

Trade Practices Commission's Final Report - Home Building - Consumer Problems And Solutions

With the kind permission of the Trade Practices Commission, the Executive Summary from the TPC Final Report "Home Building - Consumer Problems and Solutions" is set out below.

Executive Summary

The Trade Practices Commission's direct experience of the home building industry convinced it some time ago of the need for a national approach to the problems besetting it. It took widely publicised court action in the late 1980s against home builders in Western Australia, Queensland and New South Wales alleging unconscionable and misleading and deceptive conduct.

Litigation is always costly and protracted and does not always produce the most effective remedies and results. In the cases against the Kimberley, Mansard and Manfal groups the Commission had hoped to achieve not only redress for consumers directly affected but significant industry-wide deterrent effect. That wider expectation was not realised. The Commission and other consumer protection agencies continue to receive a steady stream of complaints about business practices of many house builders. The most common problems are still alleged misleading and deceptive conduct and unconscionable conduct. (As recently as September 1993 the Commission instituted proceedings against two New South Wales building companies.)

Rather than continue to attempt to resolve issues on a case by case basis, the Commission set out to identify the underlying cause of the problems Australia-wide as the first step toward developing real long term solutions.

Put briefly, the Commission's review of the industry (like individual State inquiries before it) isolated numerous areas for reform, of which the main ones are:

- contracts that consumers and many builders simply do not understand and that are also biased in builders' favour;
- significant construction delays and substantial increases in price during the life of contracts;
- the failure of existing dispute resolution mechanisms to provide inexpensive, fair and quick resolution of disputes;
- inadequate insurance cover; and
- poor performance and reputation of many of the regulatory agencies.

The Commission's conclusions and recommendations are aimed at better equipping consumers to deal with the transaction through all its stages - selection of the builder, negotiation of the contract, and dealing with unexpected setbacks and disputes if they arise. The Commission firmly believes that ethical builders will also benefit from

reforms which lead to reductions in uncertainty, tension and dispute in builder-client relationships.

The Commission recognises that Australia's Federal system makes the adoption of a single national solution difficult. Individual States and Territories will no doubt adopt the model they feel best suits local circumstances. However, this should not preclude adoption of a national approach to problems which are remarkably similar Australia-wide.

In finalising its report on the industry the Commission has found considerable support for this view and for the specific recommendations that flow from it.

A national approach requires broad agreement on several things, in particular:

- what the problems are;
- what causes them;
- what past policies and practices have failed; and
- what reforms have worked - ie what is current best practice in the approach to the problem areas.

One compelling reason for proposing a national strategy is that the industry itself is nationally organised, while representation of consumers' interests is very fragmented and lacks organisation. Agreement between Governments on the key issues would be a big step toward addressing the imbalance in bargaining platforms in the industry.

In any event, it is necessary for the industry to participate in this program of reform - to be part of the national approach. The evidence is that much of it at least is ready to do so - if only because of the recognition that lack of public confidence in existing arrangements works to nobody's advantage.

Contracts

Throughout the Commission's inquiries it was apparent that confusion about contract terms is a major source of disputes. The evidence is that builders themselves are often confused when disputes arise, and would be more so without the back-up of their associations.

One of the problems highlighted during the Kimberley Homes investigation was consumers' belief that they had no right to negotiate variations to the contract - and the fact that their solicitors did nothing to put them straight on this.

The two fundamental and closely inter-related problems with the contracts most commonly in use at present are comprehensibility and content.

Comprehensibility

The transaction between builder and owner is intrinsically complex and intrinsically vulnerable to upset as a result of usually unforeseen circumstances - for example bad weather, labour or materials shortage, unexpected adverse site conditions and the like.

It is obviously vital that both builder and owner enter the transaction with their eyes open and with all cards on the table. That cannot happen without a contract which is a clear and unambiguous formal statement of what has been agreed between them.

That requires, among other things, the elimination as far as possible of legalese and technical terms - and where that is not possible, the explanation of such terms in the body of the contract itself and in supporting material. Ideally that material would include a checklist for owners to sign in confirmation that they had read and understood the documents signed.

The Commission believes that development of a plain language standard form contract is the essential cornerstone of genuine reform in the industry. It welcomes the industry's initial steps in this direction.

Content

Plain language and comprehensibility are of course only half the story. Content and fairness are obviously equally important. Key issues are:

1. **Contract price** - this should be prominently stated together with a clear warning and explanation of the factors which might cause it to rise, in particular provisional sums and prime cost items and site access problems.
2. **Right to terminate** - the circumstances in which either party may terminate needs to be spelled out. Neither side should be forced to bear the burden of a contract for which they either cannot pay or will not be paid. There is room for debate about what threshold variations in price or completion time should trigger the right.
3. **Plans and specifications** - the Commission believes that mandatory attachment of plans and specifications to the contract would help reduce disagreements about performance.
4. **Mandatory arbitration clauses** should be eliminated.

Dispute resolution

Dispute resolution is a major problem in the industry. Existing avenues are clumsy and potentially financially ruinous for both parties to a building contract. One industry source informed the Commission that most builders will not use the existing mechanisms to pursue outstanding payments of less than \$10,000.

The Commission's inquiry found general agreement that arbitration in particular has failed because:

1. It can take as long and cost as much as going to Court.
2. Rightly or wrongly it is widely seen as inherently biased against consumers because arbitrators are nominated by the industry.

The Commission acknowledges that there may be a role for a modified form of arbitration - but strongly believes that mandatory arbitration clauses unnecessarily restrict the options available and that they should be void.

The Commission recommends that each State/Territory set up a disputes tribunal modelled on (without necessarily copying completely) Queensland's tribunal.

Ideally, the following should be features of the Tribunal and its operation:

- no monetary limit on the tribunal's jurisdiction;
- procedural flexibility;
- a commitment to pre-hearing mediation (which in Queensland seems to result in a large proportion of disputes being settled without a hearing);
- enforceability of dispute settlements; and
- formal arrangements to ensure that consumers are aware of the existence and functions of the tribunal - and how and when to approach it.

The Chairman of the Queensland Tribunal has suggested piloting a scheme to attach a duty lawyer to the Tribunal to give disputants professional and impartial legal advice about how to conduct their case. The Commission is very much in favour of incorporating such a service in the proposed tribunal.

Information and education

As is the case in many markets, the Commission found that many consumer problems in the building market stem from, or include, information deficiencies. They are, in particular, a large component of the problems with existing forms of contract.

Most consumers enter building contracts with no technical knowledge or experience of the process and scant understanding of their rights and obligations at law. The Commission believes that some of the building industry associations, which provide a variety of services for their members, rather underestimate the disadvantages consumers face in having no corresponding support.

The establishment of an adequately resourced, inexpensive consumer building advisory service should be a priority in all States/Territories. The service should be independent of licensing or other regulatory bodies, insurance providers and industry associations. Its existence should, of course, be widely advertised.

It should provide simply-expressed information on:

- **contracts** - including a discussion of the contract price and its potential to increase, and of termination rights;
- **insurance and warranties**;
- **dispute resolution options**;
- **regulatory agencies** and their functions; and
- the role of **local government inspectors**.

Insurance

Arrangements vary widely at present - some jurisdictions have statutory schemes and some private funds, while in Tasmania no cover is available at all. Most schemes have maximum claim ceilings around \$50,000. Even the New South Wales maximum of \$100,000 is fast

becoming unrealistic in view of actual building costs.

The Commission believes that:

- there should be compulsory insurance cover up to \$200,000 in all jurisdictions, with optional 'gap' insurance available where the contract price is higher than that;
- owners should be given plain English information about the insurance cover before they enter the building contract;
- insurance contracts should provide for ex gratia payments in genuine cases of hardship; and
- insurance claim decisions should be reviewable by the proposed disputes tribunal.

The Commission is opposed to a monopoly of the building insurance market, statutory or otherwise, and strongly recommends opening the market up to full private sector competition.

Conclusion

The Commission's proposed reforms have been devised as an integrated package. While their implementation in any one of the various areas would bring some improvement, it is necessary that reform take place across the board.

To illustrate:

- The adoption of plain language contracts would be a somewhat illusory gain if the terms and conditions remained biased toward builders.
- Similarly, consumer advice about insurance would be of limited use if cover were restricted and/or there were no competition.
- Building an effective disputes resolution mechanism is pointless if people do not know, or cannot find out, about it.
- Directories of licensed builders are of limited use if they contain no information about individual 'track records'.

Summary of recommendations

Contracts

- It should be a formal requirement that all home building contracts be written and contain basic elements and comply with formalities. A copy should be provided to the owner on execution.
- Contracts should be written in plain language, clearly explaining all terms and conditions, including time for completion of the work. They should include a detailed description of the work, plans and specifications.
- The contract price should be as firm as possible and prominently displayed at the beginning of the contract. It should include all known costs to be borne by the consumer.
- The statement of contract price should be accompanied by a clear warning of the possibility of price variations and an explanation of their potential impact on the final price.

Warranties

- All State/Territory jurisdictions should legis-

late to imply building (sic) specific statutory warranties into domestic building contracts.

- Such warranties should be enforceable against the builder and insurance schemes.

Dispute resolution

- Mandatory arbitration clauses should be prohibited.
- Each State/Territory jurisdiction should establish a Building Disputes Tribunal to decide home building disputes which cannot be resolved by direct negotiation or mediation.

Insurance

- Compulsory insurance cover of up to \$200,000 (indexed for inflation) should be available in all jurisdictions. Where the contract price exceeds \$200,000 'gap insurance' should be available.
- Owners should be given detailed 'plain English' information about the relevant insurance cover prior to entering the contract.
- Insurance contracts should provide for the payment of ex gratia payments in cases of hardship.
- Insurance claim decisions should be reviewable by the proposed Building Disputes Tribunal.

Licensing and registration

- A register should be kept of all builders.
- Registration should be based on a national competency standard for which suitable accredited training courses should be available.
- Builders should be deregistered on evidence of dishonesty, insolvency or poor work performance.
- There should be provisions to prevent deregistered builders from setting up business by other means, eg through a company.

Education and information

All States/Territories should give priority to the establishment of a consumer advisory service to provide information about:

- contracts;
- insurance and warranties; and
- dispute resolution options.
- Local government bodies, perhaps in cooperation with building industry regulatory agencies, should provide consumer information clarifying the role of local government in the home building industry.
- This information should make it clear that inspections to assess conformity with regulations are not concerned with issues of workmanship as such.
- A program should be established to educate solicitors and other advisers about builders' and consumers' rights and obligations under home building contracts.