content to have separate states but with the same—

Mr Simpson—It is a bit like company law. When every state had its own Companies Act it was an absolute pig's breakfast if you were a company secretary. What you want is something that is a model act that all states will sign onto. We have been pushing for that for years.

CHAIR—That would include, since we are doing home warranty insurance, the conditions around that last resort insurance.

Mr Simpson—Absolutely. It is not even in legislation in Victoria. It is a ministerial order. In New South Wales, substantives of the policy are actually in the legislation. Let's not start on how you get uniform legislation. It is a can of worms.

CHAIR—No, let's not. I think Senator Cameron has some questions.

Senator CAMERON—Dr Silberberg, the more I listen to this, the more confused I think consumers must be in terms of this 'product', in inverted commas. I am looking at your submission here and I note that you say:

The appropriate way to define 'defect' is through a standard guide of tolerances. This guide would prevent the expert arbitrator from substituting their own view of workmanship standards for the acceptable standard.

I have never come across a set of tolerances as a guide for a quality outcome. As you would be aware, we have various standards in Australia that give you quality assurance. Why would you

talk about a guide of tolerances and not a quality assurance? Tolerances are part of standards. Tolerances are not standards. Tolerances go to make up standards.

Mr Simpson—Can I answer that?

Senator CAMERON—I am totally confused with this and, if this is your answer to where we are going, I think people are going to be even more confused.

Mr Simpson—This is a bit off the topic, so we have not brought one here today for you to look at—if we had known, we would have—but we are publishing a beautiful standards and tolerances guide for our members' use. Other people have done so. The Victoria government uses one. Basically it is a guide for people assessing the question of, 'What is a defect?' Is a wall which is one millimetre out of true and two metres high a defect? If it is not, is a wall five millimetres out of true a defect? What we have attempted to do, on a voluntary basis, is produce a document which will allow people who are assessing these things to say, 'Yes, that's a defect and it ought to be rectified by the builder,' or, 'No, that's within the normal tolerances of workmanship and has been completed in accordance with industry standards.'

It contains mind-numbing stuff about how many cracks you can have in lapped boards, what is a defect in relation to glazed windows and certain sorts of paint and where the light source is to be positioned when judging whether it is defective. It is the sort of stuff that appeals to the technical people. We are attempting to have this out there in the marketplace for use by an arbitrator or a person who is required to decide whether workmanship is or is not defective. They can look at Australian standards, they can look at the Building Code of Australia, they can look at documents put out by industry groups such as cement manufacturers, glazing companies and window associations. They can look at all these documents. We have tried to bring as much of that as possible together in one document, which people can choose to use if they wish or choose not to use, but it is a way of informing opinions to assist in making decisions about what is a defect.

Senator CAMERON—It is a self-regulation type approach, is it?

Mr Simpson—Not even self-regulation. It is more an assistance. It is a tool that people can use where the consumer says, 'That wall is out of true. It is a defect,' and the builder says, 'No, it isn't.' You go to the guide. You run your tape over the wall and if it is in fact beyond the tolerances in the guide, the builder will have to do some explaining as to why. There may be perfectly good reasons for it but prima facie, if it is beyond the tolerances in the guide, it is a defect.

Senator CAMERON—Is there anywhere in Australia a legal requirement which cannot be contracted out of to build within standards?

Mr Goodwin—Where these acceptable standards of construction go, they will be called up in regulation in the next little while.

Mr Simpson—The Building Code of Australia calls up Australian standards, but those Australian standards typically lack some of the fine detail. Other Australian standards exist that are not called up in the Building Code of Australia, so you get arguments before building

tribunals as to whether the standard should be used to judge, and who was on the standards committee and whether they took into account industry practice. You get a lot of argument.

Senator CAMERON—I am an engineer by trade, a fitter by trade.

Mr Simpson—You understand tolerances.

Senator CAMERON—I have always worked on the basis that a consumer is entitled to a product not only within tolerance but that quality is an issue. It is not just tolerance. You can go within tolerance. Everything can be manufactured within tolerance, but the way it is put together can mean it is not an acceptable product. It seems to me that the building industry does not have the management tools in place to provide consumers with a reasonable outcome. And if we are depending on the HIA pulling together these tolerances, then surely we need some national legislation to enforce quality standards for consumers? It should not be left to the HIA to determine this on its own. Wouldn't you agree that consumers require something better than this?

Mr Simpson—We do have something better than this. We have the Building Code of Australia. The issue is not whether something is built or not built in accordance with the Building Code of Australia, but if I have a cement driveway poured in my home and it starts to crack, how big does the crack have to be before it is a defect? That is the sort of thing that the standards and tolerances guide is intended to give guidance to. It is not mandatory. It gives guidance. That is all.

Senator CAMERON—Let me tell you my experience. I bought a home and the home was three years old and it had a veranda on the back. The home was built on a sloping block where fill had been pushed back. After three years, the whole veranda was out of kilter, completely buckling. I made some inquiries about what I could do with this because I was told, 'Yes, it's still covered by warranty.' But I was basically told, 'Don't waste your time. It's probably cheaper to knock it down and rebuild it yourself.' What I found, when we did knock it down and rebuild it, was that the footings were in the fill and had not gone down into solid base. This is the type of thing that I think brings the industry into disrepute.

Mr Simpson—With respect, I could not agree more. Can I say that there is a local council inspection process that has failed in your case.

Senator CAMERON—I was told it was self-inspection by the builder in New South Wales.

Mr Simpson—That is not quite true.

Senator CAMERON—I am not here to run my argument on this. I am just saying to you that this is another example of how people can get really offside with the industry and it is an issue for the industry. That is why we are in so much trouble, I think, with this. You say it is not appropriate or desirable for insurers to resolve disputes between builders and consumers. You are part of the building industry. You represent builders. I have been involved in disputes over many years in many areas where insurers move in and make a decision. They make a decision because it is in their commercial interest and their legal obligation to make a decision. Why is it different in this industry?

Mr Simpson—Because what you are insuring is the quality of work. It is not the same as motor vehicle insurance, where you either have an accident or you do not. It is not the same as home contents and fabric insurance where, if you have a fire, there is no doubt that the house has burnt down. The insurers come in in relation to loss adjusting. They decide how much you have lost. But in the home warranty insurance area, the issue is not how much it is going to cost to fix up that defect: the issue is, is it a defect?

Senator CAMERON—It seems to me that this whole last resort approach has been spawned by market failure—a market failure and a business failure within this country by basically HIH—and that has left us with this type of approach which does not make a lot of sense in terms of consumers knowing what they are getting. It is confusing; the name is completely wrong. Do you agree that we should change the name?

Mr Simpson—Very few things could not be improved by changing their name, but I do not know that that is the whole answer. Certainly it is an important part of any answer. ‘Completion guarantee’ means a lot more to me as a consumer than ‘warranty insurance’.

Dr Silberberg—We get back to the point that consumers and the industry should be made aware of what the product attributes are and what they do not provide. There is a lot of confusion around that issue.

Senator FURNER—I was interested in the comments that you provided to Senator Cameron in respect to the tolerance guide. How was that compiled? Was it something that was decided on previous practices or surveys?

Mr Simpson—It has been a very painful process, quite frankly. We had an internal committee; we had staff; we have had drafts circulated. We took material from all of the other industry organisations that we could find, with their permission. We looked at standards. There was a lot of debate internally among our technical people. At the end of the day, we had a stab at it.

Dr Silberberg—How long was it in gestation: about 18 months?

Mr Simpson—About 18 months.

Senator FURNER—Did you involve consumers in the production or the arbitration of your findings on the tolerance guide?

Mr Simpson—It may be that at an earlier stage than the stage at which I saw it, to run my legal eye over it, there were such consultations. But, by and large, it is our members—

Senator FURNER—Is that yes or no?

Mr Simpson—I cannot say, but certainly not to my knowledge.

Dr Silberberg—Nor to my knowledge. The standards and tolerances guide was generated predominantly with the contribution of practising builders and professional staff in HIA who have a technical construction background.

Senator FURNER—This is not necessarily a question but a comment. We have heard today that QBSA has a lack of transparency on how matters are fixed. The Queensland building members overwhelmingly want a different rating for premiums. I, like other senators—and I am sure Senator Joyce would be in the same boat—have had homes built; in fact, I have had three homes built in my short life span of ownership. I have never had experiences other than outcomes of satisfaction with getting things fixed, and certainly a number of people that I know in the building industry, including builders, have indicated that overwhelmingly the QBSA is a reasonable product when it comes to insuring both builders and consumers.

Dr Silberberg—I am not going to take issue with that. Could I say that the Victorian Building Commission, which is the relevant regulatory authority for the industry in Victoria, undertakes post-completion surveys of householders, and well in excess of 90 per cent of those consumers were very happy or satisfied with their builder and the job that was undertaken.

Senator CAMERON—What is ‘well in excess of 90’? If 10 per cent are dissatisfied, I would think that is a big problem.

Dr Silberberg—It was in the order of a 95, 96 per cent satisfaction level, so the Victorian Building Commission was not displeased with that outcome.

Mr Simpson—Could I say that, to the extent that our members in Queensland are critical of the QBSA, we tend to represent the better—if I may say so—builders who have a perpetual concern with the standard flat rate for all builders; half of the builders are paying too much and half of the builders are paying too little. Our members tend to feel that they are in the group that are paying too much and, if they were the subject of a rating scheme, they could significantly reduce their premiums and be more competitive, so you would expect them to say that.

CHAIR—That will conclude the hearing today. Thank you once again for coming in. If there are any pressing questions that we need to ask, would we be able to write and follow up on that?

Dr Silberberg—Yes, no problem.

Mr Simpson—We will send you a copy of the standards and tolerances guide.

CHAIR—I personally have no hankering to see it.

Mr Simpson—It has nice photos!

CHAIR—But I think you did mention tabling—

Dr Silberberg—I have a ready reckoner in respect to the Queensland and New South Wales schemes, and a copy of some proposals that we provided to the New South Wales government in respect to the operation of their warranty scheme. Those recommendations in relation to New South Wales are applicable equally to Victoria.

CHAIR—Thank you all for your appearance before the committee today.

Committee adjourned at 5.32 pm
