SUBMISSION

Independent Pricing & Regulatory Tribunal

New South Wales

Review of the efficiency and effectiveness of the

NSW HOME BUILDING

COMPENSATION FUND

May 2020

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Foreword

The SecureBuild model for providing sustainable and affordable home building compensation was developed as a result of collaboration of builders with many years' experience in the building industry; people who had run home building compensations schemes in New South Wales and Queensland; and the former NSW Home Building Compensation Scheme Actuary.

SecureBuild Australia Holdings Ltd (SecureBuild) was the only company to lodge an application to the NSW State Insurance Regulatory Authority (SIRA) for a licence to provide home building compensation products as an alternative indemnity provider as provided for within *Part 6B of the Home Building Act 1989*.

In the amendments to the *Home Building Act 1989* made in June 2017, the NSW Government made provision for non-insurance underwriters, referred to as *Alternative Indemnity Providers* (AIP's) to enter the home building compensation market in New South Wales to provide innovative home building compensation products.

As outlined in the second reading speech (see **Attachment 1**) in relation to the Amendment Bill, the Government intended that AIP's would not be subject to regulation by the Australia Prudential Regulatory Authority (APRA), but rather SIRA would regulate AIP's in a manner similar to that of APRA.

Despite the creation of Part 6B of the *Home Building Act 1989,* APRA subsequently formed the view that only insurance underwriters should be allowed to provide home building compensation in New South Wales. One of the key reasons for APRA taking this position was that there was no safety net for consumers in place as SIRA indicated that it was not willing to establish the Home Building Guarantee Fund (HBGF) as provided for by section 103OA of the *Home Building Act 1989.*

Given APRA's position, SecureBuild made a request to the NSW Government that it write to the Federal Treasurer seeking an amendment to Schedule 2 of the Commonwealth *Insurance Regulations 2002*, which would have allowed AIP's to enter the home building compensation market in NSW as the NSW Government has originally intended.

As the NSW Government did not seek an amendment to the *Insurance Regulations 2002*, SecureBuild was left with no alternative but to seek an exemption from the *Insurance Act 1973.* On 21 December 2018, APRA advised that it was not willing to provide an exemption to any AIP for the reasons outlined above. A copy of the correspondence from APRA as enclosed at **Attachment 2**.

Following APRA's refusal to provide SecureBuild (or any other alternative indemnity provider) an exemption from the *Insurance Act 1973*, the company had no other alternative but to withdraw its application for a licence.

The home building compensation scheme and its predecessor, home warranty insurance, has had a vexed and chequered history with many State and Commonwealth Government inquiries into tis effectiveness.

The reality has been that each inquiry has failed to understand the micro-economic factors that lead to poor building and home building compensation outcomes. The movement to a 'last resort' provision of home building compensation in 2003 has unfortunately led to insurance underwriters and iCare solely focusing on builder financials at the expense of focusing on the more critical micro-economic factors that are involved.

The simple fact is, if a builder cannot accept building progress payment in advance of the work that they complete; and that associated work is completed defect free then a home owner will never suffer a loss that would give rise to a claim under the scheme.

Despite this, iCare continues to focus on expending considerable resources on attempting to determine a builder's financial situation, which could change with days, if not hours after an assessment is made.

Given the adverse claims history in NSW, private underwriters will not return to the home building compensation market until positive claims ratios have been achieve for several years. An actuarial analysis of the scheme loss ratios is enclosed at **Attachment 3.**

When the NSW Government agreed to recommence underwriting home building compensation in 2010, this occurred following a period of intense competition amongst private underwriters for market share from the market leader Vero. The intense competition drove premium price down to unsustainable levels.

As the low unsustainable premium prices were not increased until 2017-18, the loss ratios of the scheme deteriorated significantly. The failure to keep premium prices ahead of claims costs together with a failure to reduce the risk profile of the industry has ensured that underwriters will not return to this market.

The NSW experience is somewhat unique as many other States and jurisdictions around the world do have very sustainable home building compensation schemes. For this very reason, SecureBuild developed it product offering by incorporating the effective risk mitigation measures employed by other jurisdictions (See **Attachment 4**).

The building and construction industry has change substantially over the past two or three decades. We build far much high-density building, which are far more complex, and the labour used in construction is largely labour hire rather than via the traditional master and apprenticeship paradigm.

However, unfortunately, our approach to home building compensation has not. The scheme requires new approaches that align with the realities of contemporary construction micro-economic decisions. Failure to do so will only lead to higher premiums and a loss in confidence in building.

In summary, the way forward includes:

- Efforts to reduce the risk profile of the building industry. Some of the current measures before the NSW Parliament will assist, but more is required;
- Implementation of innovative approaches to the provision of home building compensation that put the homeowner at the heart of the offering;
- The seeking of an amendment to the Insurance Regulations; and
- A full review of iCare' manage of the scheme.

I would be more than happy to attend any public hearings the IPART may wish to conduct regarding any aspect of this submission.

[redacted]

Mr Philip Randall Sim
Executive Director

1. HISTORY OF BUILDING REGULATION IN NSW

The building and construction industry in New South Wales has been regulated by Government since the early 1970's. A brief chronology of building regulation in New South Wales is enclosed at **attachment 5**.

Up until the late 1980's and early 1990's the operating risks associated with the building and construction industry and its risk profile were low and confidence in the building and construction industry was high.

In this era builders built:

- predominately low-rise, non-complex, single dwellings;
- to prescriptive building codes and standards;
- utilised trade contractors who had come through robust apprenticeship and vocational training processes; and
- using standardised building methods and products.

Their projects were overseen by independent (Clerk of Works) council building inspectors in addition to inspections from quantity surveyors from banks and financial institutions, which provided a robust quality assurance mechanism ensuring optimal building outcomes. Within this quality assurance framework defects were identified early and remedied prior to completion.

There was also a strong, effective, and independent regulator (the Building Services Corporation) focused on ensuring industry compliance with licensing, contracting and statutory warranty requirements in addition to administering the then home warranty insurance scheme.

Within this setting, building defects and disputation was low and consumer protection included the provision of home warranty insurance for all residential building work, including high-rise projects.

Today, builders now build:

- significantly more complex, medium, and high-rise projects;
- to performance-based alternative solutions;
- utilising trade contractors who, due to skill shortages, rely heavily upon employees or subcontractors who have not come through Australia's vocational training system whereby they have not been education in relation to the NCC and applicable standards; and
- are using rapidly changing and innovative building methods and products.

Their projects are overseen predominantly by Private Certifying Authorities (PCA's) who:

- have questionable independence from developers;
- are not well supported in their task by regulatory authorities; and
- are not appropriately remunerated to undertake the quality assurance role expected of them by consumers and regulators.

Additionally, banks and financial institutions have significantly curtailed their oversight of building projects.

While the building industry has changed significantly over the past three decades, the approach to providing consumer protection via the use of home building compensation has changed very little and, despite repeated inquiries and reviews, regulatory frameworks have diminished.

As was the case around the world, during the late 1990's National Competition Policy ushered in an era of deregulation of many market sectors in Australia and the building and construction industry was not immune from this pervasive wave of policy reform.

Additionally, the strong and pervasive aspiration for home ownership by Australians saw all political parties support deregulation policies under the guise of 'red tape' and 'regulatory burden' reduction.

The changing nature of industry and its workforce, as outlined above, together with this deregulatory cycle combined to create a 'perfect storm' resulting in the unacceptably high-risk profile of the industry that we see today.

The unwillingness of insurance underwriters to re-enter the home building compensation market in NSW and their withdrawal from providing professional indemnity insurance for building professionals are clear indications that the industry's risk profile has reached a level requiring the Government to take corrective action to address distortions leading to market failure.

2 HOME BUILDING COMPENSATION IN NSW

As outlined above, the risk assessment of the industry carried out by insurance underwriters provides an excellent barometer of the health of the building and construction industry. Accordingly, the withdrawal of all private insurers from the then home warranty insurance market in 2010 should have acted as a warning as to the need for strengthening the regulatory framework of the building and construction industry in New South Wales.

The protection of homeowners from the financial losses that can occur as a result of building or buying a home has been around almost as long as regulation of the industry.

Home Building Compensation (HBC), formerly known as home warranty insurance, has had a vexed and challenging history. A brief historical chronology on HBC is enclosed to this submission as **attachment 6.**

Over the past twenty years, successive Governments have introduced reforms to HBC largely designed to keep private insurers in the HBC market. Notwithstanding the objective, each reform has resulted in an erosion of the consumer protection provided to homeowners in NSW.

Following the collapse of FAI/HIH in 2001, the NSW Government introduced the most significant of the reforms to HBC when amendments were made to the *Home Building Act 1989* in 2002 which included:

- moving from a "first resort" to "last resort" scheme;
- cover only being provided in the event of the death, insolvency or disappearance of the builder; and
- the period of cover was reduced from seven years to six years after completion of construction.

In December 2003, the requirement for HBC insurers to provide cover to owners of apartments in buildings higher than three storeys in rise was introduced.

These reforms were successful in enticing five private insurance underwriters to enter the HBC market.

In May 2009, HBC protection was strengthened by allowing a claim to be made in circumstances where NSW Fair Trading had suspended the licence of a builder who had failed to pay a court or tribunal money order.

As a result of strong competition amongst insurance underwriters for a greater share of the market, between 2005 and 2008 HBC premiums fell significantly to unsustainable levels. A combination of unsustainable premium levels and the global financial crisis saw private insurance underwriters exit the market in 2010 with the NSW Government's Self Insurance Corporation commencing to underwrite the provision of HBC.

From 2010 to 2017 the Self-Insurance Corporation (and its successor iCare) failed to lift premiums to sustainable levels. As a result of failing to adjust premium levels and employ greater levels of risk mitigation, the home building compensation scheme sustained significant deficits.

In July 2014, the name of the product was changed from home warranty insurance to home building compensation HBC and cover for dwellings constructed by owner builders was removed from the scheme.

3 HBC SCHEME PERFORMANCE

In developing its new and innovative approach to providing HBC, SecureBuild and its actuary completed a comparative analysis of the HBC schemes operating in NSW, Victoria and Queensland. The outcome of that analysis is outlined below.

When compared to the HBC schemes operating in Victoria and Queensland, the HBC scheme in NSW is performing poorly. The number of HBC claims, average claim costs and claims costs per 1000 homes constructed in NSW, Victoria and Queensland since 2002 are set out in Table 1 below.

	Victoria				NSW				QLD			
	Claims	%	Ave cost per claim	Cost per 1000 homes	Claims	%	Ave cost per claim	Cost per 1000 homes	Claims	%	Ave cost per claim	Cost per 1000 homes
Failure to commence	189	2.30%	$18,460	$4.49	248	3.89%	$23,310	$9				
Failure to complete	1,918	25.20%	$60,806	$150	1700	26.65%	$83,699	$227	4,722	20.76%	$22,989	$187
Structural defect	3,117	52.70%	$40,085	$161	3333	52.25%	$101,001	$536	11456	79.24%	$21,336	$336
Other (non-structural) defect	1,169	19.30%	$26,795	$40	424	6.65%	$52,073	$35	6562			
Total	**6,393**	**100.00%**	**$43,232**	**$356**	**5705**	**100.00%**	**$88,831**	**$807**	**22740**	**100%**	**$13,342**	**$523**

Table 1 Claims outcome data for NSW, Vic and Qld 2002-18

Due to existence of a 'first resort' scheme in Queensland the number of HBC claims in that State is much higher than NSW and Victoria. However, the average claims costs in both Victoria and Queensland are significantly lower than NSW.

The average cost of claims in Victoria is more than 50% lower than NSW and Queensland's cost of HBC claims is 150% lower than NSW.

NSW	VIC	QLD
$88,831	$43,232	$13,342
	-48%	-150%

Table 2 Home Building Compensation average claim size 2002-19

When construction volumes are taken into account, the HBC claims cost per 1000 homes in NSW is significantly higher than Queensland's 'first resort' scheme outcomes. The difference between the HBC claims cost outcomes in NSW in comparison with a more similar HBC scheme, such as Victoria is even more significant (see figure 1 below).

Figure 1 HBC claims in Victoria, NSW and Queensland 2002 to 2017.

Perhaps most significantly, the HBC claims data reveals a much higher level of claims attributable to 'major defects' in NSW when compared to Victoria and Queensland (see figure 2 below).

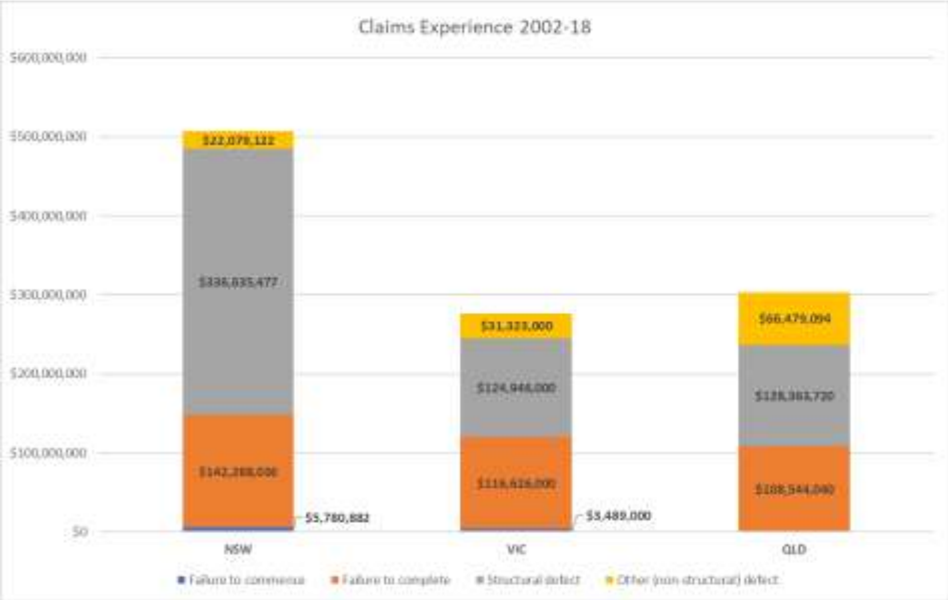

Figure 2 Total HBC claims cost comparison breakdown NSW, Victoria and Queensland (2003-04 to 2016-17).

As a result of the scheme comparatively poorer performance, the HBC premiums for consumers in NSW are substantially higher than in Victoria and Queensland (see table 3 below).

Jurisdiction	Premium for $500,00 single dwelling (2019)	% Difference
NSW	$5,695.25	
Victoria	$3,158	**-44.5%**
Queensland	$4,883.25	**-14.3%**

Table 3 HBC premium comparison

HBC premiums in NSW now represent over 1% of the contract price for a single dwelling and in excess of 3% for multi-dwellings. Premiums have risen by 60% over the past two years with iCare indicating that a further premium increase will occur by the end of the 2018-19 financial year.

Further detail setting out the rationale for substantially reforming the HBC in New South Wales is set out within **attachment 7**.

4 ATTEMPTS TO REFORM HOME BUILDING COMPENSATION

In 2015 the NSW Government indicated that the HBC scheme's deficit had reached $398m, and to its credit, commenced a consultation process seeking ideas on how to reform the scheme.

Our company, SecureBuild, lodged a submission as part of the consultation process indicating that, given the vexed history of the scheme and its failure to adequately protect consumers, new and innovative approaches to the provision of HBC were required. More specifically, our submission indicated that providers needed to provide HBC products that mitigated the significant risk of defects and prepayments in the industry.

In November 2016, the NSW Government announced a range of reforms to the HBC scheme, including:

- Splitting HBC into two separate contracts of cover (one covering the ‘construction period’ and the other covering the post construction ‘warranty’ period); and
- Allowing private insurance underwriters and non-insurers to enter the market to provide innovative HBC products.

In June 2017 the NSW Parliament passed amendments to the *Home Building Act 1989* allow for private providers (including alternative indemnity providers) to enter the HBC market.

In December 2017 the *Home Building Regulation 2014* is amended, and guidelines are published by the NSW State Insurance Regulatory Authority (SIRA) allowing for the commencement of the reforms to HBC on 1 January 2018.

In February 2018 the Australian Prudential Regulatory Authority (APRA) indicates that, despite the amendments made to *Home Building Act 1989* by the NSW Government, “Alternative Indemnity Providers” were captured by the Commonwealth’s *Insurance Act 1973* and deemed insurance businesses thereby subject to regulation by APRA.

APRA’s position effectively meant that, unless:

- The NSW Government sought an amendment to Schedule 2 of the Commonwealth *Insurance Regulation 2002*; or
- Individual exemptions are granted to HBC Alternative Indemnity Providers,

only insurance underwriters licensed by them could enter the HBC market in NSW. This is despite similar arrangements operating in the Northern Territory and the Australia Capital Territory.

SecureBuild lodged an exemption application with APRA in October 2018 and they indicated that they will not provide Alternative Indemnity Providers with an exemption from the *Insurance Act 1973* as, in their view, the prudential framework established by the NSW State Insurance Regulatory Authority (SIRA) was not adequate to protection policy HBC holders.

Our view is that APRA did not fully understand SIRA’s prudential requirements, which actually mirrored theirs.

Unless the dual regulatory issue with APRA is resolved:

- there will be no new entrants into the HBC market in NSW;
- homeowners will not be given the opportunity of experience superior consumer protection;
- scheme performance will not improve; and
- premiums will continue to increase.

5 SECUREBUILD’S APPROACH TO THE PROVISION OF HBC TO CONSUMERS

SecureBuild has developed a new and innovative home building compensation offering that has been designed to:

- Significantly increase consumer protection;
- Provide effective support to builders;
- Produce better building outcomes;
- Significantly reduce defects and overpayments by homeowners;
- Significantly, reduce claims and claims exposures;
- Deliver a profitable and sustainable scheme with lower premium; and
- Ultimately provide cover to the owners of high-rise apartments

Whereas the failure of the current approach to providing HBC comes from solely focusing on a builder's financial status (that can change at any time), SecureBuild's approach to providing HBC products was designed to mitigate the risk of a homeowners sustaining a loss as a result of building defects, overpaying or prepaying their builder.

In summary, SecureBuild's HBC product offering involved the following elements:

- Allocating a build inspector to each building project to support the homeowner and provide feedback to their builder;
- The building inspectors would conduct inspection at critical stages and, should the building work by complete and free of defects, they would notify the homeowner to pay their builder's progress claim payment;
- Where defects or incomplete building work was detected, the building inspector would advise the homeowner not to pay their builder's progress claim payment and provide the builder with a defects list;
- Once defects/incomplete work had been remedied the building inspector would reinspect;
- Building inspectors would also assist in quickly resolving and misunderstanding or dispute between the builder and the homeowner; and
- SecureBuild's building inspectors would ensure that trade contractors where aware of and had an up-to-date understanding of the National Construction Code and Australian Standards that were applicable.

Research by its actuary supported the proposition that SecureBuild's approach could reduce defect and claims costs by at least 40%.

Further details regarding SecureBuild's proposed innovative HBC product offering is set out within **attachment 8.**

6 THE WAY FORWARD FOR HOME BUILDING COMPENSATION

Given the present situation the NSW Government has a number of alternatives available to it to improve the protection HBC affords to homeowners, these include:

- Fully implementing its original reforms for the scheme by seeking an amendment to Schedule 2 of the Commonwealth *Insurance Regulations 2002*; or
- Enhancing the provision of HBC by requiring iCare to adopt new and innovative approaches to the management of risk; and
- Enhancements to the Developer Bond Scheme administered under the *Strata Schemes Management Act 2015*.

7 PROPOSED REFROMS TO REDUCE RISK AND IMPROVE OUTCOMES

The risk profile of the building and construction industry would also benefit significantly from:

- Implementation of higher qualifications for builders of medium density and high-rise building (similar to the tiered approached to licensing in Victoria and Queensland);
- Greater use of industry data to target Continual Professional Development (CPD) courses for all building practitioners;
- Regulator focus on sub-contractor accountability and capability;
- A 'one-stop-shop' approach to regulation with a single industry regulator;
- Greater accountability of building professionals (building designers and engineers as proposed by the NSW Government and Shergold Weir report);
- A central register of all building work undertaken in NSW which retains building plans and all declarations made by relevant building practitioners for future access by owner's corporations and home purchasers (similar to the reporting framework proposed by the NSW Government and Shergold Weir report);
- Implementing a framework whereby PCA's are supported by the industry regulator; and
- Introduction of a PCA allocation scheme for developer projects as a means of eliminating conflict of interest issues.

8 RESPONSES TO IPART'S QUESTIONS

1. What changes to the scheme would encourage the supply of new, innovative products - both different types of insurance and non-insurance products?

- The lowering of the risk profile of the industry via the adoption of regulatory approaches applied in other jurisdictions (see **Attachment 9**); and
- An amendment to the Commonwealth Insurance Regulation 2002; and
- An order by ASIC not requiring HBC providers to also be subject to regulation by ASIC.

2. Should private providers be allowed to mitigate risk by limiting insurance to high risk builders, or other methods?

This is where innovative approaches are required whereby builders are incentivised for lowering the risk that they may present.

At present, the only focus on the financial risk that they present. The incentive needs to be for good building practices and performance. Again, if there are not defects then there is no claims!

3. To what extent do the requirements of the Home Building Act 1989 duplicate the Insurance Act 1973 and increase costs of entry for private insurers?

A significant impediment. For private providers offering HBC they would be effectively regulate by APRA, ASIC, SIRA and the ACCC. No private business can afford the compliance costs associated with this level of over regulation.

4. What additional information would be helpful to homeowners in selecting a builder?

The current public register of builders (if used by a homeowner) is limited to information as to whether a builder has had action taken against them or a NCAT order issued.

There has now been private sector investment in developing data bases of information on builders for homeowner to inquire into before selecting a builder.

However, by and large, ironically consumers appear to be making irrational decisions when undertaking the most significant purchase in their lifetime in selecting a builder.

5. How could the claims process be made more efficient?

The outsourcing of claims management involves moral hazards that unless you completely understand the building rectification process becomes problematic. iCare's outsource approach continues to be plagued by gold plated solutions and maximum claim payments being recommended to the provider.

At the end of the day, the outsources provider's motivation is to maximise the profit it can make out of an outsourced arrangement. Accordingly, providers without the appropriate incentives in place with inflate claim assessment. The same is the case for rectifying builders.

The main objective should be to minimise of claims by proper risk mitigations during the course of construction. However, earlier dispute resolution by the provider will assist in reducing the size of claims. At present this is disconnected from the HBC process and done by NSW Fair Trading and or within NCAT.

6. What incentives should the scheme have for builders to undertake good risk management and encourage good business practices?

This has always been one of the major problems of the home building compensation schemes. The current scheme does not reward good builders for demonstrating good lower risk behaviours. That is why incentives formed a major element of SecureBuild's approach. A comparison of SecureBuild's approach to that of traditional underwriters is enclosed as **Attachment 10**.

Lower premiums do not, of themselves, act as an incentive for builders. Increasing a builder's turnover (and therefore potential profit) is far more attractive incentive.

The SecureBuild approach to incentivising the right behaviours was a combination of carrot and stick.

The carrot comprised of:

- Lower premium rates;
- Increased turnover levels (this is the most valued incentive); and
- Free dispute resolution services

The stick comprised of:

- Higher premium rates;
- Decrease in turnover levels; and
- The payment of dispute resolution services
-

7. How could enhanced information collection be used to further mitigate builders' insolvency risk?

Unless an underwriter has 24/7 access to all the financials of every builder on its books focusing on financials is illusory. A builder's financials can change in hours or days. So, any attempt to focus on this as protection against claims is fraught.

Many of the data sets available (e.g. credit reference groups) are lagged data. Accordingly, it is somewhat impossible to pre-empt a builder insolvency.

This why any sustainable approach needs to focus on the causation of claims, That is, builders getting paid in advance of the work they do and defective building work. If these two things do not occur, then there is no loss suffered by a homeowner that would give rise to a claim.

If underwriters continue to solely focus on attempting to reduce risk by monitoring insolvency, then we are doomed to history repeating itself and a continued decline in the scheme's sustainability.

8. Is an efficiency study of icare's economic costs necessary?

Absolutely. iCare have clearly demonstrated a failure to understand the micro-economic involved.

9. Do you consider the current eligibility assessment process should be simplified?

Yes, and it can be if provider move away from the lazy approach of demanding financial information from builders over and over again.

10. Could this be done without subjecting the Home building compensation fund to greater risk?

Absolutely. If providers put in place other risk mitigations measures together with proper incentives for builders, it will significantly lower risk and produce better outcomes for homeowners and claims outcomes.

11. Are there any other unnecessary regulatory or administrative burdens and barriers to entry for builders that should be reviewed?

Builder's licensing education requirements need tightening so that they are in line with other better performing jurisdictions.

Meeting iCare's financial requirement is the biggest barrier. It has ironically led to builders moving into high-rise development that does not require HBC cover.

12. What changes to the scheme would encourage private providers to enter the market?

- Enhanced educational requirement for builders;
- A reduction in the risk profile of the industry;
- An amendment to the Insurance Regulations 2002;
- An ASIC order placing HBC providers outside the Corporation's Act framework;
- Establishment of the Home Building Guarantee Fund;
- Amendments to SIRA's underwriting and licensing guidelines; and
- Several years of positive loss ratios.

13.. What conditions would encourage private entry into the HBC market?

As above.

14. Are there any financial or market barriers preventing private entry?

Yes, substantial. However, appropriate financial reserve capacity is necessary for any entrant to ensure that it can honour the claims that it receives. The key element here is ability to obtain reinsurance from a reinsurer. SecureBuild was able to obtain reinsurance support from Lloyds of London. However, SIRA failed to understand the significance of this.

The financial barriers are exacerbated if the provider is required to be regulated by APRA as well as SIRA.

15. Do Government regulations or legislation deter private entry into the HBC market?

Yes, the interoperability of State and Commonwealth laws, principally the *Home Building Act 1989, The Insurance Act 1973* and *Corporations Act 2001* were not properly canvased when the asked by the NSW Government to implement the HBCF reforms.

Once these issues become known, SIRA remained reluctant to deal with them indicating that they were issues for applicants to resolve with APRA and ASIC.

16. What changes to the scheme would encourage the supply of new innovative products – both different types of insurance and alternative products?

As above, but also requiring SIRA to address the issues outlined above.

17. Should private providers be allowed to mitigate risk by limiting insurance to high risk builders, or other methods?

As above.

18. To what extent do the requirements of the Home Building Act 1989 duplicate the Insurance Act 1973 and increase costs of entry for private insurers?

As above.

19. Are there any other deterrents to private participation in the HBC market?

No.

20. How could the scheme further reduce defects and insolvency?

As outlines above.

21. What incentives should the scheme have for builders to undertake good risk management and encourage good business practices?

As above.

– Are the current incentives sufficient for builders to undertake good risk management and encourage good business practices?

They are absent from the current scheme and this is one of the underlying causes for poor outcomes.

– What further incentives should be included for builders to undertake good risk management and encourage good business practices?

As above.

– What incentives should be included in eligibility conditions and/or premium pricing so that builders are incentivised to reduce the likelihood and severity of potential future

claims through improved quality of work?

As above.

22. How could enhanced information collection be used to further mitigate builders' insolvency risk?

Financial data is too lagged to be relied upon as a determinant of future claims. Failure of providers to employ other additional risk mitigation measures will result in continued poor scheme performance.

– How could enhanced information collection in relation to builder progress payments, critical stage inspections and issuance of compliance certificates be used to further mitigate builders' insolvency risk?

Risk mitigation processes whereby the builder only receives payment following the satisfactory completion of a building stage will significantly reduce claims. This is the cornerstone of SecureBuild's approach.

– Are licensed providers able to readily access information on builder progress payments, critical stage inspections and issuance of compliance certificates or would licensed providers be required to collect this information themselves?

Licensed provider would need to collect this information themselves. New technology allows this to occur quickly and seamlessly for the builder and homeowner.

– Could this information be used effectively in imposing conditions on builders' eligibility, either through reducing a builder's open job limit, or through a more light-handed approach by requiring that builders enter into a program with increased supervision?

Yes.

– Are there other measures that should be implemented to mitigate builders' insolvency risk?

Any sustainable scheme has to move away from the failed approach of solely focusing on builder financials.

HOME BUILDING AMENDMENT (COMPENSATION REFORM) BILL 2017

LEGISLATIVE ASSEMBLY

SECOND READING SPEECH

Mr VICTOR DOMINELLO (Ryde—Minister for Finance, Services and Property): I move:

That this bill be now read a second time.

Introduction

Madam Speaker, I am pleased to introduce the Home Building Amendment (Compensation Reform) Bill 2017. The reforms in this Bill introduce a modern, fit for purpose, Home Building Compensation scheme. The future system will be risk based, self-funding, sustainable, innovative and competitive. By comparison, the existing scheme is an old-fashioned, loss-making, unsustainable, government monopoly.

More than 55,000 home building and renovation projects are covered by this scheme every year.

The Bill will maintain consumer protection for home owners, who can be confident that the scheme will be there if their builder cannot complete or fix works on their home. At the same time, the Bill opens the door for new providers to enter the scheme with innovative product offerings. Builders will get a more transparent system that can give them more choice about how they cover their projects, while home owners can receive cover that exceeds the minimum prescribed in legislation. The Bill confirms the State Insurance Regulatory Authority's role as the independent regulator of the scheme with powers to ensure the scheme operates sustainably, and enables smarter, data-driven and efficient regulation of the building sector.

Why the need for reform? This type of insurance has presented challenges across Australia, both as a private sector provided product and as a government provided product. On February 2016, consumer advocacy group, CHOICE published an article titled, "Domestic building insurance: The story of the worst insurance product in Australia"[1]. The article stated:

State-run DBI is at a crossroads. On the one hand, claims payouts are outstripping premium intakes in many jurisdictions. On the other hand, properly designed DBI is an important safety net for homeowners, which is why it is a mandatory purchase across most of the country.

The current government monopoly scheme in NSW was established in 2010. It was said at the time that the scheme was intended to "run on a commercial basis, funded by premiums with no costs to taxpayers"[2]. The hopes for the government underwritten scheme to succeed have not been met and it remains in need of further reform.

The scheme has been financially unsustainable and has become a burden on all taxpayers. As at 30 June 2016, the HBC scheme was $375.8 million in deficit. It is inefficient, with far too much of the premium being

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[1] https://www.choice.com.au/money/insurance/home-and-contents/articles/domestic-building-insurance

[2] The Hon. Michael VEITCH MLC, Legislative Council Hansard – 01 June 2010 https://www.parliament.nsw.gov.au/Hansard/Pages/HansardResult.aspx#/docid/HANSARD-1820781676-40654

absorbed by costs, and too little returned to home owners. Before the Government's reforms, around 37% of the premium was going to brokers and scheme agents. The scheme is frustrating for many builders, who can face complicated and opaque eligibility assessments before they are allowed to buy the product, and which can delay work or disrupt their ability to win contracts. Builders cannot take their business somewhere else when they are unhappy about the level of customer service and transparency they receive.

This Bill is one part of an overhaul of the scheme that I announced on 3 November 2016. It is the culmination of a long journey of reforms to the Home Building Act. It started with amendments in 2011 that were a prelude to the biggest boom in home building activity that NSW has ever seen. The then Minister for Fair Trading, the Hon. Anthony Roberts MP, said of the 2011 Bill that it was:

"…an important step forward in fixing this messy, complex area. However, I have made very clear that these reforms only mark the beginning of a comprehensive program of reviewing and reforming the legislation"

The Bill I introduce reflects extensive industry and public consultation since that time. It builds on the reforms to the Home Building Act that the Parliament made in 2011 and 2014, and the Government's insurance reforms of 2015. The reforms also complement the NSW Government's wider efforts to improve the regulation of the building sector through reform of strata development laws, building certification, and security of payment legislation. The Bill will address the home building compensation scheme's failings and give NSW the best system in the nation.

Details of the Bill

I now turn to the details of the Bill. The Bill before you establishes a legislative framework for private sector providers to offer Home Building Compensation cover by way of insurance or alternative indemnity products. This will increase competition, consumer choice and promote competitive and sustainable pricing.

The amendments that the Bill makes to section 102 of the Act allow the Government's insurance provider, the

Self Insurance Corporation, to continue to deliver insurance to builders through icare, while opening the scheme to new players. The NSW Government has directed the Self Insurance Corporation to move its product pricing to full cost recovery and ensure it operates more efficiently, with less of the premium being dissipated on scheme costs. The Government scheme will cease to be a burden on taxpayers and new market entrants will be able to compete on a level playing field.

In April 2017, the first of these changes was implemented with the abolition of broker commissions and adjustments to premium pricing. Further premium changes will be implemented in October 2017.

The Bill inserts a new Part 6C in the Act that will provide for the State Insurance Regulatory Authority to license insurers and other providers of cover under the Home Building Compensation Scheme. Licensing of insurers and other providers is an important innovation that distinguishes these reforms from the old, privately-provided Home Warranty Insurance scheme that operated until 2010. Licensees will be subject to a far more rigorous regulatory oversight that supports the overall sustainability of the scheme.

New section 105B will deem the Self Insurance Corporation to be a licensed insurer under the Act, so it will be regulated by the Authority in a similar way to new private sector entrants to the market. The NSW Government has previously sought to separate the regulation and provision of other insurance products that the NSW Government is involved in, and these changes complete that process for the Home Building Compensation Scheme.

In addition to insurance products, the Bill will allow cover under alternative indemnity products to be offered, such as fidelity fund schemes and specialised insurance arrangements. The Bill inserts a new Part 6B to set out specific provisions for alternative indemnity products. Fidelity funds are already operating in the home building compensation market in the Australian Capital Territory and the Northern Territory.

Fidelity funds will be licensed and need to meet equivalent requirements to insurers under the scheme.

The cover offered by these products will need to meet or exceed the minimum cover requirements of the legislation in the same way as insurance. I note that, unlike general insurers, fidelity funds are not subject to oversight by the Australian Prudential Regulatory Authority. The State Insurance Regulatory Authority will draw on its experience regulating providers that are not insurers in the other regimes that it administers, to ensure that alternative indemnity products are regulated on an equal footing with insurance providers. These arrangements will be further detailed in the regulations and guidelines.

The Authority will be able to issue comprehensive Insurance Guidelines under Part 6, that bind the behaviour of licensed insurers and providers. The Insurance Guidelines will cover matters including premiums, market practices, claims handling, prudential standards, contracts of insurance, underwriting and builder eligibility to buy cover.

Premiums and builder eligibility are two matters to which I draw your attention. The Bill inserts provisions governing premiums in Part 6 of the Act. Licence holders will only be able to charge premiums that have been filed with, and approved by, the Authority. The Authority will issue Insurance Guidelines so that it is clear to licensees what they need to take into account when proposing premiums and what supporting material they must give the Authority. This is another important distinction between the new scheme and the old pre-2010 Home Warranty Insurance scheme, which did not require approval of premiums. Under the changes in the Bill, the Authority will be able to reject premiums that are excessive or inadequate. No one wants to see a re-run of insurers inadequately providing for future claims and spiralling out of the scheme. The Government's reforms will ensure that premiums are set at levels that are both sustainable and fair. This will apply both to private insurers and providers, and to the Self Insurance Corporation.

The Bill also takes builder eligibility standards out of the hands of the Self Insurance Corporation. It will ensure that these standards are set at arms-length by the Authority for all licensed insurers and providers. Eligibility is a key area of builder frustration with the current scheme. Whether a builder can obtain eligibility can make or break their business. It is important that eligibility standards are clear and transparent. Builders should get clear guidance on what options they have to lower their risk profile to get better eligibility and premium pricing outcomes. Encouraging builders to lower their risk of claims on the scheme is not only good for the scheme, but can help reduce the underlying risk to home owners.

The cost of regulating the scheme will be met from within industry rather than from taxpayers. All licence holders, including the Self Insurance Corporation, will need to contribute to a Home Building Operational Fund under proposed Division 5 of Part 6 of the Act. This will support the operations of State Insurance Regulatory Authority. Licence holders will also have to contribute funds to a Home Building Guarantee Fund under proposed sections 103OA and 103OB. These funds will be held against the risk of an insurer becoming insolvent. While I am confident that the scheme will be well regulated, it is important that this back-stop be available to address an insolvency that stems from matters outside of the government’s control.

The Bill includes changes to the scheme to enable licence-holders to offer diverse and innovative products that exceed minimum standards. One of the challenges of this product for providers is that it is a ‘long tail’ product. The current insurance product can only be offered as a single product that covers both the risk that work will not be completed during the construction phase of a project, as well as the risk of defects out to the end of the statutory warranty period that extends to 6 years after the work is complete.

The Bill amends these requirements that are set out in section 99 so that cover may be provided as two separate products, which can be provided by different licence holders. One product will cover home owners against the risk of loss due to non-completion and associated breaches of statutory warranty during the construction period. The second product will cover home owners against the risk of loss after the work is complete for the duration of the statutory warranty period. Builders will still need to take out cover for both risks, whether through buying a combined cover product, or by buying the two split cover products.

There is no reduction in protection for consumers, in fact it will be enhanced. In 2011 the NSW Government increased the minimum cover for home owners to $340,000. In 2017, we will set each of the split cover amounts at $340,000, with the result that home owners will have a minimum total cover of $680,000 available. Currently, non-completion claims degrade the amount of cover remaining to home owners if latent defects become apparent down the track requiring a further claim. Under split cover, the full $340,000 will be available to them during the warranty period, regardless of whether they have previously claimed for non-completion. For insurers and providers, they will be able to specialise in one or other split cover product and limit the nature and duration of risk they are insuring. This could potentially include ‘hybrid offerings’ where an alternative indemnity product covers one side of the split and conventional insurance covers the other.

The potential for product innovation is also enabled by the Bill’s amendments to section 102 of the Act. These amendments confirm that insurers are able to offer products that exceed the minimum requirements of the Act. The Act currently requires that products must at least cover losses arising from non-completion or breach of statutory warranty in the case where the builder has died, disappeared, become insolvent or has failed to comply with certain Court or Tribunal orders. The amendments in the Bill confirm that cover can be offered for other circumstances, including for additional kinds of risk or loss. This could potentially include 'first resort' style products that offer consumers access to help while a builder is still solvent and trading. It could include the provider and the builder agreeing on arrangements to improve quality control of building work or to help manage disputes as part of the cover. It could include the facility for the home owner to purchase top-up cover.

The Act will allow examples to be prescribed in the regulation to confirm beyond doubt that they may be offered.

The Bill also contains provisions to enable better gathering of data form the scheme, and enables it to be used, shared and published to support the effectiveness and transparency of the scheme as well as supporting the wider building regulation system. The Government's previous reforms in 2014 included sensible reforms enabling the publication of an online register of insurance certificates so that home owners and home buyers could check whether property was insured and if there were any claims. This Bill will go further so that the Authority will have wider powers to be able to collect, analyse and publish information relating to licensed insurers and providers, policies and claims, and to exchange information with other regulators. These changes will enable smarter regulation that maximises our ability to make use of modern data analytics to better target and tailor regulatory action by Government for the building industry. The Data Analytics Centre has already examined builder and claims information and based on early analysis can predict builder insolvency with 85% certainty.

Consultation on reform

The review of the Home Building Act that kicked off in 2012 included extensive consultation with a host of public and industry stakeholders that are too many to name over a period of two years. It resulted in wide-ranging amendments to the Act in 2014. These included some changes to the Home Building Compensation scheme, such as the public register of insurance certificates and the restriction of the scheme to professional, licenced builders.

However, it was also clear that detailed, and focused work specifically targeted at the scheme would be required. In 2014, the then Minister for Fair Trading, the Hon. Matthew Mason-Cox MLC announced this second review focused on the problems with the scheme. This included first a targeted consultation through a Building Industry Working Group. The Working Group included the Housing Industry Association, the Master Builders Association of NSW, the Insurance Council of Australia, the National Insurance Brokers Association, NSW Fair Trading, the Self Insurance Corporation and the Office of the Small Business Commissioner. The output of this Working Group helped to inform a set of options that I released for public consultation in late 2015. Public feedback was received from a range of stakeholders including builders, building industry associations, the insurance industry and consumer protection associations.

In total, 74 submissions and 775 survey responses were received, evidencing strong interest in the future of this scheme. Many of the submissions and survey responses recognised that the current scheme is broken and in need of reform. However, there was no clear consensus about what should be done aside from broad support for a mandatory scheme to be retained in one or other form.

I would like to thank those stakeholders who have offered constructive assistance and support for these reforms: I thank Mr Dallas Booth, CEO of the National Insurance Brokers Association, who I note has said of the reforms that “Insurance brokers believe competition and innovation will bring higher standards of service and support to builders and home owners, as well as new initiatives in the areas of risk assessment, risk management and insurance”.

I also thank Mr Brian Seidler, Executive Director of the Master Builders' Association, who said:

"These are long overdue and far reaching reforms to the home building compensation fund scheme. The MBA has been closely involved in reform discussions with the government on this over many years. This Bill is the first of a number of key steps needed to improve the scheme for both builders and consumers. The MBA believes these reforms are a positive step and looks forward to working with the government on the more detailed regulations and guidelines that will be needed to put these reforms into practice."

Finally I thank Mr Phil Sim and Steve Griffin from Secure Build who said, "the reforms outlined in the Bill will allow for new and innovative approaches to be delivered vastly improving consumer protection and allowing builders to get on with building the housing we require in this State".

This Bill establishes a new framework for home building compensation. Subject to Parliament's approval, the next stage will be for the Authority to consult on development of supporting regulations and Insurance

Guidelines. This will be an extensive process through the second half of 2017. The Authority will consult carefully to ensure the new scheme achieves the confidence of home owners, builders, brokers and prospective insurers and providers. This will enable the new scheme to commence in early 2018. I have also asked the Authority to work with co-regulators such as Fair Trading on how the Home Building Compensation scheme can be better aligned with and support other aspects of building sector regulation.

I would like to thank staff of the State Insurance Regulatory Authority that contributed to these reforms, particularly Anthony Lean the outgoing CEO of the Authority, and Carmel Donnelly who has so capably acted as CEO since Anthony’s move to a new role. I thank also Dr Rhys Bollen, Dr Petrina Casey, Richard Potts, Anneliese French, Chris White, Gavin Robertson, Tanya Briggs, Louise Briffa, Steve Harrison, George Pozo, Jason Donohoe, Felipe Charry, Penelope Worthington, Ibrahim Khoury, and Rebecca Neilson. I also acknowledge the contribution of the SIRA board:

Chair Trevor Matthews, Deputy Chair Nancy Milne, Abby Bloom and Dr Graeme Innes.

I also thank staff at the Department of Finance, Services and Innovation that have contributed to these reforms, led by Secretary Martin Hoffman. I thank Matthew Press, Katherine Sharah and Mitchell Harris. I thank also the team at NSW Fair Trading for their input to these reforms, including Commissioner Rod Stowe, John Tansey, Lynelle Collins, Wendy Parsons and Amber Pathak as well as Vivek Bhatia, Jon East and Steve Hunt and their team at the Self Insurance Corporation for their work to improve the administration of the government scheme. Finally I thank my Ministerial staff Matt Dawson and Jane Standish for their work on this important reform.

I commend the Bill to the house.

ENDS

AUSTRALIAN PRUDENTIAL REGULATION AUTHORITY
1 Martin Place (Level 12), Sydney, NSW 2000
GPO Box 9836, Sydney, NSW 2001

T 02 9210 3000 | W www.apra.gov.au

APRA

21 December 2018

Ashurst Australia
Level 11
5 Martin Place
Sydney NSW 2001

Attention: Rehana Box

Dear Ms Box

SB FIDELITY LTD – APPLICATION FOR DETERMINATION UNDER SECTION 7 OF THE INSURANCE ACT 1973 (CTH)

I refer to the application made by Ashhurst via email on 12 November on behalf of SB Fidelity Ltd ACN 624 035 301 (SecureBuild) for a determination under section 7(1) of the *Insurance Act 1973* (the Act) that Part 3 of the Act, other than Division 3A, not apply to SecureBuild at all times its insurance business is regulated by the State Insurance Regulatory Authority (SIRA).

From the application it appears that SecureBuild is seeking to provide an alternative indemnity product (AIP) in the form of a fidelity fund to be established under the amended NSW Home Building Act scheme. The scheme has been in effect since 1 January 2018. SecureBuild proposes to offer home warranty cover (relating to losses arising from non-completion of building work or breach of statutory warranties).

The application [p.6] states that the offer of home warranty cover, by way of a contract of insurance, will comprise insurance business under the Act. APRA agrees with this characterisation.

It is also common ground that the proposed offer of home warranty cover does not fit within any of the exemptions (from authorisation) specified in section 3A of the Act and the Insurance Regulations made under the Act.

You have submitted [on pps.7-8] that an authorisation should not be required by SecureBuild under section 12 of the Act. The reason you state is that regulation by SIRA will suffice to protect policyholder interests (i.e. named beneficiaries under contracts to be issued by SecureBuild). However, in APRA's view, no amount of oversight by SIRA will adequately protect policyholders unless SecureBuild is required to hold eligible capital of an amount which is adjusted in accordance with the scale, nature and inherent risks associated with its proposed insurance business.

APRA has a suite of prudential standards which authorised insurers must comply with including standards relating to capital matters, approved auditor and approved actuary requirements. These standards apply a risk based methodology and are sensitive to changes in the nature of the risks being taken by a particular insurer. This is not a feature of SIRA's prudential regime where a key requirement is maintaining minimum capital of $2 million. This falls well short of APRA's capital requirements and, if solely relied upon to protect policyholders, would prove inadequate if an AIP insurer were to face financial difficulties.

APRA cannot therefore be satisfied that the requirements imposed by SIRA are of an equivalent kind to those that apply to insurers authorised under the Act. Indeed, with respect to the regulation of CTP and workers compensation business in New South Wales, SIRA and APRA each require insurers participating in such business to be separately licensed by each of SIRA and APRA. You have provided no grounds as to why such dual regulation is not appropriate for AIP insurers in general or SecureBuild in particular. I am therefore not satisfied there is a special case for exempting SecureBuild from being required to obtain authorisation under the Act.

For the above reasons, I cannot be satisfied that SecureBuild should be exempted from complying with the requirements of Part 3 of the Act (other than Division 3A). Indeed I believe such an exemption might potentially cause material detriment to policyholders of SecureBuild should SecureBuild not be required to hold capital and obtain actuarial advice consistent with the requirements of the prudential standards determined under the Act.

I note that in the event of there being an insufficiency in the assets of a fidelity fund (of the kind proposed by SecureBuild) to meet claims made by policyholders that SecureBuild can call upon its ordinary unit holders to subscribe additional capital. This is not helpful in the circumstance where ordinary unit holders may not be willing or able to subscribe additional capital to meet such shortfalls.

I further note that while a fund may be established by the New South Wales government to partially meet shortfalls in such circumstances, the arrangement has yet to be put in place. APRA has not been advised of the particulars of the fund (its administration and sources of funding) and I therefore cannot draw comfort that in the event of an AIP provider being wound up, policyholder interests will be properly protected. As I have noted above, this can only be achieved satisfactorily where an AIP provider is required to comply with APRA's capital and other prudential standard requirements.

Based on the above reasoning, as a delegate of APRA under subsection 7(1) of the *Insurance Act 1973*, I refuse the application you have made to not apply Part 3 of the Act to SecureBuild.

[redacted]
APRA Member - Insurance

ATTACHMENT 1

THE HISTORY OF BUILDING REGULATION IN NEW SOUTH WALES

1970's

- In 1971 the NSW Government passed the *Building Licensing Act 1971* creating the Builders Licensing Board (BLB). The BLB was made responsible for setting qualifications requirements for builders and regulating builders.

- In 1972 two home warranty insurance schemes commenced operating under the 'House Purchasers Agreement' and 'Trade Indemnity Agreement'. Both schemes were administered by the Builders Licensing Board. The House Purchasers Agreement initially provided cover of up to $40,000 for individual building work above $1,000. The Trade Indemnity Agreement initially provided cover above $200 up to $1,000
- for work performed by individual tradespersons.

- Between 1972 and 1978 the BLB extended licensing to various trade occupations

- In 1979 the *Plumbers, Drainers & Gasfitters Act 1979* was passed by the NSW Government and took effect in April 1980. The PD&G Act created a Plumbers Board who were responsible for the licensing of plumbers, drainers and gas fitters.

1980's

- The Plumbers Board was subsequently merged with the Builders Licensing Board to form the Building Services Corporation (BSC) in 1987 following the passing of the *Building Services Corporation Act 1987* (later replaced by the Building Services Corporation Act 1989).

- In 1989, the NSW Government passes the *Home Building Act 1989*. Many of the provisions of that Act remain today.

- In March 1990 the Home Purchasers Agreement and the Trade Indemnity Agreement were replaced with the Comprehensive Insurance Scheme and the Special Insurance Scheme, established under the *Building Services Corporation Act 1989*.

- Under the Comprehensive Insurance Scheme, the maximum cover for defective work was $100,000 and $25,000 for incomplete work. Major structural defects were covered for seven years, and general defects for three years, from the date of substantial commencement of the building work. The Special Insurance Scheme applied to other residential building work, being single trade or specialist trade work. The maximum level of cover was $10,000 for one year.

1990's

- In 1990, the NSW Government amends the BSC Act making the BSC responsible for the licensing of electrical contractors and abolishes renewal fees for qualified supervisors.

- The 1992 report by the Royal Commission into the Building Industry was released (the Gyles report) recommending, amongst other things, a move towards the private underwriting of home warranty insurance.

- In 1993 the Dodd Inquiry into the Building Services Corporation (the Dodd report) recommended the disbanding of Building Services Corporation and a move toward private underwriting of home warranty insurance.

- In 1995 the NSW Government accepted the recommendations of the Dodd Inquiry and the former BSC is integrated into the Department of Fair Trading (now the Office of Fair Trading which from 2003 formed part of the Department of Commerce).

- After the State election in 1995, the Government examined the possibility of introducing an insurance scheme operated by the private sector.

- In November 1996 the NSW Government passed amendments to the HBA establishing mechanisms for home warranty insurance to be provided private insurers. Under the private scheme all defects were required to be covered for seven years. The minimum cover required was $200,000. This applied to both defective and incomplete work.

- In May 1997 the private Home Warranty Insurance scheme commenced.

- The introduction of the scheme coincided with the disbandment of the BSC insurance schemes. However, the Government retained responsibility for potential future claims made under the old schemes. The Government continued to administer the run-off of the closed BSC schemes through the Fair Trading Administration Corporation (FTAC).

- The scheme's assets were exhausted resulting in claims being funded out of the Government's consolidated fund. Generally, no further claims were accepted after 30 April 2004. However, the Home Building Act 1989 provided for the Commissioner for Fair Trading to exercise discretion to accept claims for an additional three years.

- In 1998, the NSW Government amends the *Environmental Planning & Assessment Act 1979* to allow for certification by private principle certifying authorities.

2000's

- In March 2001 HIH/FAI collapsed creating severe dislocation of the Home Warranty Insurance market. HIH/FAI had around 30–40% of the HWI market and, in many cases the HIH offered the lowest premiums and easiest criteria for builders to obtain cover.

- After the HIH/FAI collapse, significant delays were caused to builders attempting to obtain cover for new work. Some ex-HIH/FAI clients also could not meet the requirements of the remaining insurers underwriting the scheme - Royal & Sun Alliance (Vero), Dexta/Allianz and Reward.

- In April 2001, the Government established the HIH Rescue Scheme. Homeowners covered by HIH/FAI policies were indemnified by the Government, with the Rescue Scheme for Home Warranty Insurance administered by the Building Insurers' Guarantee Corporation (BIG Corp).

- In February 2002 the Consumer, Trader and Tenancy Tribunal (CTTT) was established to handle building dispute claims.

- In March 2002 the NSW and Victorian Governments moved to put in place arrangements for the necessary reinsurance for Allianz to continue supporting Dexta to provide Home Warranty Insurance. However, on 31 December 2002, Dexta ceased writing new business as its insurer, Allianz, withdrew from the market.

- In June 2002 the report into the National Review of Home Builders Warranty Insurance and Consumer Protection (the Allen report) was released.

- In July 2002 amendments to the *Home Building Act 1989* via the *Home Building Amendment (Insurance) Act 2002* commence. The amendments make fundamental changes to the home warranty scheme including moving from a "first resort" to "last resort" scheme. Cover now only provided in the event of the death, insolvency or disappearance of the builder. Period of cover is reduced from seven years to six years after completion of construction.

- In 2002 the report by the Joint Select Committee on the Quality of Buildings (the Campbell report) released recommending the establishment of an independent Building Authority.

- In February 2003 the NSW Government announces that, in response to the Campbell Report recommendations, it will establish the NSW Home Building Service (a major division within NSW Fair Trading). The Home Building Service includes additional investigators to provide onsite inspection and mediation services.

- In May 2003 Minister Della Bosca announces the Inquiry into the New South Wales Home Warranty scheme and Mr Richard Grellman is appointed by the Governor of New South Wales to undertake the Inquiry.

- In July 2003 the Home Building Service commences to deliver dispute resolution and onsite inspection and mediation services.
- In October 2003 the final report of the NSW Home Warranty Insurance Inquiry released. The Government endorses the thrust of the principal recommendations. The Inquiry found that home warranty insurance should continue to be provided by the private sector and made seven primary recommendations for reform of the scheme to ensure its transparency and accountability as well as its accessibility and affordability to builders and the level of protection provided to homeowners.
- A Home Warranty Insurance Scheme Board is appointed to oversee the implementation of the Inquiry's recommendations.
- In December 2003, the NSW Government amends the HBA removing the requirement for home warranty insurance in relation to the construction of high-rise (multi storey) residential buildings (i.e. buildings with a rise of more than three storeys containing two or more dwellings).
- Australian International Insurance Limited (AIIL) takes over the home warranty insurance business of Reward Insurance Limited.
- In May 2004 approval is given for CGU Insurance Limited (part of the IAG Group) to provide home warranty insurance in New South Wales.
- In November 2004, the Commonwealth Productivity Commission releases its research report into Reform of Building regulation.
- In February 2005 approval is given for Lumley General Insurance Limited to provide home warranty insurance in New South Wales.
- In May 2005 approval is given to QBE Insurance (Australia) Limited to provide home warranty insurance in New South Wales.
- In September 2006, a review of Licensing in the NSW Building Industry is conducted by Ms Irene Moss following ICAC's detection of fraudulent builder licence application schemes.
- In November 2007, report of an inquiry into the NSW Home Building Service by the NSW Legislative Council.
- In November 2009 private underwriters indicate their intent to leave the HWI market in New South Wales.

2010's

- 1 July 2010, the Self-Insurance Corporation (SiCorp) of NSW Treasury commence underwriting home warranty insurance in New South Wales. SiCorp utilises agents QBE and Calliden to deliver services to builders and homeowners.

- In November 2012, a review into insolvencies in the NSW Building Industry conducted by Mr Bruce Collins is released.
- In May 2013, the Government releases a review completed into Certification conducted by Mr George Maltabarow.
- In July 2014, the NSW Government changes the name of home warranty insurance to 'home building compensation' (HBC).
- In late 2014, NSW Fair Trading is merged into the Better Regulation Office (part of the Department of Services, Technology and Innovation).
- In 2015 Owner Builders are moved from the requirements to hold HBC cover and the NSW Self Insurance Corporation changes its name to 'iCare'.
- In August 2015, IPART releases its report into Reforming Licensing in NSW.
- In October 2015, the NSW Government releases the report into a review of the *Building Professionals Act 2005* conducted by Mr Michael Lambert.
- In November 2015, the NSW Government releases a discussion paper in relation to reforms to the HBC announcing that iCare has a $398m deficiency in relation to HBC.
- In November 2016, the NSW Government announces reforms to HBC along with a return to private provision of HBC cover by both insurers and alternative indemnity providers.
- On 22 June 2017, the NSW Government passes amendments to the *Home Building Act 1989* in relation to its planned reform to HBC.
- Mid-2017, the Building Ministers Forum (BMF) agreed to commission a review assessing the effectiveness of compliance and enforcement systems for building and construction across Australia.
- In December 2017, the *Home Building Regulation 2014* is amended, and guidelines are published allowing for the commencement of the reforms to HBC on 1 January 2018.
- On 1 January 2018, Legislative reforms allowing new private providers to enter the HBC market with new product offerings commences.
- In February 2018, the BMF releases the Building Confidence report setting out the findings of a review conducted by Peter Shergold and Bronwyn Weir.
- 10 February 2019, Minister for Better Regulation, the Hon Matt Keen, MP announces the NSW Government's commitment to consolidation of building regulation in response to Shergold/Weir report.

ATTACHMENT 2

HOME WARRANTY INSURANCE IN NEW SOUTH WALES

1972

Home Warranty Insurance was first introduced in New South Wales as a government-run scheme. Its purpose was to protect consumers from loss where a builder performed faulty work, incomplete work or became insolvent.

1972 - 1987

Two insurance schemes commenced operating under the 'House Purchasers Agreement' and 'Trade Indemnity Agreement'. Both schemes were administered by the Builders Licensing Board (the Board). The House Purchasers Agreement initially provided cover of up to $40,000 for individual building work above $1,000. The Trade Indemnity Agreement initially provided cover above $200 up to $1,000 for work performed by individual tradespersons.

1987

The Board was abolished and replaced by the Building Services Corporation (BSC), which was established under the *Building Services Corporation Act 1987* (later replaced by the *Building Services Corporation Act 1989*).

March 1990

The Home Purchasers Agreement and the Trade Indemnity Agreement were replaced with the Comprehensive Insurance Scheme and the Special Insurance Scheme, established under the *Building Services Corporation Act 1989*.

Under the Comprehensive Insurance Scheme, the maximum cover for defective work was increased to $100,000 and $25,000 for incomplete work. Major structural defects were covered for seven years, and general defects for three years, from the date of substantial commencement of the building work.

The Special Insurance Scheme applied to other residential building work, being single trade or specialist trade work. The maximum level of cover was $10,000 for one year.

1992

Report by the Royal Commission into the Building Industry released (the Gyles report), which recommended a move towards private underwriting.

1993

Report by the Inquiry into the Building Services Corporation (the Dodd report) which recommended the disbanding of Building Services Corporation and a move toward private underwriting.

1995

The BSC was integrated into the Department of Fair Trading, now the Office of Fair Trading which from 2003 forms part of the Department of Commerce (now Department of Customer Services). After the State election in 1995, the Government examined the possibility of introducing an insurance scheme operated by the private sector.

Late 1996
Legislation establishing a new private scheme was passed. Under the private scheme all defects were required to be covered for seven years. The minimum cover required was increased to $200,000. This applied to both defective and incomplete work.

1 May 1997
The private Home Warranty Insurance scheme commenced.

The introduction of the scheme coincided with the disbandment of the BSC, but the Government retained responsibility for potential future claims made under the old BSC scheme.

The Government continued to administer the run-off of the closed BSC scheme through the Fair Trading Administration Corporation (FTAC). The scheme's assets were exhausted in 2002 and all claims were then funded out of the Government's consolidated fund.

Generally, no further claims were accepted after 30 April 2004. However, the *Home Building Act 1989* allowed the Commissioner for Fair Trading to exercise discretion to accept claims for an additional three years.

In the initial years following the commencement of the private scheme there were up to five insurers underwriting the market. The market was competitive and premium levels were similar to the earlier government scheme.

March 2001
The collapse of HIH created severe dislocation of the Home Warranty Insurance market. HIH had around 30–40% of the market and, in many cases; HIH offered the lowest premiums and easiest criteria for builders to obtain cover.

After the HIH collapse, significant delays were caused to builders attempting to obtain cover for new work. Some ex-HIH clients also could not meet the requirements of the remaining insurers underwriting the scheme - Royal & Sun Alliance (Vero), Dexta/Allianz and Reward.

The Government established the HIH Rescue Scheme. Consumers covered by HIH policies were indemnified by the Government, with the Rescue Scheme for Home Warranty Insurance administered by the Building Insurers' Guarantee Corporation (BIG Corp).

Early 2002
The Home Warranty Insurance market was again in turmoil with the withdrawal of certain reinsurers.

February 2002
Creation of the Consumer, Trader and Tenancy Tribunal (CTTT).

March 2002
The NSW and Victorian Governments moved to put in place arrangements for the necessary reinsurance for Allianz to continue supporting Dexta to provide Home Warranty Insurance. However, on 31 December 2002, Dexta ceased writing new business as its insurer, Allianz,

withdrew from the market. The New South Wales Government still retained certain exposures and liabilities relating to the period it provided reinsurance to Allianz.

June 2002
Report of the National Review of Home Builders Warranty Insurance and Consumer Protection (the Allen report) released.

July 2002
The *Home Building Amendment (Insurance) Act 2002* commences. The amending legislation makes fundamental changes to the home warranty scheme including:

- moving from a "first resort" to "last resort" scheme;
- cover now provided in the event of the death, insolvency or disappearance of the builder; and
- the period of cover was reduced from seven years to six years after completion of construction.

Report by the Joint Select Committee on the Quality of Buildings (the Campbell report) released.

September 2002
Report by the Legislative Council Standing Committee on Law and Justice on the *Home Building Amendment (Insurance) Act 2002*, examining the recent amendments released.

December 2002
Allianz withdraws from market.

February 2003
The launch of the NSW Home Building Service (Government's response to Campbell Inquiry) and the commencement of recruitment of building inspectors and additional investigators to provide onsite inspection and mediation services.

May 2003
Minister Della Bosca announces the Inquiry into the New South Wales Home Warranty scheme. Richard Grellman was appointed by the Governor of New South Wales to undertake the Inquiry.

July 2003
Commencement of operation of the Home Building Service dispute resolution and onsite inspection and mediation services.

October 2003
Final report of the *NSW Home Warranty Insurance Inquiry* released. The Government endorses the thrust of the principal recommendations. The Inquiry found that home warranty insurance should continue to be provided by the private sector and made seven primary recommendations for reform of the scheme to ensure its transparency and accountability as well as its accessibility and affordability to builders and the level of protection provided to homeowners.

An interim Scheme Home Warranty Insurance Scheme Board was appointed to oversee the implementation of the Inquiry's recommendations. Legal and actuarial consultants (i.e. Allens Arthur Robinson and Ernst & Young) subsequently appointed to assist with implementation project.

November 2003 – June 2004
Consultation undertaken with insurers, Insurance Council of Australia and building industry organisations in developing market practice guidelines, conditions of approval and an industry deed.

December 2003
Removal of requirement for home warranty insurance in relation to the construction of high-rise (multi storey) residential buildings (i.e. buildings with a rise of more than three storeys containing two or more dwellings).

Australian International Insurance Limited (AIIL) takes over the home warranty insurance business of Reward Insurance Limited.

May 2004
Approval given for CGU Insurance Limited (part of the IAG Group) to provide home warranty insurance in New South Wales.

September 2004
Release of market practice guidelines and amended conditions of approval for insurers to provide home warranty insurance in New South Wales. Conditions require compliance with industry guidelines including the market practice guidelines.

The guidelines address issues such as underwriting procedures, premium rates, publication of information, assessment of eligibility, service standards, reasons for decisions, outsourcing, intermediaries and complaint handling/dispute resolution.

Approval for Lumley General Insurance Limited to provide home warranty insurance in New South Wales.

October 2004 – May 2005
Consultation undertaken with insurers, Insurance Council of Australia and building industry organisations in developing claims handling guidelines, data reporting and exchange requirements.

Consultation also undertaken on a proposal that the *Home Building Regulation 2004* be amended to provide for the deemed acceptance of a claim where it has not been determined after 90 days of its receipt by an insurer as was the case in Victoria. At the time, in New South Wales, a claim was deemed to be refused if it has not been determined after 45 days of its receipt by an insurer. This triggered a right of appeal to the Consumer, Trader and Tenancy Tribunal.

Discussions were also held with the Insurance Council of Australia and the Insurance Ombudsman Service Limited in relation to complaints about home warranty insurers being handled by the Insurance Ombudsman.

December 2004

The *Home Building Amendment Act 2004* receives assent. The amending legislation includes provisions that:

- formally established the NSW Home Warranty Insurance Scheme Board to monitor the operation of the scheme and provide advice to the Minister on matters affecting the operation of the scheme;
- enabled the Minister to enter into an Industry Deed on behalf of the Government with the insurers operating in the insurance scheme;
- recognised that builders may seek insurance from more than one insurer, and, therefore, authorise and require insurers to seek and provide relevant information between themselves regarding builders; and
- authorised the Commissioner for Fair Trading to exchange relevant information about builders with insurers.

April 2005

Commencement of the licensing, discipline and compliance provisions of the *Home Building Amendment Act 2004.*

May 2005

Approval for QBE Insurance (Australia) Limited to provide home warranty insurance in New South Wales. Interest expressed by other insurers in entering the market.

2005 - 2009

Home building compensation premiums fall significantly due to strong competition amongst insurance underwriters.

May 2009

Additional trigger for lodging a HBC claim introduced for circumstances where a builder's licence had been suspended by NSW Fair Trading as a result of failing to pay a money order issued by a court or tribunal.

November 2009

Private underwriters indicate their intent to leave the HBC market

1 July 2010

The NSW Government via the Self-Insurance Corporation (SiCorp) commence underwriting of HWI in NSW. SiCorp utilising agents QBE and Calliden to deliver services to builders and homeowners.

July 2014

The name of the product is changed from home warranty insurance to 'home building compensation' (HBC)

Owner Builders are moved from the requirements to hold HBC cover.

The NSW Self Insurance Corporation changes its name to 'iCare'.

November 2015

The NSW Government releases a discussion paper in relation to reforms to the HBC announcing that iCare has a $398m deficiency in relation to HBC.

November 2016

The NSW Government announces a return to private provision of HBC cover by both insurers and alternative indemnity providers.

23 June 2017

Amendments to the Home Building Act 1989 are passed by both houses of the NSW Parliament that allow for private providers to enter the HBC market.

December 2017

The Home Building Regulation 2014 is amended, and guidelines are published allowing for the commencement of the reforms to HBC on 1 January 2018.

1 January 2018

Legislative reforms allowing new private providers to enter the HBC market with new product offerings commences.

February 2018

Australian Prudential Regulatory Authority (APRA) indicates that, despite the amendments made to *Home Building Act 1989* by the NSW Government, "Alternative Indemnity Providers" were captured by the Commonwealth's *Insurance Act 1973* and deemed insurance businesses thereby subject to regulation by APRA.

December 2019

APRA indicates that it will not provide Alternative Indemnity Providers with an exemption from the *Insurance Act 1973* as, in their view, the prudential framework established by the NSW State Insurance Regulatory Authority (SIRA) was not adequate to protection policy HBC holders.

RATIONALE

A New approach to home building compensation

BACKGROUND

When home warranty insurance was first introduced in NSW in 1972 the residential construction industry and regulatory environment was very different to what it is today.

BACKGROUND

The regulatory environment was vastly different.

Local council building inspectors did compliance inspections throughout the building process.

Banks had quantity surveyors or bank managers inspect construction stages before paying the builder progress claim payments.

1970’s and 80’s

BACKGROUND

In 1972, the regulator and provider of home warranty insurance, the Building Services Corporation (BSC), could safely assume that the regulatory environment that existed at the time was effectively reducing the risk of financial losses being suffered by home owners as a result of incomplete or defective building work.

WHAT'S DIFFERENT TODAY?

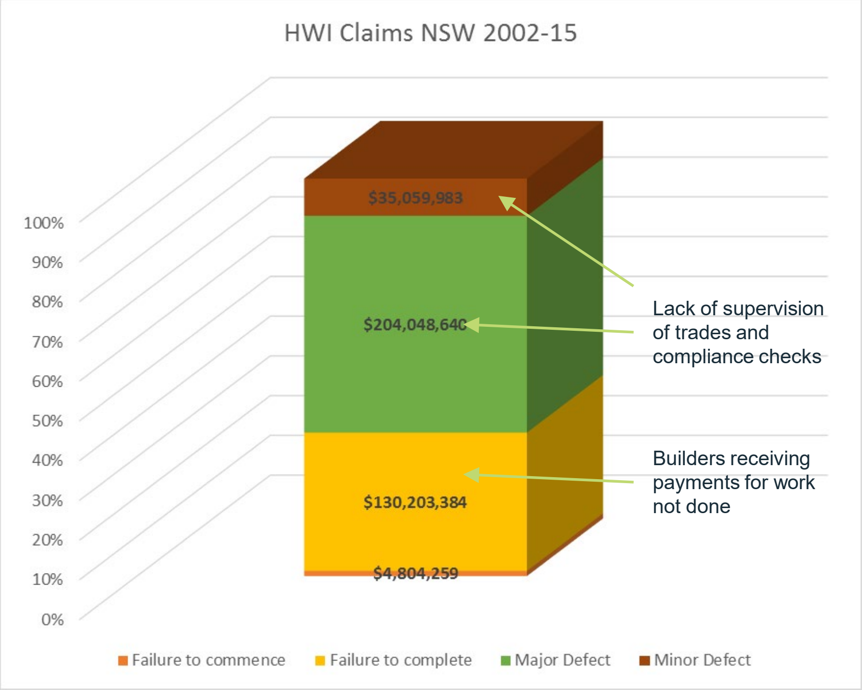
- We build vastly different homes using vastly different products and methods.
- A much greater demand for medium to high density accommodation.
- Increasing rate of new products and methods entering the market.
- Council Building Inspectors have (by and large) been replaced by Private Certifying Authorities (PCA's) who do little to no compliance inspections.
- Financial Institutions rarely carry out inspections prior to the home owner paying a builder's progress claim payment.
- A shortage of skilled sub-contractors.
- There is very little designer and engineer accountability

THE UNDERWRITING OF HWI TODAY

- Has hardly changed in 30 years
- The previous assumptions regarding the efficacy of the regulatory compliance framework no longer hold
- Substantially focused on monitoring the financial status of builders with static (point in time) reporting
- Is continuing to result in unsustainable loss ratios

WHAT'S WRONG WITH THE CURRENT APPROACH?

- Relying on assumptions that no longer hold
- Little or no mitigation of the causes of losses
- Lack of proper incentives (positive and negative) to change builder behaviour



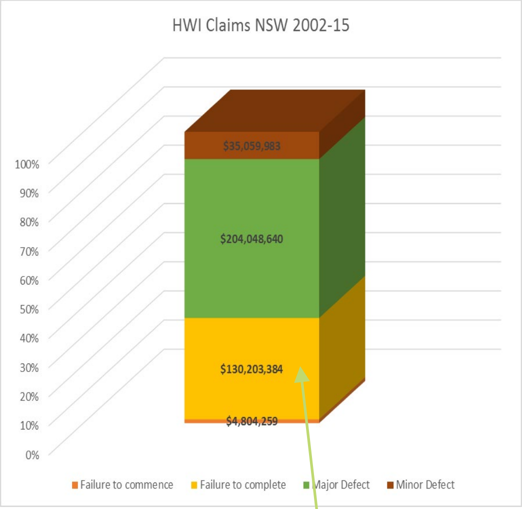
WHAT ARE THE RISKS NOT BEING MITIGATED?

(A) PROGRESS PAYMENTS

A progress payment for residential building work under a contract is authorised **only** if the progress payment is …

- a specified amount or specified percentage of the contract price; and
- that is payable following **completion;** or
- a progress payment for labour and materials in respect of work **already performed or costs already incurred**

Section 8A of the *Home Building Act 2002*



Builders receiving payments for work not done in breach of the law

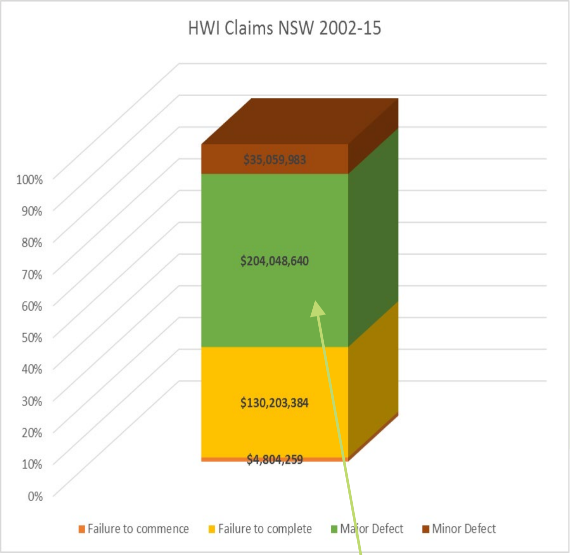
In reality the majority of builders are "contracting out" of the legislation

WHAT ARE THE RISKS NOT BEING MITIGATED? (CONT..)

(B) Major Structural Defects

As a result of:

- Builders failing to appropriately supervise sub-contractors
- Certifiers are not conducting sufficient compliance inspections
- Sub-contractors are not being held accountable

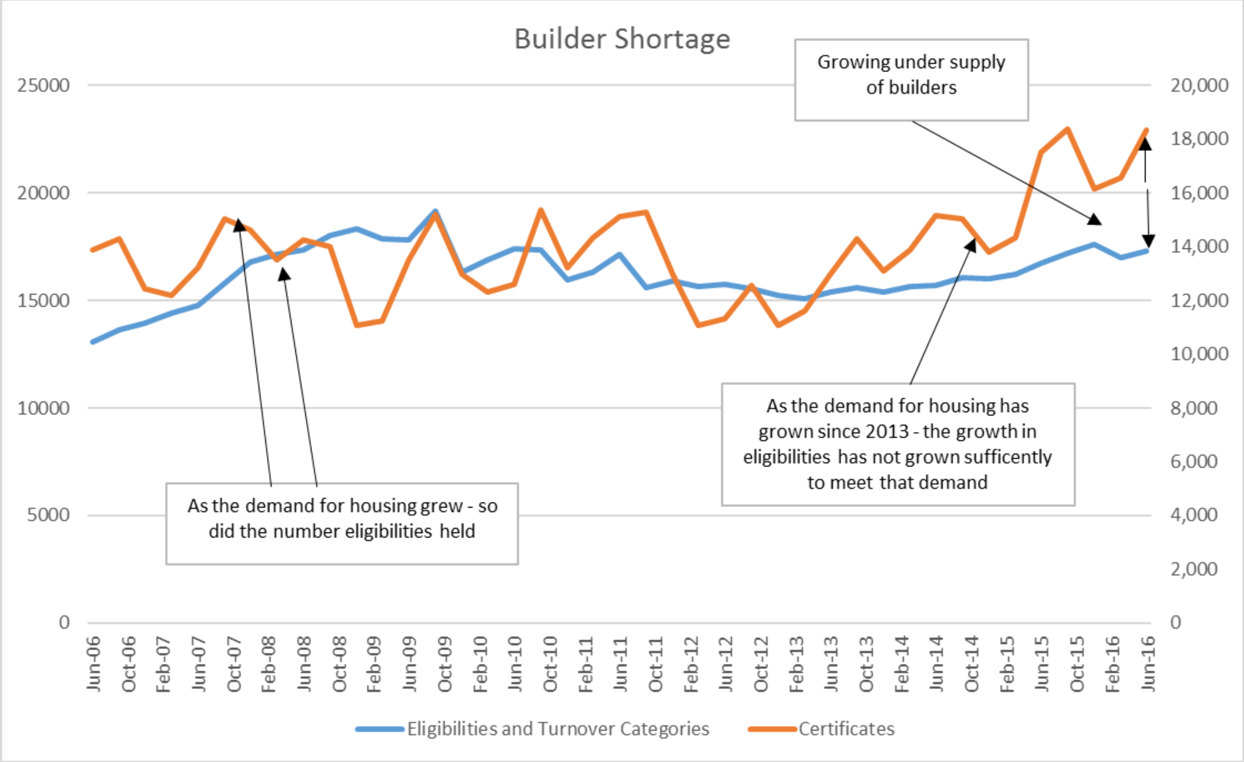


Lack of supervision of trades and compliance checks

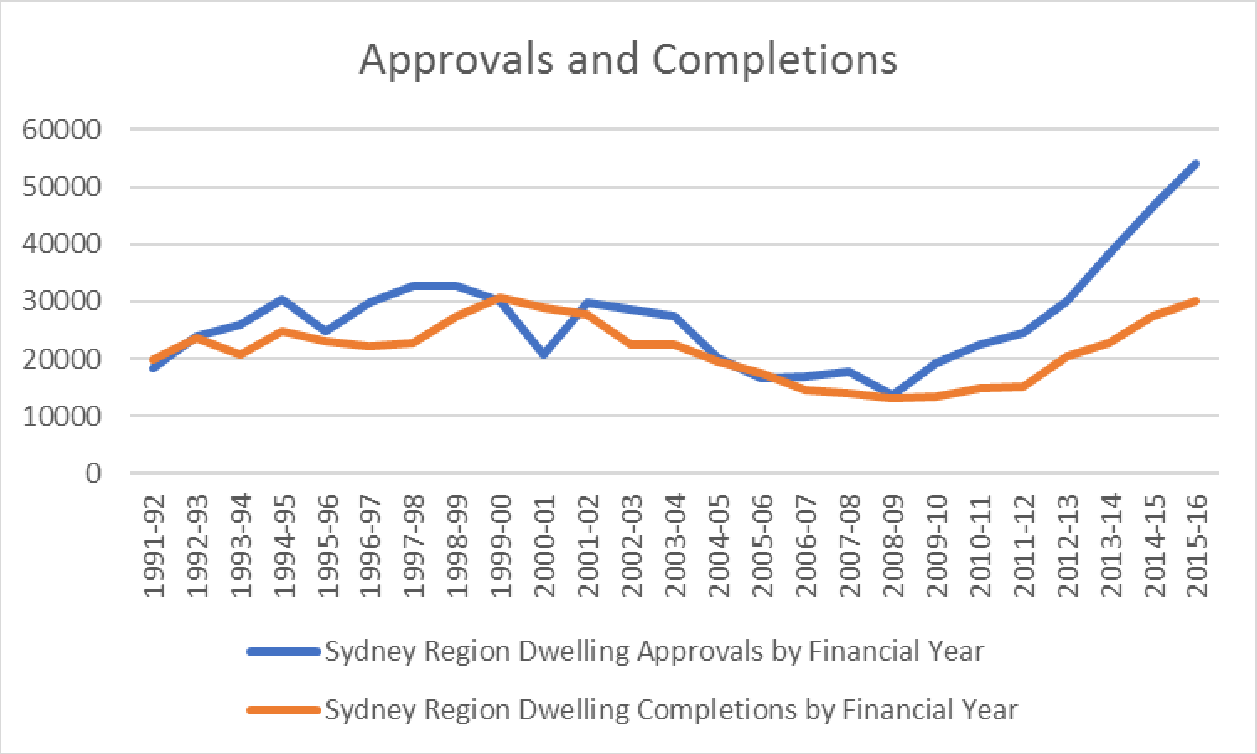
THE IMPACT OF THE CURRENT UNDERWRITING APPROACH

- The NSW HWI scheme is not sustainable ($82m loss in 2015-16 with a cumulative deficit of $375m)
- Same or worsening claims experience
- Builder’s finding it increasingly difficult to get eligibility or greater red tape requirements applied to maintain cover
- Builders view HWI as a blight on the industry
- Home owners view HWI as an unnecessary tax
- Reducing the supply of builders to the industry and impacting on the State’s capacity to meet the demand for housing

THE IMPACT OF THE CURRENT UNDERWRITING APPROACH

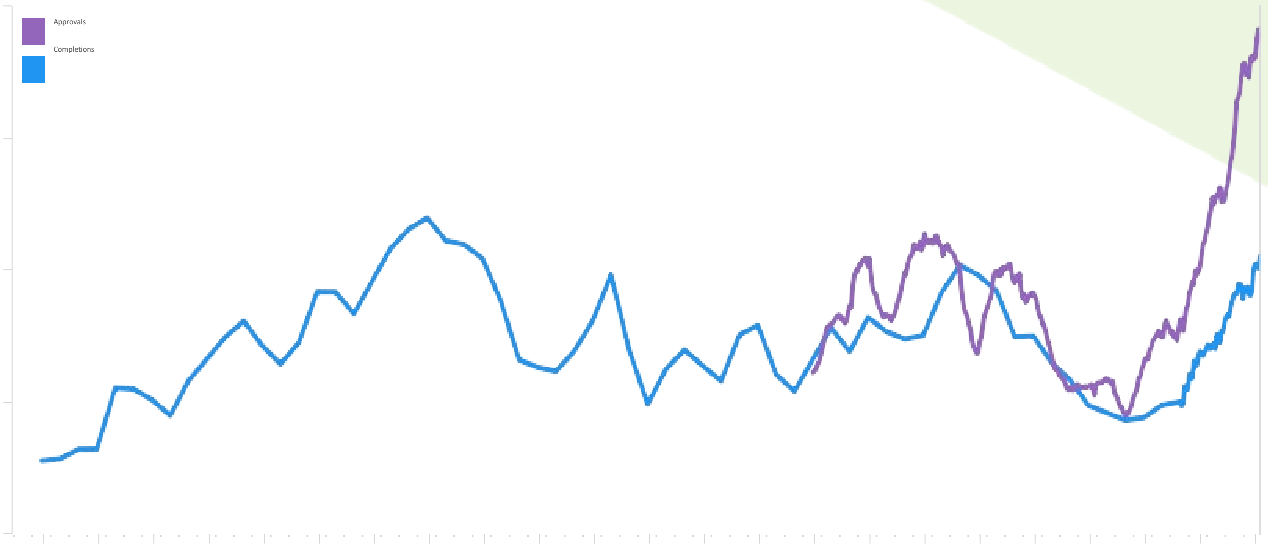


THE IMPACT OF THE CURRENT UNDERWRITING APPROACH

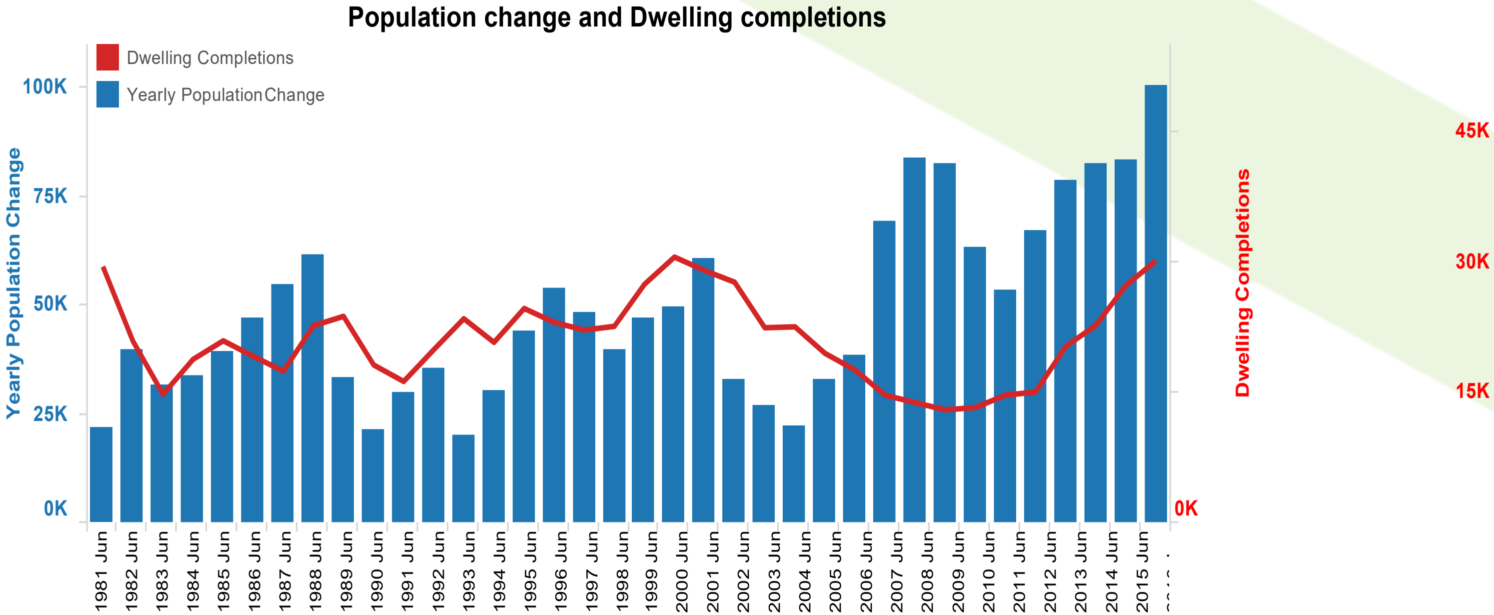


THE IMPACT OF THE CURRENT UNDERWRITING APPROACH

Sydney Approvals and Completions - Long Run



THE IMPACT OF THE CURRENT UNDERWRITING APPROACH



Date Published: ***20/12/2016***
Data Source: ***Australian Bureau of Statistics, Sydney Water Connections***

NSW GOVERNMENT | Planning & Environment

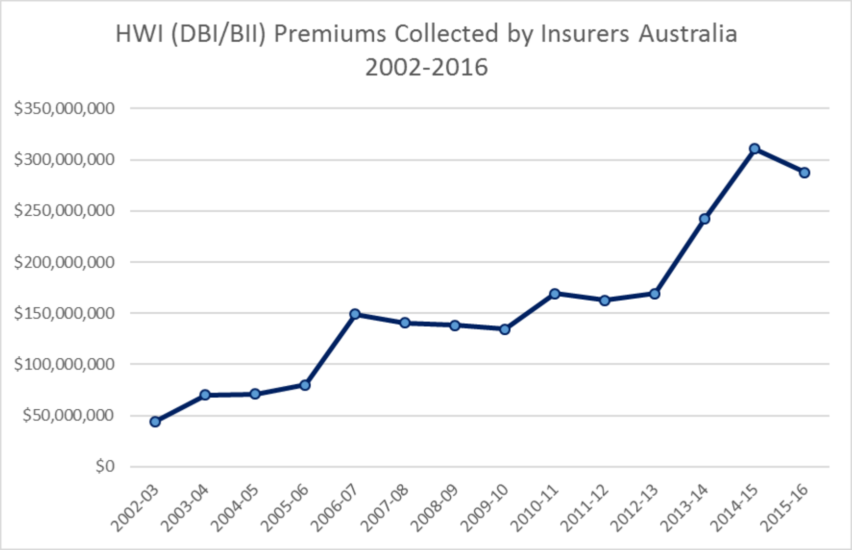
WHAT'S THE COST OF NOT TRYING NEW APPROACHES?

The cost of re-work in Australia is in the billions of dollars. Affecting Industry, Government, Builders and Home Owners...

- $66.5 billion in residential construction in Australia in 2015-16 -
- $19.6 billion in residential construction in NSW in 2015-16 -

That's lost profit to builders or alternatively home owners are paying 5 to 15% more for new homes in Australia than they should!

PREMIUM INCREASES



WHAT'S THE COST OF NOT TRYING NEW APPROACHES (cont..)?

- HWI consumer protection will be unattractive to private providers requiring the government and general taxpayers to continue to support it.
- Premiums will have to increase significantly impacting home owner decisions
- Claims experience will continue to worsen as the underlying losses suffered as a result of incomplete and defect work continue unabated
- Home owners in NSW will continue to pay inflated prices for new home and renovation construction due to the building industry's institutionalising of defect costs.
- The price for new homes and renovations will increase as the stock of builders reduces due to poor succession planning
- The demand for housing will continue to outstrip supply further impacting on housing affordability

WHAT SHOULD NEW HWI APPROACHES LOOK LIKE?

- They should not rely on old assumptions and contain risk mitigations that recognise and address weakness within the regulatory compliance framework.
- Specifically, they should:
- ensure that progress payments made to builders by home owners accord with the value of the work done; and
- Ensure that defects are detected and remedied during the course of the building process
- They should continue to provide post construction protection for 6 years
- They should be customer-centric, engage and support home owners throughout a process which is foreign to many of them
- They should be supportive of builders and contain incentives to change behaviors and produce optimal outcomes

SecureBuild

Build with confidence

The SecureBuild product case manages the home building process with home owners to significantly reduce risk

	Risk Management Strategies	NSW	VIC	QLD	UK	SecureBuild
1	Financial Assessment & Monitoring	✓	✓	✓	✓	✓
2	Revenue/Turnover Limits	✓	✓	✓	✓	✓
3	Independent Quality Assurance Inspections	✗	✗	✗	✓	✓
4	Progress Claim Payment Limits	✗	✓	✓	✓ *	✓
5	Ensuring profitable Contracts	✗	✗	✗	✗	✓
6	Progress payments monitoring & approval	✗	✗	✗	✗	✓
7	Early Dispute Resolution Services	✓	✓	✓	✓	✓
8	Contractual Relationship with Builder	✗	✗	✗	✗	✓
9	Support and Advisory Services	✗	✗	✗	✓	✓
10	Education & Awareness	✗	✗	✓	✓	✓
11	Incentive rewards for reducing risk	✗	✗	✗	✓	✓

* Managed through conveyancing

	Risk Management Strategies	NSW	VIC	QLD	UK	SecureBuild
1	Financial Assessment & Monitoring	Y	Y	Y	Y	Y
2	Revenue/Turnover Limits	Y	Y	Y	Y	Y
3	Independent Quality Assurance Inspections				Y	Y
4	Progress Claim Payment Limits		Y	Y	Y*	Y
5	Ensuring profitable Contracts				Y*	Y
6	Progress payments monitoring & approval					Y
7	Early Dispute Resolution Services	Y	Y	Y	Y	Y
8	Contractual Relationship with Builder					Y
9	Support and Advisory Services				Y	Y
10	Education & Awareness				Y	Y
11	Incentive rewards for reducing risk					Y

* Managed through conveyancing

BACKGROUND // PROBLEMS WITH EXISTING HBC

FOR BUILDERS

- HBC currently focuses solely on the builder's financials to reduce risk
- Costly and time consuming reviews of builders' financials
- Bonds, bank guarantees and securities are used tying up builders' capital
- A builder's turnover (maximum revenues) are severely restricted
- The processes for obtaining cover is complex and not easy for builders to understand (can take two to three months)
- Obtaining HBC certificates is not straight forward and takes days

FOR HOMEOWNERS

- Limited actual mitigation of real risks for homeowners
- Homeowners don't view the product as providing any tangible value
- Claims process is paper-based and inefficient (can take up to six months)
- Only 1.52% of home owners actually make a claim
- Premiums are getting more and more expensive each year (now over 1% of the contract price)
- Perceived as 'Junk Insurance' providing little value

SecureBuild
Build with confidence

SecureBuild's innovative product supports builders and homeowners throughout building process significantly delivering better outcomes, reducing risk and claims exposures

SecureBuild's Service Offering to Homeowners

SecureBuild's service offering for homeowners includes:

- Allocating an independent building inspector to support them throughout the building process who will:
    - Provide advice regarding the building process
    - Advise them when to pay their builder's progress payment claim
    - carry out defect inspections
- Quickly resolving disputes with their builder

SecureBuild
Build with confidence

Homeowners can also request additional inspections for greater peace of mind

SecureBuild's Service Offering to Builders

SecureBuild's service offering for builders includes:

- Providing access to technology for rapidly assessing their contract prices to ensure that their contracts are profitable;
- Allocating independent building inspectors to each building project to carry out defect inspections
- Advising their homeowner clients to pay their progress payment claims
- Rapid resolution of disputes

SecureBuild

Build with confidence

More services on the next slide

SecureBuild's Service Offering to Builders (cont..)

- Early identification of defects during construction and bring these to the attention of the responsible sub-contractor;
- Ensuring the builder and their subcontractors have up-to-date knowledge regarding NCC and Australia Standards requirements
- Assisting with managing post construction defect complaints or claims before NCAT.

SecureBuild
Build with confidence

Utilising proven building and construction risk mitigation strategies

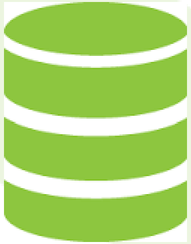
SecureBuild – How it works (cont..)

Lock-up Pre-lining

Step 2:
Review photographs received, street view or inspection outcome

360 panoramic photographs of project

Real time recording of inspections and builder/homeowner interactions



SecureBuild CRM

Step 3:
Home Owners notified to pay builder progress payment

Step 4:
Builder receives payment for work completed

Step 1:
Builder Notifies SecureBuild Inspector of stage completion

SecureBuild as an Alternative Indemnity Provider

Is not an insurance underwriter

SecureBuild

Build with confidence

Fidelity Fund

Trust Accounts

ASIC

Australian Securities & Investments Commission

NSW GOVERNMENT State Insurance Regulatory Authority

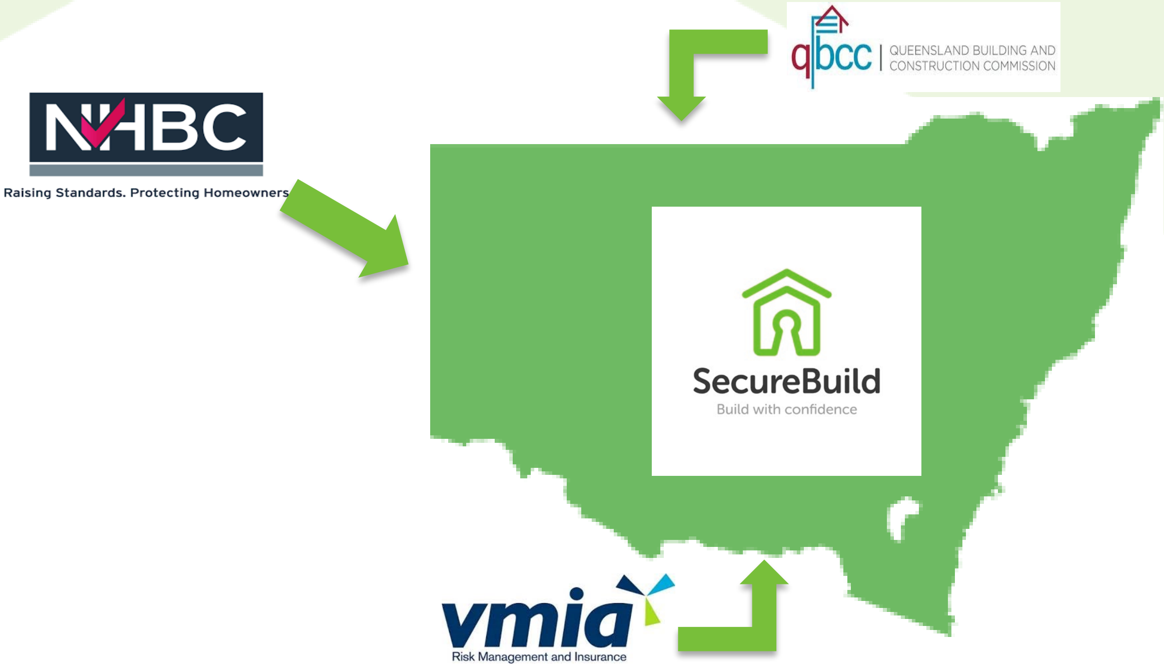
SecureBuild intends to initially enter the HBC market as an alternative indemnity provider operating a fidelity fund trust account regulated by ASIC and the NSW Government

New approach to risk mitigation

HBC schemes in other jurisdictions in Australia and the UK have achieved reasonable results in recent years

In developing its operating model and product offering, SecureBuild focused on determining the key factors primarily responsible for delivering the better outcomes in these jurisdictions.

SecureBuild's Risk Mitigation



As a result of its research, the majority of the risk mitigation activities contained within SecureBuild's operating model were adopted and/or adapted from those proven to deliver better outcomes in these jurisdictions.

How does SecureBuild's approach compare to others?

SecureBuild will be unrivalled in its innovative approach to reducing risk

icare hbcf | vmia Risk Management and Insurance | qbcc Queensland Building and Construction Commission | NHBC Raising Standards. Protecting Homeowners | SecureBuild Build with confidence

	Risk Management Strategies	NSW	VIC	QLD	UK	SecureBuild
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7	Early Dispute Resolution Services	✓	✓	✓	✓	✓
8	Contractual Relationship with Builder	✗	✗	✗	✗	✓
9	Support and Advisory Services	✗	✗	✗	✓	✓
10	Education & Awareness	✗	✗	✓	✓	✓
11	Incentive rewards for reducing risk	✗	✗	✗	✓	✓

* Managed through conveyancing

How does SecureBuild's approach compare to others?

Builder's own CPA accountable for financial verification of builder

Expert independent building inspectors to progressively inspect build progress

Progress payments approved where progress and quality are independently verified

We intervene where builder and owners are in dispute

Ensure builders are kept up to date on codes and standards

Contributions system driven by demonstrable performance of builder

	Risk Management Strategies	NSW	VIC	QLD	UK	SecureBuild
1	Financial Assessment & Monitoring	✓	✓	✓	✓	✓
2	Revenue/Turnover Limits	✓	✓	✓	✓	✓
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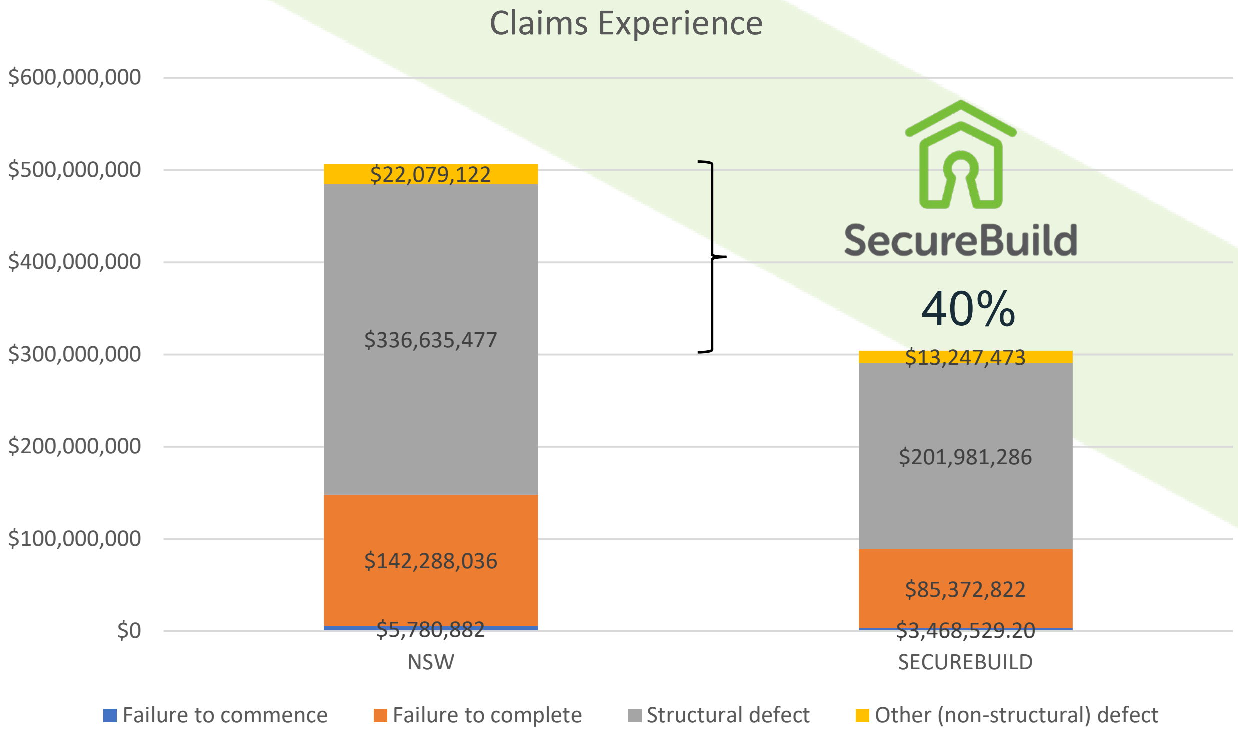
10	Education & Awareness	✗	✗	✓	✓	✓
11	Incentive rewards for reducing risk	✗	✗	✗	✓	✓

* Managed through conveyancing

Claims experience with SecureBuild approach



SecureBuild's risk mitigations and operating model are anticipated to reduce claims exposures by 40%

This has been sense-checked by comparing the NSW experience with Vic and Qld schemes that have controls that are more focused on minimising risk but not as comprehensive as SecureBuild's intended strategies

SecureBuild

Build with confidence

A new revolutionary home building compensation product

www.securebuild.com.au

Builders’ Warranty Around Australia & UK

Jurisdiction	Name of Cover	Underwriter	Cover Type	Mandatory (Y/N	Mandatory Level	Minimum Insurance Cover	Max. Pay-out fro non-completion	Max.Pay-out for defects	Duration of Cover	Risk Mitigation	Further information
NSW	Home Building Compensation (HBC)	Government (iCare)	Last Resort	Yes	$20,000	$340,000 'Construction Period' $340,000 'warranty period'	$340,000 or up to 20% of contract	$340,000	12 months from the cessation of work (incomplete 'contruction period') 6 years from completion for Structural (Major) defects 2 years for non-structural (minor) defects	Assessment of the building contractor financials; limiting turnover, limiting size of single contracts and work types	www.sira.nsw.gov.au/insurance-coverage/home-building-compensation-insurance/do-i-need-home-building-compensation-insurance
Victoria	Domestic Building Insurance (DBI)	Hybrid of Government (VMIA) & Private	Last Resort	Yes	$16,000	$300,000	20% of contract	$300,000	3 months from handover until 6 6 years from completion for structural 2 years non-structural	Assessment of the building contractor's financials; limiting turnover Prescribed restrictions in relation to the size of progress payments	www.dbi.vmia.vic.gov.au
Queensland	Home Warranty Insurance (HWI)	Government (QBCC)	First Resort	Yes	$3,300	$200,000 for incompletions and defects and $200,000 no fault subsidence	$200,000	$200,000	6 months from handover until 6.5 years from completion $200,000 no fault subsidence cover	Assessment of the building contractor's financials; limiting turnover Prescribed restrictions in relation to the size of progress payments	www.qbcc.qld.gov.au/contractor-insurance-requirements/overview
South Australia	Building Indemnity Insurance (DII)	Hybrid of Government (SAicorp) & Private	Last Resort	Yes	$12,000	$150,000	$150,000	$150,000	3 months from handover until 5 years from completion	Assessment of the building contractor's financials; limiting turnover	www.safa.sa.gov.au/SAicorp/building-indemnity-insurance
Western Australia	Home Indemnity Insurance (HII)	Government & QBE	Last Resort	Yes	$12,000	$100,000	$100,000	$100,000	6 years from completion for structural defects, 4 months for minor defects	Assessment of the building contractor's financials; limiting turnover	www.commerce.wa.gov.au/publications/home-indemnity-insurance
Tasmania	Residential Building Warranty Insurance (RBWI)	Private	Last Resort	No	$12,000	$200,000	$200,000	$200,000	6 years from completion	Assessment of the building contractor's financials; limiting turnover	
ACT	Residential Building Insurance (RBI)	Private QBE and MBA Fidelity Fund	Last Resort	Yes	$12,000	$85,000	$85,000	$85,000	5 years from completion for structural 2 years non-structural	Assessment of the building contractor's financials; limiting turnover	www.planning.act.gov.au/__data/assets/pdf_file/0011/897221/Building_in_the_ACT.pdf
Northern Territory	Residential Building Insurance (RBI)	Private	Last Resort	Yes	$12,000	$200,000	$200,000	$200,000	6 years from completion for Structural 1 Year non-structural	Assessment of the building contractor's financials Prescribed restrictions in relation to the size of progress payments	https://nt.gov.au/property/building-and-development/build-or-renovate-your- http://www.fidelityfundnt.com.au/
United Kingdom	Home Construction Warranty	Private (NHBC - Buildmark) and others	First Resort	Yes	?	$100,000	10% of contract or $100,000	Unlimited	10 years structural	Assessment of the builders financials Staged inspections of contruction Support services to building contractors	http://www.nhbc.co.uk/Homeowners/WhatdoesBuildmarkcover/

HBC OPERATING MODELS (COMPARISON)

Model	MODEL	Eligibility	Time	Outcome	HBC product Issue	Time	Risk Mitigation during construction	Post Construction	Claims & Recoveries
TRADITIONAL UNDERWRITING	Insurance Underwriting (currently underwritten by government)	1. Licensed by NSW Fair Trading 2. Financial risk assessment by outsourced provider 3. Risk assessment of company structure 4. Assessment of financials of individuals involved in building business 5. Indemnity, bond, bank guarantee, security or paid up capital requirement 6. Risk rated loading or discount	Several Weeks	• Turnover limit allocated • Job specific limits allocated • Participation in BCRP • Risk rating of builder (discount or loadings to premiums)	(A) Premium Pricing • Build Type (C01 to C09) • Location (Metro/Regional) • Discount/Loading depending upon risk rating (B) Contract Assessment Only in relation to specific architect design projects or multi-dwelling applications (C) Issued • HBC project certificate • Policy document	2 to 3 days	Nil for majority However, Builder Contractor Review Program (BCRP) for some new and small/medium builders Periodic reviews of financials	Nil by HBC provider. However, Fair Trading and NCAT available to assist homeowners to enforce their statutory warranty rights	• 'Trigger' events to enable a claim to be lodged • Outsourced providers undertake loss adjustment and claims management • Minimal scope for 3rd party recovery action
SECUREBUILD	**(1)** Alternative Indemnity Provider (AIP) operating a fidelity fund approved and regulated by SIRA Membership scheme (discretionary management fund) with Trust Deed regulated by ASIC Or **(2)** Outsourced agency for existing insurance underwriter	1. Licensed by NSW Fair Trading 2. Financial position verified by an appropriate accountant prior to the granting of eligibility and periodically thereafter in accordance with SecureBuild's Minimum Financial requirements 3. Non-financial risk assessment 4. Building contractors acceptance of SecureBuild's membership terms & conditions **5.** Risk rating determine member benefits and level of support and supervision of building contractor	20 Minutes following acceptance of registration	• Turnover category (limit) allocated • Member status level	(A) Contribution Pricing • Build Type (C01 to C09) • Location (Metro/Regional) • Rebate depending upon member status (B) Contract Assessment • Evaluation of contract price (value) • Setting of appropriate progress claim payments under the building contract (C) Issued • Evidence of Cover certificate • Fidelity Fund Contract • Brochure regarding inspection & payment services • Details of the building inspector allocated to oversee the project	Immediate upon payment by members	• Inspections by highly-qualified building inspectors • Approval of progress claim payments upon satisfactory completion of project stages • Resolution of misunderstandings/disputes between building contractors and homeowners	Dispute resolution services to homeowners utilising member terms & conditions to assist homeowners enforce their statutory warranty rights without recourse to formal processes No cost to homeowners.	• 'Trigger' events to enable a claim to be lodged • Loss adjustment undertaken by building inspector involved in the building process (non-completion). • To avoid a potential conflict of interest a different building inspector is used to do loss adjustment in relation to defect claims • In relation to non-completion claims potential recovery action against the PI of the Accountant who certified the building contractors' financials; • Defect claim recovery against PI of building inspector

Comparison		• Adoption of QBCC approach to financial assessment of the building contractor:
		  ○ Negates costly assessments by outsourced provider(s)
		  ○ Significantly reduces eligibility application timeframes; and
		  ○ Provides an additional cost recovery target
		• Building contractor acceptance of membership terms & conditions create a legal contract requiring the contractor to comply with risk mitigation requirements
		• Member benefits provide meaningful rewards for risk lowering behaviours of building contractor
		• Support and supervision of building contractor reduces risk of insolvency and defective building work
			Technology platform developed by SecureBuild allows it to:
			○ verify licensing and other assessment information via AIP connections to existing systems (e.g. OneGov);
			○ online eligibility applications by contractor or broker ensuring all required information is received to determine eligibility
				Instead of placing restrictions of the value of any single contract or type of building work the building contractor can undertake, SecureBuild mitigates the risks presented by these factors by applying a higher level of scrutiny of the contract and building process	An assessment of the contract value is carried out prior to issuing an HBC certificate (majority via automated processes) to ensure that the building contract to be entered into is likely to produce a profit for the building contractor is an essential factor in preventing the insolvency of the building contractor.
					
					SecureBuild had developed an AIP connection with Cordell (RPData) construction cost estimator tool will allows SecureBuild's system to check the appropriateness of the building contractors quoted contract price.
					
					It is a membership term & condition that the building contractor adjust their contract price to the level agreed to with SecureBuild.
					
					Homeowner is provided with information regarding SecureBuild's support services and introduced to their building inspector who will support them throughout the build
						Technology platform developed by SecureBuild allows building contractors or their brokers to apply for HBC certificates online and for the builder and their homeowner client to immediately receive policy and other documentation.
						
						SecureBuild building inspector contacts homeowners to confirm services provided and processes to be followed throughout the build
							• Throughout the building process the building inspector confirms satisfactory completion of each stage of the build.
							• Where defect or incomplete work are detected, the builder and homeowner are provided with a report setting out the list of defects or incomplete work
							• Where there are no defects or incomplete work are present the homeowner is advised to pay the building contractors progress claim
							• SecureBuild has develop a technology platform that allows its inspectors to provide reports to homeowner and builders whilst still on site
							• During inspections SecureBuild's building inspectors will provide advice and guidance to the builder and their trade contractors on compliance with the NCC and Australian Standards
							• During inspections building inspectors will:
							  ○ liaise with trade contractors and suppliers to glean intelligence; and
							  ○ monitor the speed of completion of projects by building contractors
							to determine whether the builder's financial circumstances have changed
								• Using the membership terms & conditions SecureBuild will be in a position to assist homeowners enforce their statutory warranty rights against the building contractor
								• Conversely, the project data and information collected by SecureBuild can assist the building contractor defend a spurious claim that could lead to insolvency
									• Use of building inspectors in loss adjustment process significantly reduces claims costs and assessment timeframes

Rating		**Superior**	**Superior**	**Similar**	**Superior**	**Superior**	**Superior**	**Similar**	**Superior**