Performance of Victoria’s Domestic Building Insurance Scheme 2012-2013

November 2013

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ESSENTIAL SERVICES COMMISSION

PERFORMANCE OF VICTORIA'S DOMESTIC BUILDING INSURANCE SCHEME 2012-2013

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CONTENTS

EXECUTIVE SUMMARY

This is the Essential Services Commission's third annual report on the performance of Victoria's domestic building insurance (DBI) scheme. The DBI market has undergone significant change since this mandatory insurance scheme was introduced in 2002, and reforms to domestic building consumer protection, announced by the Victorian Government in 2013, are likely to have implications for the performance of the DBI scheme in the years ahead.

DBI (which is also known as builders' warranty insurance) is taken out by builders and compensates a home-owner for losses resulting from non-completion or defects in domestic building work where the builder cannot be pursued directly because they have died, disappeared, or become insolvent. It is compulsory for all domestic construction contracts over $12 000 in value.

When the current scheme was first introduced in 2002, the market was served by five competing private sector insurers. From 2009, all but one of these insurers started to leave the market (although they remain liable for claims against the policies they wrote before their exit from the scheme). In response to this development, and following an official mandate issued by the Victorian Government in March 2010, the Victorian Managed Insurance Authority (VMIA) began offering DBI.

Within this context, the Commission has terms of reference to report annually on the performance of Victoria's DBI scheme, covering the number of eligible builders; the number of project certificates (policies); premium levels; and the number and amounts of claims. In examining each of these areas, the Commission collects quarterly data from insurers. This data is not audited and the Commission relies on insurers providing accurate data.

This latest performance report covers the period up to 30 June 2013.

One of the key features of DBI is that it is a long-tail insurance scheme, which means that claims come in over a long period of time (up to ten years) after the issuing of the policy. Because of this, insurers must forecast the sufficiency of premiums collected in one year to meet the cost of claims incurred in future years, and to assess if their product is financially viable.

A key measure of DBI scheme performance is the simple loss ratio, which shows the cost of claims as a percentage of the premium collected. The Commission's updated data reveal that, between 2006 and 2009, premium revenue was not increasing at the same rate as the number of project certificates being issued. A period of premium discounting was taking place between the private sector insurers operating in the DBI market at the time as they fought for market share. The period of premium discounting coincided with an increase in claims and precipitated the exit of all but one of the private sector insurers from the market. For policies issued in 2008, which marks the onset of the global financial crisis, the updated data indicate that claim costs have reached 70 per cent of premium reserves, higher than any other year.

Calliden and VMIA are currently the only two insurers offering DBI in Victoria, with the latter having the vast majority of the market. Under the current arrangements, DBI eligibility with an insurer is a pre-requisite to a builder's registration. VMIA and Calliden both use turnover limits to protect against over-exposure to builders at risk of insolvency.

Because DBI is currently mandatory, the number of project certificates issued is an indication of the overall level of activity in the Victorian domestic building market. After peaking at just over 62 400 in 2010, the total number of certificates issued has fallen annually, a trend that seems set to continue in 2013 based on the data collected for the first half of the year. Project certificates for new dwellings account for the largest share of total DBI project certificates issued and the premium pool.

And there appears to be some concentration in the issuing of projects certificates. There are almost 20 000 individually registered builders in Victoria, but large building companies are responsible for the majority of domestic building contracts.

Premiums charged for DBI differ according to project type, builder risk rating and project size (value). Since the withdrawal of most private sector insurers in 2009, DBI premiums have risen. Indeed, the average cost of a project certificate is more than 60 per cent higher than it was when premiums were at their lowest in 2008, although premiums have been relatively stable since VMIA issued a revised premium schedule in July 2011.[1] The long-tail nature of the DBI scheme means that it is difficult to present claim numbers in their true context until at least six years after the issue date of project certificates. Nevertheless, it appears that claims are relatively infrequent in relation to the number of project certificates issued. The revised data show that 4 506 claims have been lodged (with 3 151 of these claims accepted) since the DBI scheme commenced in 2002. Nevertheless, there are signs that the frequency of DBI claims is rising. Each claim represents a major inconvenience for customers who suffer from defective building work and the stress of trying to locate their builder. Claims are complicated for insurers to manage, and can take a long time to finalise due to the technical nature of the investigations and repairs. Insolvency is by far the most common reason that

[1] In its *Domestic Building Insurance Premium Validation Review*, released in May 2013, the Commission concluded that VMIA's premiums: (i) are sufficient to cover its expenses, risks and long-term claims costs; and (ii) are not set above the level required by the VMIA to cover its expenses and the risks and long-term claims costs.

claims on DBI are made, and almost half the claims received related to a structural defect.

The average cost of a DBI claim for work undertaken by a registered builder is around $33 000 (although this falls to under $29 000 when the figures are adjusted for claims relating to multiple properties, such as common property defects in multi-unit developments). Claims for failure to complete are the most costly to insurers, making up around one third of all finalised claims costs.

The time it takes for a claim to go through each stage of the claim process can be used to examine how the scheme is operating in general and may give an indication of how well consumers are being served. Since the scheme started in 2002, the average time between receiving a notification and a claim being finalised is 356 days, or about twelve months.

REFORMS TO DBI

The Victorian Government has announced a number of reforms to the building industry and arrangements for domestic building consumer protection, which will be implemented during 2013 and 2014. (See Appendix D for a summary of the reforms).

The reforms will broaden domestic building insurance beyond last resort insurance and will introduce additional triggers alongside the current criteria. Domestic building insurance will be triggered where a project is incomplete, or there is a defect, and the builder or building entity has died, disappeared or become insolvent (this is the current criteria and is known collectively as DDI);

- the Victorian Building Authority has certified that a rectification order has not been complied with by the builder;
- the builder or building entity has been partially suspended, suspended or de-registered and thus cannot complete the project; or
- is certified as being significantly and permanently incapacitated.

The reforms also include the removal of compulsory eligibility for DBI as a necessary pre-condition of registration for domestic builders. However the purchase of DBI before a builder commences a domestic building project, remains a mandatory requirement.

The standard excess for a DBI claim is on a sliding scale between $500 and $1 000 depending on the time since completion of the building work. This will be changed to be $1 500 (and indexed to reflect increases in building costs) in all cases under the reforms.

The reforms provide insurers with more scope to pursue builders and recoup costs of claims, because builders will be required to disclose whether they are acting as an agent of a financial vehicle, such as a family trust, where it would be difficult to pursue recovery actions. In the past, builders who had been declared DDI could re-register under a new entity and resume trading. With changes to registration practices, this practice will not be possible unless a builder has reimbursed their insurer for DBI claims.

The effects of these reforms will be reflected in future DBI performance reports prepared by the Commission.

GLOSSARY

Building Commission	A statutory authority that oversees the building control system in Victoria.
Building Practitioners Board	The licensing arm of the Building Commission.
Claims liability	The cost of a claim to an insurer. This includes money paid out as well as estimates of future costs.
Died, disappeared or insolvent (DDI)	The three triggers for Victoria's DBI scheme.
Domestic building insurance (DBI)	A mandatory insurance that compensates home-owners for non-completion or defect where the builder is unable to rectify the works because they have died, disappeared or become insolvent (also referred to as Builders Warranty Insurance).
Eligibility	Pre-approval from an insurer for a builder to be issued project certificates.
First resort	An insurance scheme that provides compensation regardless of the builder's circumstances (as opposed to a last resort scheme).
Investment returns	The revenue earned by an insurer by investing premium revenue.
Last resort	An insurance scheme where compensation is only available where all other avenues for resolution have been exhausted
Liability period	The period of time that an insurer is liable for claims on a policy.

Long-tail insurance	Insurance products where the full cost of claims is not known for a long time after the premium is charged.
Owner-builder	A person who constructs or renovates a domestic building on his or her own land, who is not in the business of building.
Policy	For owner-builders, DBI coverage is issued in the form of a policy. Owner-builders are only required to take out a policy if they sell the property within six and a half years of completion.
Premium	The charge for insurance coverage.
Private insurers	Independently trading insurance companies that compete in the market. Generally they are publicly listed entities, trading for profit.
Project certificate	For registered builders, DBI coverage is issued in the form of a project certificate that is specific to the domestic building work undertaken in a domestic building contract.
Rectification Order	A binding order issued by the VBA requiring the performance of building work; the payment of money to the builder, or into a trust account for release upon completion of work.
Run-off period	The time after an insurer has stopped issuing insurance, but is still responsible for claims on existing policies.
Simple loss ratio	Net incurred costs relating to claims made on project certificates issued in a year, divided by the total premium earned for that year. Excludes the costs of claims that are yet to be made. Excludes costs that the insurer incurs in administering the scheme or income from investments.
Turnover limit	An insurer's calculation of a builder's capacity to undertake work. This is the total value of construction work that an insurer will issue certificates for in a 12 month

	period.
Victorian Building Authority (VBA)	A newly formed integrated regulator responsible for building, plumbing, consumer interests and architecture. The VBA replaces the Building Commission, the Plumbing Industry Commission and the Architects Registration Board of Victoria.
Victorian Managed Insurance Authority (VMIA)	A statutory body which operates as the 'captive insurer' for the State of Victoria.

1 INTRODUCTION

This introduction aims to provide the basic background and vocabulary needed to understand this report. Abbreviations and terms included in the glossary are highlighted in bold and italics.

DBI compensates a home-owner for losses resulting from non-completion or defects in domestic building work where the builder cannot be pursued directly for redress because they have died, disappeared, or become insolvent. These three triggers are collectively abbreviated as ***DDI***. DBI is known as a ***last resort*** insurance scheme as it is only available where all other avenues for resolution have been exhausted. A ***first resort*** scheme provides compensation for defects even if the builder is still trading (such as the Queensland Home Warranty Scheme administered by the Building Services Authority — see appendix C).

In March this year, the Victorian Government announced a reform strategy for consumer protection in the domestic building industry, including the establishment of a new regulator, the ***Victorian Building Authority (VBA)***. The implementation of these reforms will take place during 2013 and 2014, and will have implications for all aspects of DBI. Notably, three new triggers for a DBI claim will be added to the standard policy. In addition to ***DDI***, a claim can be made where: a builder has not complied with a ***rectification order***, the builder's registration with the VBA has been suspended or cancelled, the builder is certified as permanently or significantly incapacitated.

1.2 ELIGIBILITY

Currently, all builders are required to have ***eligibility*** with a DBI insurer in order to maintain their registration with the ***Building Practitioners Board*** (BPB). Eligibility is like pre-approval from an insurer to take out DBI ***project certificates***. Insurers use the eligibility process to evaluate the financial position of the builder and impose an annual ***turnover limit***, which is their assessment of the maximum value of building projects the builder can take on without risking insolvency.

Under the reforms to the regulation of the building industry announced in March this year, the requirement for compulsory eligibility will be removed. However this does not change the mandatory requirement for a builder to purchase DBI insurance before commencing a domestic building project.

1.3 PROJECT CERTIFICATES AND PREMIUM

In Victoria, DBI cover is compulsory for all domestic building works with a contract value over $12 000. When a contract for the work has been agreed, the builder takes out a DBI policy known as a ***project certificate*** on behalf of the customer. The project certificate is specific to the work in the associated contract. A ***premium*** is calculated by the insurer based on the contract value, and is paid by the builder.

Under the reforms to DBI announced in March this year, the minimum contract value for which DBI is compulsory will be raised to $16,000 and will be indexed annually.

1.4 OWNER-BUILDER POLICIES

A home-owner is legally allowed to undertake building work on their property as an ***owner-builder*** subject to certain regulatory requirements. Owner-builders are not registered builders, and must obtain consent from the ***Building Commission*** to do any work with a value over $12 000. Owner-builders do not require DBI to commence work, but must take out a policy to cover defects if they sell the property within six and a half years of completion. DBI cover for owner-builders is referred to as a ***policy*** rather than a project certificate.

1.5 CLAIMS

DBI covers a home-owner for defects that occur up to 6 years from the completion of the building project.[1] DBI is referred to as ***long-tail insurance*** because of the length of time faced by insurers between charging a premium and knowing the full cost of claims. This is distinct from home contents policies or car insurance where premiums are calculated annually and the ***claims liability*** is generally known within a few months of the year's end. Insurers earn ***investment returns*** on the premium pool while they wait to pay out claims. In long-tail insurance this revenue can be significant over the years it takes for claims to occur.

The period of time that insurers must consider claims against a policy is known as the ***liability period***.[2] For its analysis, the Commission assumes that construction is

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[1] Claims for 'failure to commence' or 'failure to complete' can be made if the builder is DDI before the project is completed.

[2] In some circumstances, a home-owner can make a claim after the liability period has expired (s.54, *Insurance Contracts Act 1984* (Cth)).

complete 12 months after the certificate issue date, but the construction of a domestic dwelling could take 3 years while a renovation could be completed in 2 or 3 months. Insurers do not collect data on completion times from builders.

There is no limit in legislation on the time that can elapse between notification of a claim and the submission of information required to open a claim. Over 90 per cent of claims to date have been received within 90 days of the first notification, but closed notifications can be re-opened for assessment years after being received by an insurer.

It is difficult to calculate the length of the liability period on a project certificate given that the construction period varies and notifications can be re-opened. The Commission considers 7 years to be a reasonable assumption for analysis, while accepting insurers' comments that the liability period could extend to 10 years or even longer. To date, only about 5 per cent of claims have been lodged more than 7 years beyond the certificate issue date.

Insurers who leave the market are still liable for claims on the project certificates they issued before they left. This is known as a ***run-off period***, and will continue for at least 6 or 7 years after the issue of a project certificate as claims are made by home-owners.

There are several key dates used to track a claim's progress (see table 1.1)

TABLE 1.1 KEY DATES IN THE DBI CLAIM PROCESS

Date	Description
Certificate issue date	The date the project certificate is issued by the insurer. This is at the commencement of construction. This date is also known as the 'underwriting date' as it is the point where the premium is charged.
Loss date	The date a claimant became aware of a defect or failure. This date is supplied by the claimant.
Notification date	The date the insurer first receives notification in writing of a potential claim. These 'notification only claims' can be escalated into claims on provision of minimum information. If the notification has not been escalated within 90 days it is closed on the insurer's system, but can be re-opened at any time.
Claim received date	The date the insurer receives the minimum information required to open a DBI claim on their system.
Liability decision date	The date the insurer made the decision to accept or deny a claim. If no decision is made within 90 days, the claim is deemed to be accepted.
Claim finalised date	The date the claim was closed on the insurer's system with all costs paid out.

2 SCHEME PERFORMANCE

KEY FINDINGS

A key measure of the viability of DBI is the simple loss ratio, which shows the cost of claims as a percentage of premium collected. An insurer's simple loss ratio will suffer if claims incidence and costs exceed the estimates made at the time premiums were set.

A period of premium discounting between 2006 and 2009 coincided with an increase in claims, resulting in rising simple loss ratios. This precipitated the progressive exit of five private insurers from the DBI market.

For certificates and policies issued in 2008 (at the onset of the global financial crisis), the simple loss ratio stood at 70 per cent as at 30 June 2013.

An insurer's profitability will depend on whether revenue — that is, premiums combined with investment returns — covers the cost of claims expenses and other operating expenses. An insurer's ability to estimate this cost relies on predicting the number and cost of claims that will be made by policy holders. In DBI, the lag between setting premiums and knowing the total cost of claims means that any assessment of the scheme relies on gradual build-up of claims information and assumptions about future claims.

2.2 SIMPLE LOSS RATIOS

The nature of long-tail insurance means that claims continue to come in over a long period of time after the issuing of the policy — for DBI this could be up to ten years from certificate issue date.[1] Because of this, insurers must forecast the sufficiency

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[1] DBI insurers are liable for defects up to 6 years after the completion of domestic building work. A project certificate is taken out when a project commences and it is assumed that construction is complete within 12 months giving a 7 year liability period. However, in practice, delays in construction and notification can mean that claims are made up to 10 years after the certificate is issued. In some circumstances, a home-owner can make a claim after the liability period has expired (s.54, *Insurance Contracts Act 1984* (Cth)).

of the premiums collected in one year to meet claims costs of subsequent years and to assess if their product is financially viable.

A key measure of viability is the simple loss ratio, which shows the cost of claims as a percentage of premium collected. This measure does not account for investment returns or any other costs an insurer faces aside from direct claim expenses. An insurer's simple loss ratio will suffer if claims incidence and costs exceed the estimates made at the time premiums were set. Table 2.1 shows the high level statistics for premium and claims costs since 2002, including the loss ratio. Close reading reveals that between 2006 and 2009 premium revenue was not increasing at the same rate as the number of project certificates being issued. This period of premium discounting coincided with an increase in claims as the portfolio matured and precipitated the progressive exit of five private insurers from the market.

TABLE 2.1 SCHEME PERFORMANCE — SIMPLE LOSS RATIO

All builders

Year	Number of project certificates	Premium excluding charges ($000)	Net incurred costs ($000)[a]	Years of liability remaining[b]	Loss ratio (%)
2002	17 731	10 661	4 560	0	43
2003	40 305	27 521	11 491	0	42
2004	34 720	27 536	17 151	0	62
2005	46 975	31 986	17 903	0	56
2006	53 142	32 119	16 090	0	50
2007	54 690	30 574	17 493	1	57
2008	53 113	27 650	19 405	2	70
2009	61 555	34 251	21 949	3	64
2010	65 101	41 881	16 153	4	39
2011	61 355	44 330	9 492	5	21
2012	57 703	46 678	2 946	6	6
2013 Jan-Jun	28 748	24 313	168	7	1

a Includes all claim costs including claims denied and notification. Costs have been assigned to the year in which the project certificate was issued. **b** Assumes 12 month construction period plus 6 year liability period.

FIGURE 2.1 CHANGE IN SIMPLE LOSS RATIO OVER TIME

All builders

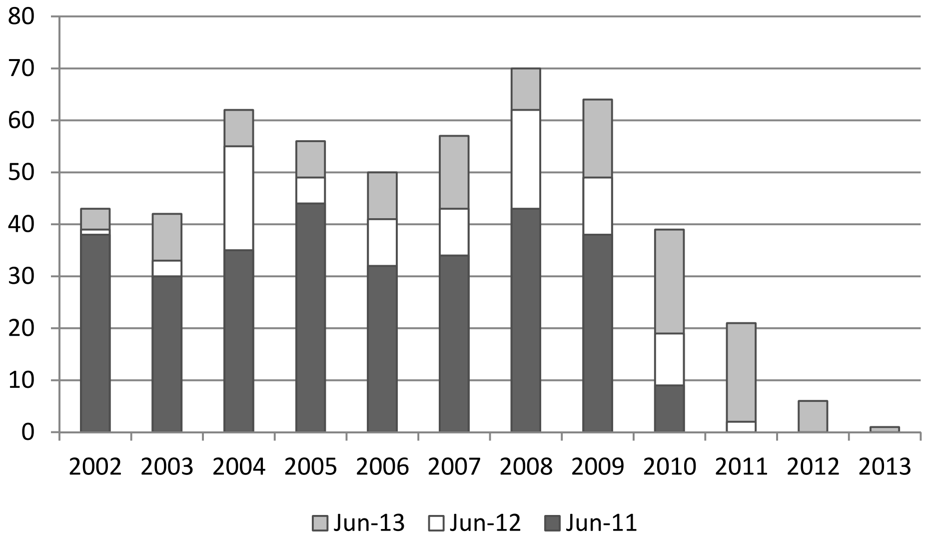


Figure 2.1 shows how, for each year in which certificates were issued, the simple loss ratio has grown over the period that the Commission has been reporting it (i.e. as of 30 June 2011, 30 June 2012 and 30 June 2013). Each year, as new claims are lodged and old claims are settled or re-estimated, any additional costs are assigned to the year's premium reserves, which do not change.

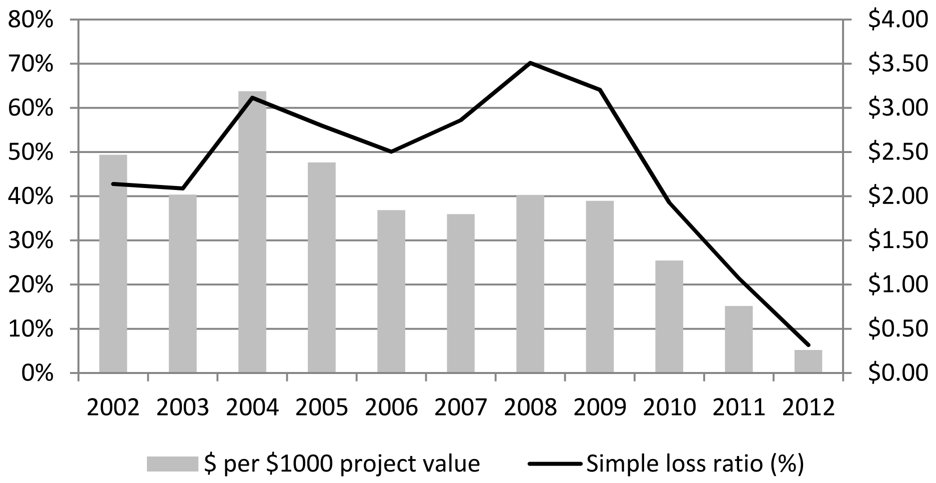
Our 2010-11 report highlighted that 2008 (at the onset of the global financial crisis) had a high loss ratio for certificates only three years into their liability period. As at 30 June 2013, claims costs have reached 70 per cent of premium reserves, higher than any other year. Claim costs are actually higher for 2009 than in 2008, but the loss ratio is worse in 2008 because insurers collected less in premium.

2.2.2 EFFECT OF COSTS AND PREMIUM ON LOSS RATIO

If the premium charged was too low or costs are higher than expected in a given period, the costs will exceed the funds set aside, and insurers face a loss. In figure 2.2 the black line shows the simple loss ratio for each year in the ten years to 2012. The columns show claims costs as a share of the total value of projects insured each year. Between 2006 and 2009, claims costs are fairly consistent relative to the total value of building work, but rise as a share of premium collected. During this time, competing insurers discounted premiums in a buoyant construction market. Insurer losses in this period can be attributed as much to insufficient premium reserves as a rising claim rate.

FIGURE 2.2 CLAIMS COSTS AS A SHARE OF PREMIUM AND TOTAL PROJECT VALUE

All builders – January 2002 to December 2012



3 ELIGIBILITY

KEY FINDINGS

There are currently just two insurers offering DBI in the Victorian market – Calliden and the VMIA. Over the last year, the share of eligible builders with turnover under $1 million has grown by 3 per cent. This could be an indication of a more conservative approach to underwriting, or an increase in builders who are seeking eligibility for registration purposes only.

One of the reforms to domestic building announced by the Victorian Government earlier this year is the removal of compulsory eligibility for DBI as a necessary pre-condition of registration for domestic builders. Builders will only need to be eligible when they are engage in a domestic building contract with a customer.

Before a builder takes out a DBI project certificate in relation to a specific building project, they must first have 'eligibility' with an insurer, which sets out the terms and conditions under which the insurer will offer DBI to the builder. Under current regulations, eligibility with an insurer is a pre-requisite to a builder's registration, without which they cannot enter into a domestic building contract with a consumer or perform work for another builder.

3.1 WHAT DOES DBI ELIGIBILITY MEAN?

Eligibility with an insurer for DBI is a form of pre-approval for taking out project certificates. Under the *Domestic Building Contracts Act 1995*, each time a builder enters a domestic building contract over $12 000 with a customer, they must take out a project certificate specific to the works covered by the contract.

Before granting eligibility, an insurer reviews a builder's business history and finances to assess their risk. Insurers impose an annual turnover limit on builders based on their assessment of the value of works that a builder can prudently undertake given their financial position. In some circumstances insurers require a financial security or indemnity of some form before granting eligibility.

In any given year, an eligible builder can take out project certificates up to the value of their turnover limit. DBI eligibility is reassessed annually by the insurer, and builders also have the option of applying to reassess their turnover limit at any time through the year.

3.2 OBTAINING DBI ELIGIBILITY

Builders may apply and take out eligibility with one of the two insurers in the Victorian market — VMIA or Calliden. The VMIA entered the market in May 2010 following the exit of most private insurers, and adopted the eligibility and turnover limits from each builder’s previous insurer to ensure continuity of cover. Since then, the VMIA has introduced its own underwriting criteria. The VMIA has a commercial arrangement with QBE, which acts as its agent issuing policies and assessing builder eligibility for DBI via insurance brokers. VMIA issues eligibility guidelines to QBE to ensure its underwriting standards are met.

3.3 TURNOVER LIMITS

Insurers impose conditions on builder eligibility. The VMIA and Calliden both use turnover limits to protect against over-exposure to builders at risk of insolvency

Annual turnover limits effectively cap the total value of contracts an eligible builder can make with customers in a year. From an insurer's perspective, the turnover limit is necessary to mitigate against a builder taking on more work than they can support financially, and becoming insolvent. Domestic building is capital intensive and cash flow is lumpy, and attempts to 'trade out of trouble' by taking on extra projects could be seen as risky by insurers who will be liable for the cost of unfinished work if the builder becomes insolvent.

FIGURE 3.1 ELIGIBLE BUILDERS BY TURNOVER BAND

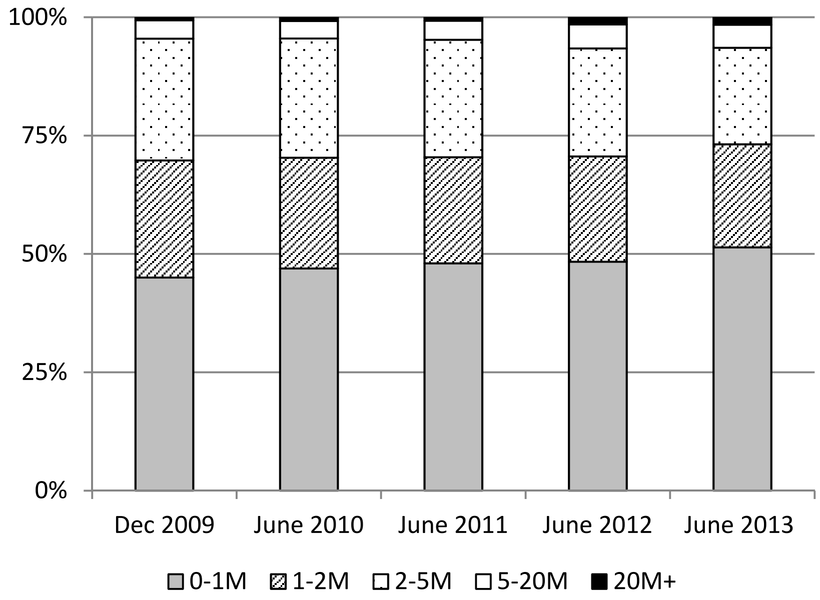


Figure 3.1 shows the share of eligible builders in turnover bands over time. In the last twelve months, the share of eligible builders with turnover under $1 million has grown by 3 per cent. The 2-20 million dollar range has shrunk by the same measure, while the other bands have remained constant. This could be an indication of a more conservative approach to underwriting, or an increase in builders who are seeking eligibility for registration purposes only, and have no intention of taking out project certificates.[1]

3.4 REFORMS TO ELIGIBILITY

One of the reforms to domestic building consumer protection framework announced by the Victorian Government earlier this year is the removal of compulsory eligibility for DBI, as a necessary pre-condition of registration for domestic builders. Those builders who do not undertake domestic building work will not need to maintain DBI eligibility under the new regulations, although they will still

[1] DBI eligibility is compulsory for builders in order to maintain registration. However, not all registered builders routinely enter domestic building contracts with consumers and so not all registered builders will end up taking out project certificates.

be subjected to tests of their financial capacity under the revised rules for registration with the VBA.

4 PROJECT CERTIFICATES AND PREMIUMS

KEY FINDINGS

Because DBI is mandatory, project certificate numbers are an indication of the overall level of activity in the Victorian domestic building market. The total number of certificates issued has fallen annually since 2010, and data for the first half of 2013 continues this trend.

New dwelling project certificates issued to registered domestic builders are the largest contributor to the number of DBI project certificates and the premium pool.

Since the withdrawal of most private sector insurers in 2009, premiums have risen. The average cost of a certificate has risen 67 per cent between 2008 and 2013, while average project value has risen by 8 per cent over the same period. However, the average cost of a project certificate has remained fairly stable since September 2011.

The challenge for insurers is to set an efficient premium structure — to match the premium paid for the project certificate with the risk to the insurer that is presented by the particular builder and project covered by the certificate.

In terms of premiums per $1000 of project value, high volume, high value categories of building (such as new dwellings) have always had the lowest premium rates, while swimming pools have had the highest.

Builders must take out Domestic Building Insurance on every building contract exceeding $12 000 in value. The premium is calculated specifically to the contract taking into consideration the value of the work, the type of work and the builder's risk rating and the policy is referred to as a "project certificate".

This chapter presents information on the number of DBI project certificates that have been issued to registered builders, and the value and types of building projects insured. It also examines the total premium pool collected by insurers and the average premiums being charged by insurers.

4.1 DBI PROJECT CERTIFICATES

Project certificates are issued in several categories depending on the type of building work specified in the contract.

Table 4.1 shows the relative contribution of each category over time to the total number of project certificates issued. The vast majority of project certificates are issued for construction of new dwellings. In 2012, new dwelling construction constituted 62 per cent of certificates issued. The figures for the first half of 2013 are consistent with this pattern.

TABLE 4.1 NUMBER OF PROJECT CERTIFICATES ISSUED BY TYPE

Year	New dwellings	Structural renovations	Non-structural renovations	Swimming pools	Total
2005	27 978	8 105	3 424	3 049	42 556
2006	30 052	10 125	3 887	3 273	47 337
2007	32 400	10 905	3 959	3 310	50 574
2008	32 155	9 377	4 301	4 113	49 946
2009	40 681	9 681	4 298	3 865	58 525
2010	43 474	12 357	3 418	3 165	62 414
2011	40 241	10 263	6 706	2 046	59 256
2012	34 684	12 205	7 270	1 759	55 918
2013 Jan-Jun	17 460	6 098	2 624	1 640	27 822

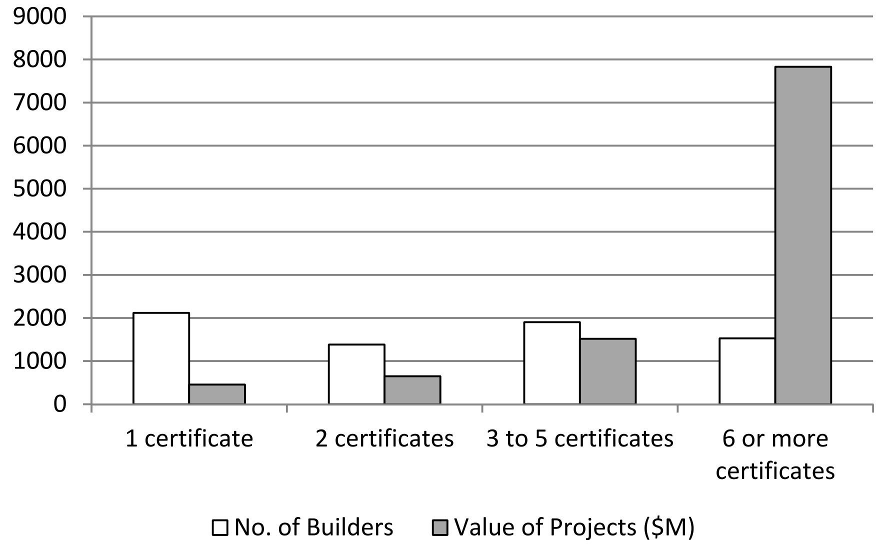
Because DBI is mandatory, project certificate numbers are an indication of the overall level of activity in the Victorian domestic building market. The total number of certificates issued has fallen annually since 2010, and data for the first half of 2013 continues this trend.

4.1.1 CONCENTRATION OF PROJECT CERTIFICATES

In figure 4.1, the distribution of certificates per builder is split to illustrate the concentration of project value in the top quarter of builders.

FIGURE 4.1 VMIA CERTIFICATES ISSUED PER BUILDER

Registered builder

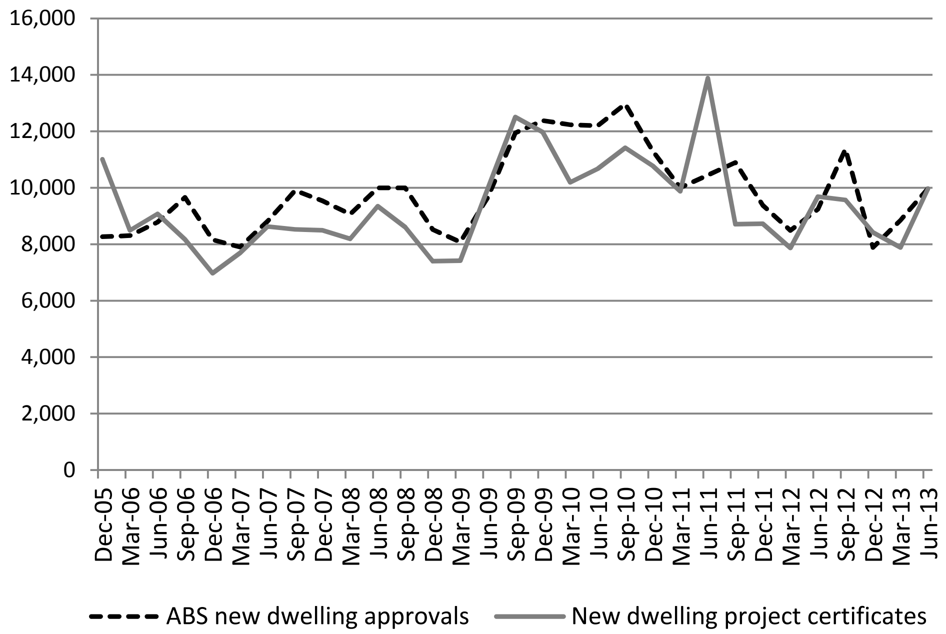


4.1.2 NEW DWELLING PROJECT CERTIFICATES

New dwelling project certificates issued to registered domestic builders are the largest contributor to the number of DBI project certificates and the premium pool. Figure 4.2 compares the number of project certificates issued for new dwellings with ABS quarterly data on building approvals. It is a way to check that builders are taking out insurance as required. However, the data series will not be an exact match mainly because the ABS uses compiled survey data.

The two data sets in figure 4.2 tracked closely until December 2009, when the withdrawal of insurers from the market may have led to delays in processing of project certificates, creating a time lag between the issue of a building permit and the issue of a DBI certificate. In June 2011, there was a spike in certificates issued as high volume builders brought forward as many certificates as possible in advance of a premium increase on 1 July 2011. The number of project certificates has since stabilised and appears to be tracking the ABS data.

FIGURE 4.2 NUMBER OF NEW DWELLING APPROVALS IN VICTORIA



Data source: ABS 8731.0 Building Approvals, Australia, Table 23. Dwelling Units Approved in New Residential Buildings, Number and Value, Original — Victoria. Includes houses, semi-detached dwellings, and units/apartments ≤ 3 storeys.

4.2 PREMIUMS

As outlined in chapter 3, insurers set premiums so that premium revenue, combined with investment and other income, adequately covers the expected future cost of claims and administration costs to ensure profitability.

4.2.2 AGGREGATE PREMIUM

Premiums differ according to project type, builder risk rating and project size (value). The total premium pool in any year is a combination of the rates being charged and the total amount of domestic construction that commences. Table 4.2 shows the total premium pool collected each year since 2005. Collectively, insurers have received between $25 million and $45 million in annual premiums.

TABLE 4.2 TOTAL ANNUAL PREMIUM

Registered builder (excludes GST, stamp duty and brokerage)

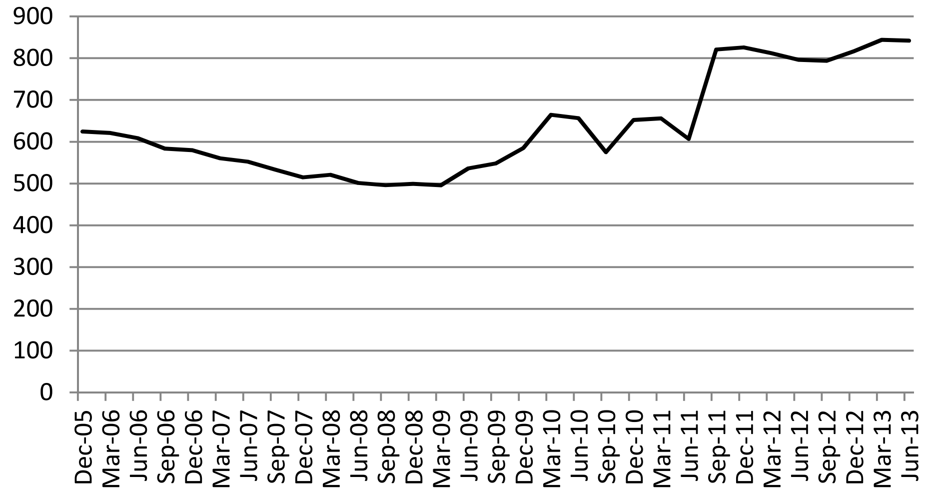
Year	Number of project certificates	Value of projects ($m)	Premium ($m)	Average project value ($)	Average cost of a project certificate ($)
2005	42 556	6 839.01	27.36	160 706	643
2006	47 337	8 034.60	28.32	169 732	598
2007	50 574	8 778.59	27.29	173 579	540
2008	49 946	8 953.82	25.18	179 270	504
2009	58 525	10 717.94	31.95	183 134	546
2010	62 414	12 195.22	39.68	195 392	636
2011	59 256	12 058.64	42.34	203 501	714
2012	55 918	10 917.21	44.95	195 236	804
2013 Jan-Jun	27 822	5 493.80	23.44	197 462	843

4.2.3 AVERAGE COST OF A PROJECT CERTIFICATE

Since the withdrawal of competing insurers in 2009, premiums have been rising. The average cost of a certificate has risen 67 per cent between 2008 and 2013, while average project value has only gone up by 8 per cent in the same period.

FIGURE 4.3 AVERAGE COST OF A PROJECT CERTIFICATE

Registered builder – December 2005 – June 2013



Since a period of some volatility between June 2010 and September 2011, the average cost of a project certificate has remained fairly stable at about an average of $820. The dip in June 2011 correlates with the heavy purchase of certificates by high volume builders at discounted rates in the last months before the discount was eliminated.

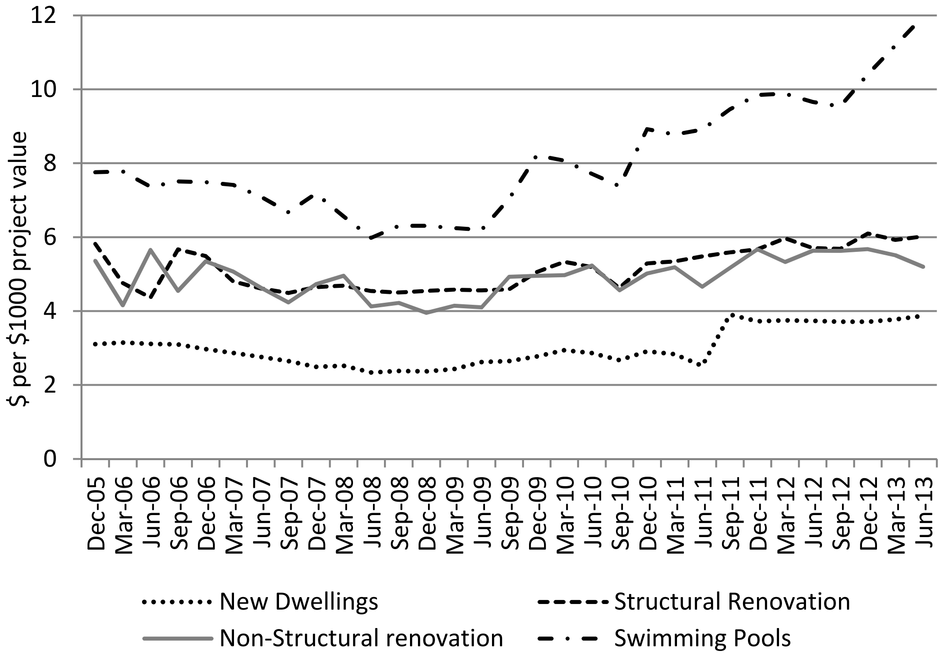
4.2.4 PREMIUM RATES — REGISTERED BUILDER

The Commission typically converts premiums into a value per $1000 of project value to enable comparison between insurers and over time.

Figure 4.4 shows premium rates for different project types over time. The average rates for all project types were at their lowest before September 2008. At this time competition between insurers was strong, but the market for DBI was still in its infancy, and a lack of information about costs could have driven premiums below cost reflective levels. By June 2010 all but one of the competing insurers had stopped offering DBI, and the VMIA had been brought in by the Government to maintain the supply of the product. In its first year, VMIA adopted QBE's premium rates, but on 1 July 2011 a new premium schedule was released which led to an increase in average rates.

FIGURE 4.4 AVERAGE PREMIUM RATE PER $1000 OF PROJECT VALUE

Registered builder. (excludes GST, stamp duty and brokerage)



The challenge for insurers is to set an efficient premium structure — to match the premium paid for the project certificate with the risk to the insurer that is presented by the particular builder and project covered by the certificate.

The VMIA publishes its premium schedule on its website (see appendix B) and it is based on the following parameters:

- the value of the contracted works (in bands)
- the category of work (structural, non-structural, swimming pools) and
- the insurer's rating of the builder's individual risk (A, B, or C).

When the VMIA premium schedule is converted to premium rates, it shows a sliding scale, with higher value projects attracting lower premium rates. This approach is compatible with the historical trends in DBI, where high volume, high value categories of building (e.g. new dwellings) have always had the lowest premium rates. Swimming pools, which have an average project value of around $50 000, have the highest premium rates.

Previous work undertaken by the Commission concluded that VMIA's premiums:[1]

- are sufficient to cover its expenses, risks and long-term claims costs
- are not set above the level required by the VMIA to cover its expenses and the risks and long-term claims costs.

4.3 REFORMS TO PREMIUMS

Under the Government's reforms to the regulation of the building industry, the minimum contract value for which DBI is mandatory will be raised from $12 000 to $16 000. This will reduce the number of certificates issued because smaller jobs that previously required DBI will become exempt.

[1] Essential Services Commission 2013, Domestic Building Insurance, *Premium Validation Review*, May (available on www.esc.vic.gov.au).

5 CLAIMS

KEY FINDINGS

DBI claims are not especially common, with only 4 506 lodged since the scheme was introduced in 2002. Nevertheless, there are signs that the frequency of DBI claims is rising.

Builder insolvency is by far the most common reason that claims on DBI are made, and almost half the claims received related to a structural defect.

Claim turnaround times are an important indicator of scheme performance. Since the scheme began, the average time between receiving a notification and a claim being finalised is 356 days.

Under reforms announced by the Victorian Government, new additional triggers will be introduced to allow consumers to pursue a DBI claim.

Claims under Victoria's DBI scheme can only be made under certain limited circumstances. The *Domestic Building Contracts Act 1995*, contains a number of implied warranties concerning a builder's work. DBI claims are only available where rights under these warranties cannot be pursued because the builder has died, disappeared or become insolvent. These three triggers are collectively abbreviated as DDI.

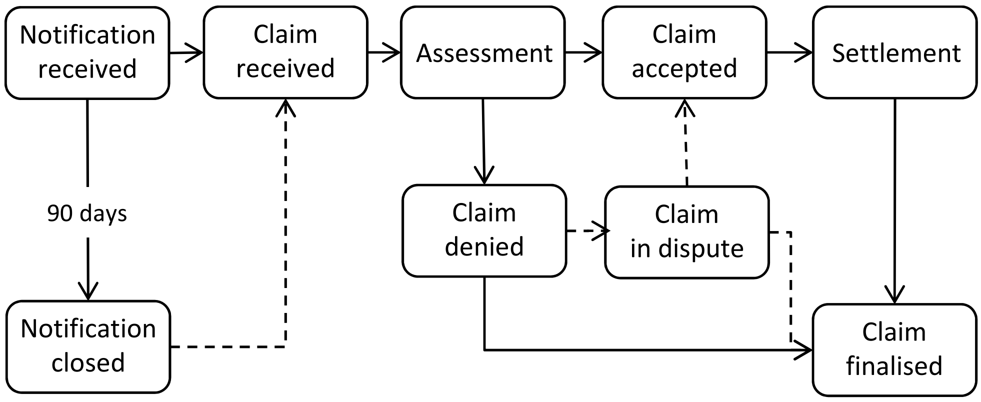
This chapter presents high level data relating to claims frequency and costs since the current scheme began for registered builders in 2002. As has been mentioned in our previous reports, the long liability period for DBI means that it is difficult to present claim numbers in their true context until at least six years after the issue date of project certificates.

5.1 DBI CLAIMS PROCESS

Claims are relatively infrequent in relation to the number of project certificates issued, but each one represents a major inconvenience for the customer whose home building project is incomplete or defective and whose relationship with their building contractor has completely deteriorated.

When a consumer notifies their insurer they would like to make a claim, it passes through multiple stages in its development, as illustrated in figure 5.1.

FIGURE 5.1 DBI CLAIMS PROCESS



A policy holder may notify an insurer of a fault at any time after a project certificate has been issued by providing very basic information. This notification escalates into a claim when the claimant provides minimum claims information. If the minimum information is not received within 90 days, the notification is closed, but remains on file. The notification may be re-opened at a later stage and escalated into a claim with provision of minimum information. The Commission's analysis concentrates on claims that have graduated beyond the notification stage. In many cases, the minimum claims information is received immediately, and a claim is opened without a notification period.

The insurer assesses a claim when minimum claims information has been provided. This involves investigating the builder to determine if they are DDI, and examining the claimed defect or non-completion to see if it qualifies for compensation. The assessment period may be a matter of days or months depending on the individual circumstances. The insurer then accepts or denies liability for the claim. If the claim is denied, the claimant has the opportunity to dispute the insurer's decision, otherwise the claim is finalised. If the insurer accepts the claim, a settlement period begins in which the compensation is calculated and paid. When the claim is fully settled with the claimant it is considered finalised, and closed.

DBI is considered to be a long-tail insurance as claims can be made for up to two years after completion in relation to non-structural defects, and for up to six years after completion in relation to structural defects.[1] As there is a lag between when the project certificate is issued and when the work is completed, DBI claims can sometimes be made as late as ten years after a certificate is issued. Therefore, the total number and cost of claims relating to certificates issued in any given year will not be known for a long period of time.

5.2 OVERVIEW OF CLAIMS

Table 5.1 shows the overall number of claims relating to registered builders since the introduction of the DBI scheme in 2002. Since the scheme began, insurers have received 4506 claims and 1781 notifications.

TABLE 5.1 CLAIM NUMBERS BY STATUS

Registered builder — January 2002 to June 2013

	Open	Closed / finalised	Total
Claims			
Accepted[a]	757	2 394	3 151
Pending[b]	205		205
Total accepted or pending	**962**	**2 394**	**3 356**
Liability denied	36	1 114	1 150
Total claims	**998**	**3 508**	**4 506**
Notifications	82	1 699	1 781
Grand Total	**1 080**	**5 207**	**6 287**

[a] Includes deemed, full, and partially accepted claims. [b] Includes claims being assessed and claims in dispute.

DBI claims are not especially common, with only 3 151 accepted since 2002, but they are complicated for insurers, and can take a long time to finalise due to the technical nature of the investigations and repairs.

Table 5.2 splits all claims received against registered builders, whether accepted or not, by the reported cause and claim type. Insolvency is by far the most common

[1] In some circumstances a home-owner can make a claim after the liability period has expired ((s.54, *Insurance Contracts Act 1984* (Cth)).

reason that claims on DBI are made for registered builders and almost half the claims received related to a structural defect.

TABLE 5.2 CLAIMS RECEIVED BY TYPE AND CAUSE

Registered builder only — January 2002 to June 2013

	Insolvency	Death	Disappearance	Other / unspecified	Total
Failure to commence	117	2	4	2	125
Failure to complete	1 255	19	50	25	1 349
Structural defect	1 917	38	119	29	2 103
Non-structural defect	871	13	35	10	929
TOTAL	4 160	72	208	66	4 506

Note: Excludes notifications

Table 5.3 illustrates the progressive build-up of claims since the scheme was first introduced. The annual total by the year of claim notification shows more claims coming in every year. In the right hand column, the same claims have been distributed into the year in which the affected project certificate was issued.

TABLE 5.3 CLAIMS RECEIVED OVER TIME

Registered builder only

	Claims by year of notification	Claims by certificate issue year
2002	2	158
2003	40	399
2004	56	355
2005	148	537
2006	187	536
2007	317	580
2008	458	514
2009	576	415
2010	629	467
2011	673	396
2012	957	140
2013 (Jan-Jun)	463	9
TOTAL	**4506**	**4506**

Note: Data revised since previous report. Includes all open and finalised claims. Excludes notification only claims.

Organising claims by the year that the affected certificate was issued helps to put the rising number of claims in context. If we consider the liability period to be exhausted for certificates issued in the years before 2007, there are signs that the frequency of DBI claims is rising.

5.2.2 COMMON PROPERTY CLAIMS

Generally, a claim relates to a single property and can be tracked back to a single project certificate, but there are instances where one claim is lodged which is shared between multiple properties (and therefore multiple project certificates). These claims are for common property defects in multi-unit developments, and can be paid out up to the $200 000 cap for each property affected.

Since the last report, the Commission has received data from insurers on the largest of the common property claims and, where indicated, some of the tables that calculate averages include an adjustment to account for the number of properties affected by the claim (as detailed in table 5.4).

TABLE 5.4 MULTI-UNIT ADJUSTMENT

Registered builder — January 2002 to June 2013

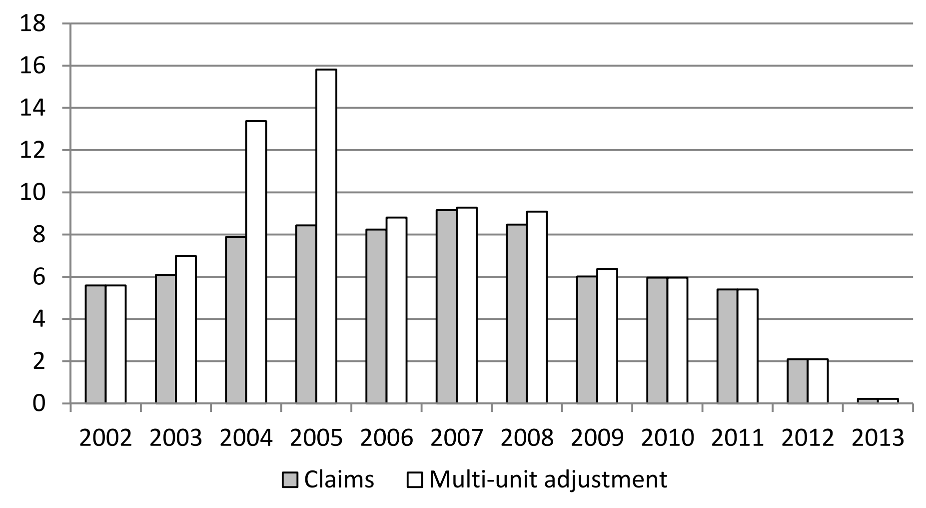
	Accepted	Denied	In Dispute / Being assessed	Total
Claims	3 151	1150	205	**4 506**
Properties affected	3 755	1209	205	**5 169**

5.2.3 CLAIMS AS A SHARE OF CERTIFICATES ISSUED

To properly quantify the relationship between the number of claims and the number of certificates issued, it is necessary to include the number of properties affected by common property claims. Figure 5.2 shows the number of accepted and pending claims per 1000 certificates each year, and the adjusted rate after accounting for common property claims. Between 2004 and 2005, there were 12 large common-property claims, affecting as many as 104 properties each.

FIGURE 5.2 CLAIMS PER 1000 CERTIFICATES ISSUED

Registered builder – January 2002 to June 2013



Note: Accepted and pending claims only. Excludes claims denied and notification only claims

Claim rates for the years before 2007, where liability is mostly exhausted, range from 5.6 claims per 1 000 certificates in 2002 to 8.2 in 2006. If the impact of common property claims is factored in, the rate is as high as 15.8 in 2005. The rate for 2010 is already 6.0, with three to four years of liability remaining.

5.3 CLAIM COSTS

As the number of claims for each project certificate year increases, so will the cost of claims from those years. The development of claim costs over time will depend on the number of claims, as well as the type of claims (e.g. non-completion or structural).

Insurers record costs against each claim. Net incurred costs is the main measure of claim costs. This is made up of several categories and represents the insurer's total liability at any given point in time (see box 5.1).

BOX 5.1 CALCULATION OF NET INCURRED COSTS

	$ Paid to claimant	Payments made directly to the home-owner to date.
plus	$ Paid to third party	Includes cost of investigation, structural assessments, legal fees.
less	Third party recoveries	Monies recovered from builders, suppliers, other insurances etc.
plus	Outstanding estimate	Insurer's estimate of the future costs relating to the claim. A finalised claim has no outstanding costs.

Some claims will be accepted and finalised with no costs, and a claim may incur costs for investigation even if it is not accepted. The total cost is more significant to insurers than the number of claims received, as it is the test of their premium setting and drives their profitability.

Table 5.5 shows that the average claim cost at different stages of claim development.

TABLE 5.5 CLAIMS COSTS BY STATUS

($000) Registered builder only — as at June 2013

	Open			Closed		Total
	Accepted	Denied	Pending	Accepted	Denied	
Number of claims (no.)	757	36	205	2394	1114	**4506**
Properties affected (no)[a]	1025	95	205	2730	1114	**5169**
Sum paid to claimant	25637	207	567	87862	1189	**115 462**
(plus) sum paid to third parties	4431	142	400	9660	1160	**15 792**
(less) sum of third party recoveries received	280	10	0	3769	59	**4 119**
(plus) sum of net outstanding estimate	17396	1057	3549	0	0	**22 002**
Sum of net incurred cost	47184	1396	4516	93752	2290	**149 138**
Average cost per claim	62.3	38.8	22.0	39.2	2.1	**33.1**
Average cost per property	46.0	14.7	22.0	34.3	2.1	**28.9**

[a] Reflects adjustments for common property claims as detailed in table 5.4

Average costs are lower in finalised registered builder claims compared with open and accepted claims, where the insurer is estimating the cost of the outstanding liability. This could indicate that actual costs tend to come in under the insurer's estimate, or that the costs are higher for more recent claims which are not yet finalised.

Even though the average cost of a DBI claim for a registered builder is around $33 000, this drops under $29 000 when the figures are adjusted for claims relating to multiple properties. These averages are influenced by the inclusion of denied claims, which tend to have lower costs than claims where rectification work is required. Average claim costs for finalised, accepted claims are shown by claim type in table 5.6, which are a more accurate indication of the costs faced by insurers. Claims for failure to complete are the most costly to insurers, making up around one third of all finalised claims costs.

TABLE 5.6 AVERAGE CLAIM COST BY CLAIM TYPE

Registered builder — January 2002 to June 2013

	Number of claims	Number of properties[a]	Net incurred costs ($)	Average cost per claim ($)	Average cost per property ($)
Failure to commence	93	93	1 886 130	20 281	20 281
Failure to complete	832	832	45 599 437	54 807	54 807
Structural defect	1028	1229	33 952 789	33 028	27 626
Other (non-structural) defect	441	576	12 313 547	27 922	21 378
Total	**2394**	**2730**	**93 751 903**	**39 161**	**24 341**

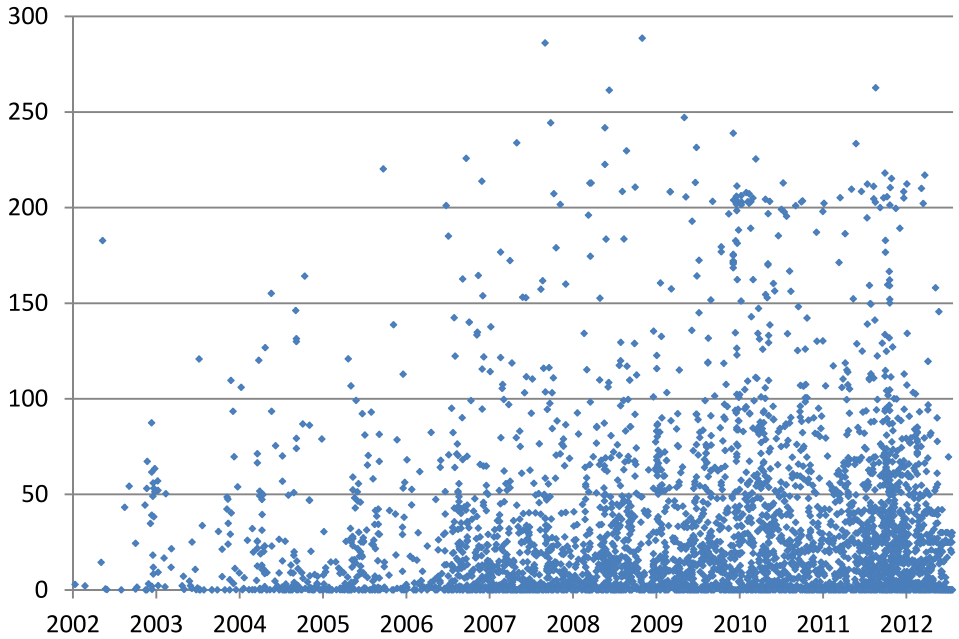
Note: Finalised, accepted claims. **a** Reflects adjustments for common property claims as detailed in table 5.4

The cost of a claim is influenced by many factors, some of which are outside the insurer's control. The age of the property affected and the nature of the defect influences the cost of rectification. Over time, an insurer's ability to manage costs of investigation and repair will help to determine their profitability.

In Figure 5.3 every claim received is plotted to show the net incurred cost and the date on which it was received by the insurer. Allowing for common property claims, this includes 5 169 data points, and illustrates the mix of large and small claims that have built up as the scheme matures. A third of claims are above the average cost of $28 852, and nearly a quarter of all claims are settled for less than $1 000. The median cost of a DBI claim is $12 522.

FIGURE 5.3 CLAIMS COST BY CLAIM RECEIVED DATE ($'000)

Registered builder – January 2002 to June 2013



Note: Includes all accepted, pending and denied claims. Excludes notifications. Common property claims are split into multiple claims per property

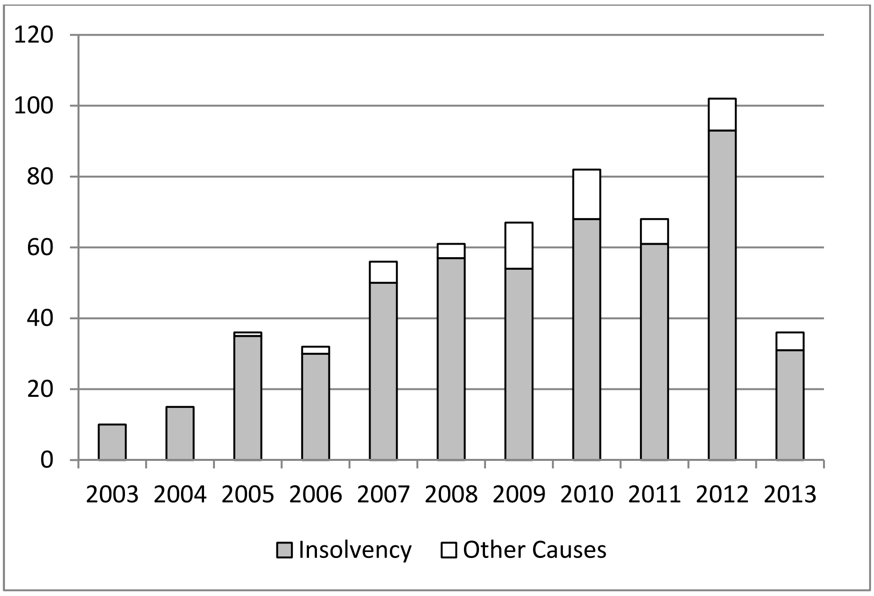
5.4 RELATIONSHIP BETWEEN BUILDERS AND CLAIMS

The 3 151 claims that have been accepted since 2002 have come from 565 separate builders. Each new builder that is determined to be DDI exposes an insurer to claims for every certificate issued on their behalf. An insurer's exposure in the event of a builder becoming insolvent depends on the number of certificates held, and the quality of work performed by the builder. Figure 5.4 organises builders with claims by the year in which their first claim was accepted. This shows clearly that the number of new builders becoming insolvent is rising.

There were 92 builders accepted by insurers as insolvent in 2012 and another nine died or disappeared. This is nearly double the number of builders that were declared DDI in 2007, when 56 builders went under. Of the 205 claims currently in dispute or pending, 75 per cent are related to builders whose DDI status has already been established in previous claims. The remaining 55 pending claims are from 32 "new" builders who have not been determined to be DDI in a previous claim.

FIGURE 5.4 DDI BUILDERS BY FIRST CLAIM DATE

Registered builder – January 2002 to June 2013



Note: where a builder has claims for multiple causes, the date of the earliest claim was used.

Not all insolvent builders are equally costly to insurers. A small builder whose work was of reasonable quality would not pose the risk of excessive claim costs. There are eighteen builders who have been declared DDI, but have not incurred any claims costs. The most costly scenario for an insurer is a large building company going under with multiple projects underway. Claims for failure to complete incur higher costs, and are payable even without a defect being present.

The Commission considers any builder with net incurred costs exceeding $1 million or more than 15 claims (accepted or pending) to be a “large” insolvency. There are currently 53 builders in this category. Several large insolvencies dominate the DBI landscape. The top ten insolvencies to date account for 28 per cent of costs incurred for accepted claims.

TABLE 5.7 TOP TEN INSOLVENCIES

Registered Builders - January 2002 to June 2013

	Accepted Claims	Units[C]	Net incurred Costs ($000)	Pending claims	Pending costs ($000)	Total claims	Total Cost ($000)
Top 10	559	1 040	39 203	12	231	571	39 434
Other big cases[a]	907	991	36 715	58	58	965	38 130
The rest[b]	1685	1724	65 012	135	135	1 820	67 886
Total	3151	3755	140 936	205	4 516	3 356	145 452

Note: a Includes insolvencies with more than 15 claims, or costs exceeding $1 million. b Includes 512 registered builders with claims accepted. c Reflects adjustments for common property claims as detailed in table 5.4.

5.5 CLAIMS MANAGEMENT

5.5.1 CLAIMS TURNAROUND

The time it takes for a claim to go through each stage of the claim process can be used to examine how the scheme is operating in general and may give an indication of how well consumers are being served. Looking at the claims that have been accepted and finalised since the scheme started in 2002, the average time between receiving a notification and a claim being finalised is 356 days, or about twelve months. The bulk of this time seems to be between the liability being accepted and the claim being finalised.

Under DBI legislation, if an insurer has not made a liability decision within 90 days of minimum claim information being received, the claim is deemed to be accepted. There are circumstances in which this period can be extended with the agreement of the claimant, but in general, insurers aim to make a liability decision within this time frame. After a claim has been accepted, the length of time it takes to finalise can be influenced by many factors, including an insurer’s approach to claims handling.

5.5.2 CLAIMS DENIED

Insurers can deny claims on the basis of several criteria. As shown in table 5.8, most claims are denied either because the fault reported was not deemed a defect, or because the builder was not insolvent. Previous reports have highlighted the need for consumer education to help home-owners understand what is covered under DBI.

TABLE 5.8 REASONS FOR CLAIMS DENIED

Registered builder only

	Claims (number)	Proportion (%)
Incorrect Insurer	50	4
Out of time	88	8
Builder found	100	9
Builder not dead	5	0
Builder not insolvent	371	32
Not deemed a defect	512	45
Other	24	2
TOTAL	**1150**	**100**

5.6 REFORMS TO CLAIM TRIGGERS AND PAYMENTS

5.6.1 NEW ADDITIONAL TRIGGERS

New triggers will be introduced (in addition to death, insolvency and disappearance) that will allow consumers to pursue a DBI claim where a project is incomplete, or there is a defect, and:

- the Victorian Building Authority has certified that a rectification order has not been complied with by the builder;
- the builder or building entity has been partially suspended, suspended or de-registered and thus cannot complete the project; or
- the builder is certified as being significantly and permanently incapacitated.

The first two of these triggers are aligned with the VBA's new powers to enforce building standards. The third trigger will protect customers of builders who have ceased trading due to severe injury, but do not qualify as DDI. Insurers will need to make their own assessment of how many claims will be made on these new triggers and adjust their forecast parameters.

5.6.2 CHANGES TO CLAIM PAYMENTS

DBI claims are presently capped at a maximum cost of $200 000, which includes legal expenses. Under the reforms this will rise to $300 000 and there is ongoing consultation as to whether legal expenses will be removed from this cap.

The standard excess for a DBI claim is between $500 and $1 000. This will be raised to $1 500 under the reforms.

The reforms provide insurers with more scope to pursue builders and recoup costs of claims because builders will be required to disclose whether they are acting as an agent of a financial vehicle, such as a family trust, where it would be difficult to pursue recovery actions. In the past, builders who had been declared DDI could re-register under a new entity and resume trading. With changes to registration practices, this practice will not be possible unless a builder has reimbursed their insurer for DBI claims.

The effect of these reforms on DBI claims rates and costs will be reflected in future performance reports prepared by the Commission.

6 OWNER-BUILDERS

KEY FINDINGS

Owner-builders carry out building on their own property, and require DBI if they sell the home that they have constructed within six and a half years of completion.

The number of owner-builder policies has been declining since 2006, although it has remained fairly stable since 2011, at around 500 per quarter.

Owner-builders are considered a higher risk category than registered builders and have a higher rate of claims, even though the total number of claims is very small (just 173 since 2002).

The most common reason for claims against owner-builders is disappearance. It is more difficult for new owners of a property to track down the original owner-builder to rectify faults.

An owner-builder is defined as someone who carries out building on their own property. Owner-builders are generally not in the building industry and must obtain a Certificate of Consent from the Building Practitioner's Board to obtain a building permit for domestic building work valued at more than $12 000. In doing so, owner-builders take on all the risks and responsibilities of a registered building practitioner.

Owner-builders require DBI if they sell the home that they have constructed within six and a half years of completion. They are required to provide the purchaser with evidence of a DBI policy and a report on any building defects by a prescribed building practitioner. In this way, it is quite distinct from DBI purchased by a registered builder.

The insurance policy (an owner-builder policy is not called a project certificate) is for the benefit of the purchaser and subsequent owners, in the event that the owner-builder dies, disappears or becomes insolvent, and the building work is defective.

To obtain DBI they must provide details of the cost of work, building inspections and certificate of occupancy date and location of the property. They must also provide a current defects report and a copy of the building permit. The DBI policy does not commence until the contract of sale is signed.

6.1 POLICIES AND PREMIUMS

Table 6.1 compares the number and value of building permits issued to owner-builders for new domestic buildings with owner-builder DBI policies issued. The majority of domestic building permits issued to owner-builders do not require DBI as the property is not sold within the relevant time frame.

TABLE 6.1 OWNER-BUILDER ACTIVITY

	Number of building permits[a]	Value of building permits ($000)	Number of DBI policies	Value of DBI policies ($000)	Total premium ($000)
2002	28 600	1 761 732	3 068	363 702	645
2003	29 791	1 923 515	3 370	405 389	744
2004	29 545	1 982 845	3 388	457 190	3 714
2005	26 807	1 683 667	4 419	672 393	4 625
2006	24 714	1 438 931	5 805	952 246	3 804
2007	24 776	1 318 842	4 116	674 972	3 285
2008	24 396	1 374 818	3 167	549 537	2 470
2009	22 674	1 277 676	3 030	492 269	2 301
2010	24 107	1 478 535	2 687	471 311	2 196
2011	20 616	1 364 132	2 099	373 092	1 992
2012	19 287	1 244 310	1 785	318 538	1 731
2013 Jan-Jun	11 847	744 878	926	164 331	872

[a] Includes permits for new dwellings and renovations/alterations.

Data source: Data for number and value of building permits from Building Commission Pulse.

Insurers treat owner-builders as a separate risk category from registered builders and have different premiums although the insurance coverage is very similar. Owner-builder policies cover structural and non-structural faults under the same rules as registered builder project certificates, but do not cover ‘failure to commence’ and ‘failure to complete’. The liability period may be shorter because the policy is only taken out when the house is sold. Insurers also have more information to assess risk at the time of writing the policy because construction is typically complete and a defect report is available.

Figure 6.1 shows the number of owner-builder policies being issued has been declining since 2006, but has remained fairly stable in the last few years at around 500 per quarter.

FIGURE 6.1 NUMBER OF OWNER-BUILDER POLICIES ISSUED

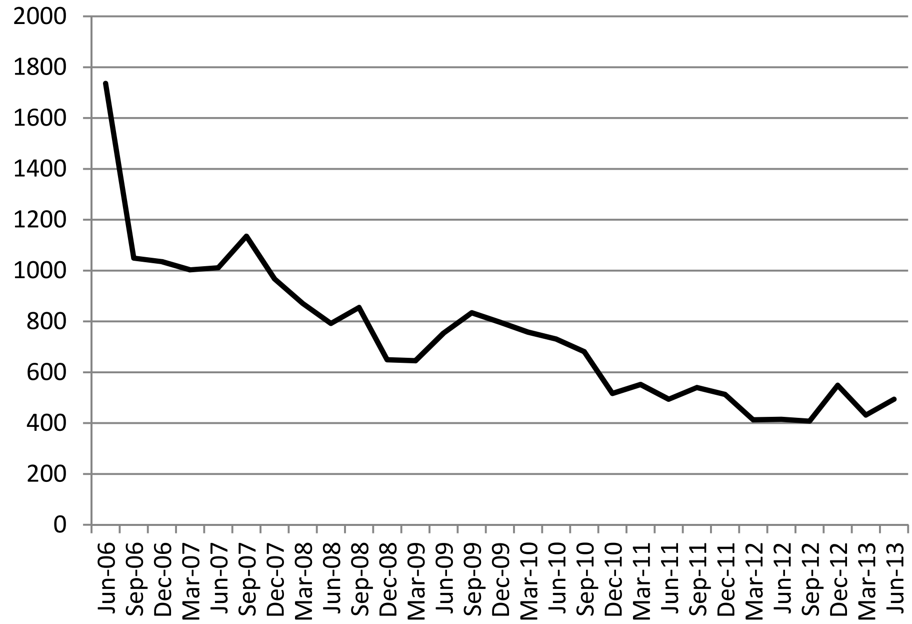
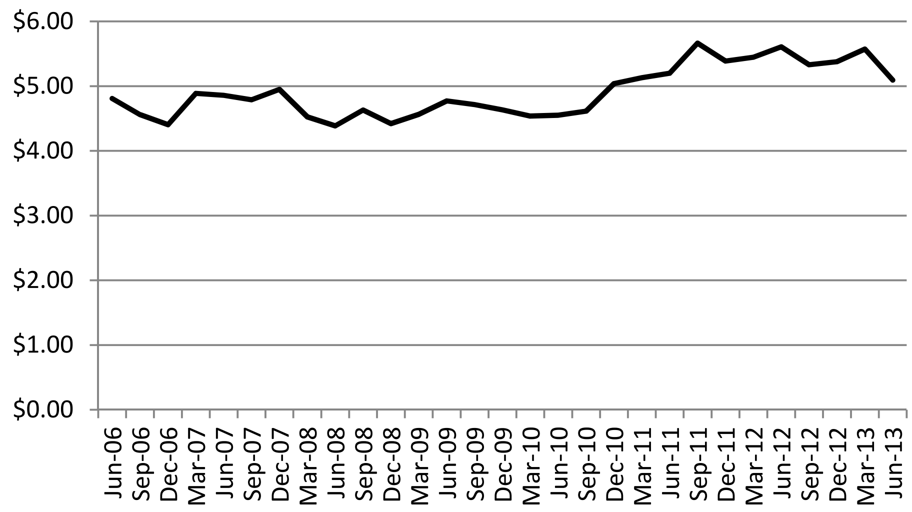


Figure 6.2 shows how the average premium per $1000 of project value has changed over time. Compared with registered builders, owner-builders pay a higher average premium rate, but over the last three years the rates have come closer to parity. There has been little volatility in the owner-builder rate since it rose above $5.00 at the end of 2010, while the registered builder rate has been rising steadily since 2009 (as shown in figure 4.4). Due to the low number of policies issued, and the project-specific factors used to determine the cost of each policy, the quarterly average rate can easily be affected by the mix of properties insured.

FIGURE 6.2 AVERAGE PREMIUM PER $1000 OF PROJECT VALUE

Owner-builders



6.2 CLAIMS

Owner-builders are considered a higher risk category than registered builders, and have a higher rate of claims even though the total number of claims is very small. Since 2002, there have been 173 claims accepted, and a further three have a liability decision pending. There have been nearly as many claims denied as accepted in this time. For registered builders, the ratio of claims denied to accepted is closer to 3:1. This could be attributable to the lack of centralised information about owner-builder properties, which leads consumers to use a DBI claim as a first step in investigating any problems.

TABLE 6.2 CLAIM NUMBERS BY STATUS

Owner-builders – January 2002 to June 2013

	Open	Closed	Total
Accepted	29	144	173
Pending	3	0	3
Total accepted or pending	**32**	**144**	**176**
Claims denied	4	146	150
Total Claims	**36**	**290**	**326**
Notifications	1	49	50
Grand Total	**37**	**339**	**376**

The most common reason for claims against owner-builders is disappearance. In the absence of a central licensing body, as exists for registered builders, it is more difficult for new owners of a property to track down the original owner-builder to rectify faults. Half of all the claims denied by insurers were cases where the insurer was able to locate the original owner-builder.

TABLE 6.3 CLAIMS BY CAUSE

Owner-builder – January 2002 to June 2013

	Number	Share (%)
Insolvency	67	39
Death	5	3
Disappearance	99	57
Other	2	1
TOTAL	**173**	**100**

Note: accepted claims only. Excludes claims pending a decision, claims denied and notifications

Based on the 173 claims accepted to date, the average cost of a claim on an owner-builder policy is $26 718.

APPENDIX A TERMS OF REFERENCE

Essential Services Commission Act **2001**

Essential Services Commission

Terms of Reference

Domestic Building Insurance – Data and Performance Monitoring

I, Tim Holding MP, Minister for Finance, WorkCover and the Transport Accident Commission, request the Essential Services Commission (the Commission) to provide ongoing monitoring reports on the pricing and performance of the Victorian Managed Insurance Authority's (VMIA) provision of domestic building insurance (DBI). The reports will cover claims management, the pricing of private domestic building insurers during the transition period from 29 March 2010 to the establishment of the new arrangements, and the claims management of the private domestic building insurers during the run-off period of their insurance policies.

Background

DBI has been compulsory in Victoria since 2002 for all residential building works in excess of $12,000 carried out by licensed builders.

DBI policies are taken out by the builder in favour of the homeowner and cover loss or damage resulting from non-completion of the work. This includes loss of deposit or breach of statutory warranty if the homeowner cannot recover compensation from the builder because of the death, disappearance or insolvency of the builder.

DBI was provided solely by private insurers. However, after a decrease in the number of private insurers and the associated levels of competition, the Government announced on 29 March 2010 that the VMIA would become a statutory monopoly provider of DBI after a transition period.

Scope of the Advice – Data and Performance Monitoring

The Commission is to annually monitor and report on the pricing and performance of the VMIA and private insurer's provision of DBI on an ongoing basis. The scope of the monitoring is to cover the:

- pricing and claims management of the VMIA;
- pricing of private domestic building insurers during the transition period; and
- private domestic building insurers' claims management during the run-off period.

The ongoing reporting is to be delivered in the form of annual reports.

The purpose of the annual reports is to inform the public of the performance of DBI.

The Commission will be required to publish a monitoring report each year that will be made publicly available. Any confidential or commercially sensitive material should be included in a separate attachment.

The purpose of the annual reports with the attachment is to inform the Government's consideration of DBI developments.

The annual reports will analyse quarterly data, including the number of eligible builders, project certificates, premiums levels, the number and amounts of claims for both the VMIA and private domestic building insurers and any other metrics the Commission and the Department of Treasury and Finance consider relevant.

Advice Process – Performance Monitoring

The monitoring reports are to be prepared independently by the Commission, under subsection 10(g) of the *Essential Services Commission Act* 2001 (the ESC Act), which provides the Commission with a general function to provide advice to the Minister for Finance.

The first data monitoring report is to cover the period from 1 July 2008 to 30 June 2010. Subsequent reports are to cover data for each financial year from 2010-11 onwards. The reports are to be provided by 30 November each year.

In providing this advice, the Commission is to have regard to its statutory objectives in section 8 of the ESC Act.

TIM HOLDING MP
Minister for Finance, WorkCover
and the Transport Accident Commission

Date: 9/07/2010

APPENDIX B VMIA PREMIUM SCHEDULE

Victorian Domestic Building Insurance Rate Chart

STRUCTURAL WORKS (Excludes MBW)

	CAT A				CAT B				CAT C			
	Base	GST	Stamp Duty	Total	Base	GST	Stamp Duty	Total	Base	GST	Stamp Duty	Total
$12,000	$ 391.00	$ 39.10	$ 43.01	$ 473.11	$ 460.00	$ 46.00	$ 50.60	$ 556.60	$ 735.00	$ 73.50	$ 80.85	$ 889.35
$12001 - $25,000	$ 403.00	$ 40.30	$ 44.33	$ 487.63	$ 475.00	$ 47.50	$ 52.25	$ 574.75	$ 760.00	$ 76.00	$ 83.60	$ 919.60
$25,001 - $50,000	$ 429.00	$ 42.90	$ 47.19	$ 519.09	$ 500.00	$ 50.00	$ 55.00	$ 605.00	$ 805.00	$ 80.50	$ 88.55	$ 974.05
$50,001 - $75,000	$ 442.00	$ 44.20	$ 48.62	$ 534.82	$ 518.00	$ 51.80	$ 56.98	$ 626.78	$ 830.00	$ 83.00	$ 91.30	$ 1,004.30
$75,001 - $100,000	$ 480.00	$ 48.00	$ 52.80	$ 580.80	$ 561.00	$ 56.10	$ 61.71	$ 678.81	$ 900.00	$ 90.00	$ 99.00	$ 1,089.00
$100,001 -$150,000	$ 555.00	$ 55.50	$ 61.05	$ 671.55	$ 650.00	$ 65.00	$ 71.50	$ 786.50	$ 1,042.00	$ 104.20	$ 114.62	$ 1,260.82
$150,001 - $200,000	$ 669.00	$ 66.90	$ 73.59	$ 809.49	$ 785.00	$ 78.50	$ 86.35	$ 949.85	$ 1,255.00	$ 125.50	$ 138.05	$ 1,518.55
$200,001 - $250,000	$ 821.00	$ 82.10	$ 90.31	$ 993.41	$ 963.00	$ 96.30	$ 105.93	$ 1,165.23	$ 1,540.00	$ 154.00	$ 169.40	$ 1,863.40
$250,001 - $300,000	$ 946.00	$ 94.60	$ 104.06	$ 1,144.66	$ 1,110.00	$ 111.00	$ 122.10	$ 1,343.10	$ 1,780.00	$ 178.00	$ 195.80	$ 2,153.80
$300,001 - $350,000	$ 1,073.00	$ 107.30	$ 118.03	$ 1,298.33	$ 1,260.00	$ 126.00	$ 138.60	$ 1,524.60	$ 2,015.00	$ 201.50	$ 221.65	$ 2,438.15
$350,001 - $400,000	$ 1,199.00	$ 119.90	$ 131.89	$ 1,450.79	$ 1,410.00	$ 141.00	$ 155.10	$ 1,706.10	$ 2,255.00	$ 225.50	$ 248.05	$ 2,728.55
$400,001 - $450,000	$ 1,326.00	$ 132.60	$ 145.86	$ 1,604.46	$ 1,555.00	$ 155.50	$ 171.05	$ 1,881.55	$ 2,490.00	$ 249.00	$ 273.90	$ 3,012.90
$450,001 - $500,000	$ 1,386.00	$ 138.60	$ 152.46	$ 1,677.06	$ 1,630.00	$ 163.00	$ 179.30	$ 1,972.30	$ 2,610.00	$ 261.00	$ 287.10	$ 3,158.10
$500,001 - $750,000	$ 1,512.00	$ 151.20	$ 166.32	$ 1,829.52	$ 1,780.00	$ 178.00	$ 195.80	$ 2,153.80	$ 2,850.00	$ 285.00	$ 313.50	$ 3,448.50
$750,001 - $1,000,000	$ 1,639.00	$ 163.90	$ 180.29	$ 1,983.19	$ 1,930.00	$ 193.00	$ 212.30	$ 2,335.30	$ 3,080.00	$ 308.00	$ 338.80	$ 3,726.80
Over $1,000,001	$ 1,719.00	$ 171.90	$ 189.09	$ 2,079.99	$ 2,025.00	$ 202.50	$ 222.75	$ 2,450.25	$ 3,240.00	$ 324.00	$ 356.40	$ 3,920.40

NON-STRUCTURAL WORKS (Excludes MBW)

	CAT A				CAT B				CAT C			
	Base	GST	Stamp Duty	Total	Base	GST	Stamp Duty	Total	Base	GST	Stamp Duty	Total
$12,000	$ 113.00	$ 11.30	$ 12.43	$ 136.73	$ 134.00	$ 13.40	$ 14.74	$ 162.14	$ 213.00	$ 21.30	$ 23.43	$ 257.73
$12001-$25000	$ 125.00	$ 12.50	$ 13.75	$ 151.25	$ 148.00	$ 14.80	$ 16.28	$ 179.08	$ 237.00	$ 23.70	$ 26.07	$ 286.77
$25,001 - $50000	$ 132.00	$ 13.20	$ 14.52	$ 159.72	$ 156.00	$ 15.60	$ 17.16	$ 188.76	$ 249.00	$ 24.90	$ 27.39	$ 301.29
$50,001 - $75000	$ 138.00	$ 13.80	$ 15.18	$ 166.98	$ 163.00	$ 16.30	$ 17.93	$ 197.23	$ 261.00	$ 26.10	$ 28.71	$ 315.81
$75,001 -$100,000	$ 151.00	$ 15.10	$ 16.61	$ 182.71	$ 178.00	$ 17.80	$ 19.58	$ 215.38	$ 284.00	$ 28.40	$ 31.24	$ 343.64
$100,001 -$150,000	$ 163.00	$ 16.30	$ 17.93	$ 197.23	$ 192.00	$ 19.20	$ 21.12	$ 232.32	$ 308.00	$ 30.80	$ 33.88	$ 372.68
$150,001 - $200,000	$ 189.00	$ 18.90	$ 20.79	$ 228.69	$ 222.00	$ 22.20	$ 24.42	$ 268.62	$ 355.00	$ 35.50	$ 39.05	$ 429.55
$200,001 - $250,000	$ 227.00	$ 22.70	$ 24.97	$ 274.67	$ 266.00	$ 26.60	$ 29.26	$ 321.86	$ 425.00	$ 42.50	$ 46.75	$ 514.25
Over $250,001	POA				POA				POA			

SWIMMING POOLS

	CAT A				CAT B				CAT C			
	Base	GST	Stamp Duty	Total	Base	GST	Stamp Duty	Total	Base	GST	Stamp Duty	Total
$12,000	$ 488.00	$ 48.80	$ 53.68	$ 590.48	$ 575.00	$ 57.50	$ 63.25	$ 695.75	$ 920.00	$ 92.00	$ 101.20	$ 1,113.20
$12001-$25000	$ 505.00	$ 50.50	$ 55.55	$ 611.05	$ 592.00	$ 59.20	$ 65.12	$ 716.32	$ 950.00	$ 95.00	$ 104.50	$ 1,149.50
$25,001 - $50000	$ 535.00	$ 53.50	$ 58.85	$ 647.35	$ 630.00	$ 63.00	$ 69.30	$ 762.30	$ 1,005.00	$ 100.50	$ 110.55	$ 1,216.05
$50,001 - $75000	$ 552.00	$ 55.20	$ 60.72	$ 667.92	$ 650.00	$ 65.00	$ 71.50	$ 786.50	$ 1,035.00	$ 103.50	$ 113.85	$ 1,252.35
$75,001 -$100,000	$ 598.00	$ 59.80	$ 65.78	$ 723.58	$ 705.00	$ 70.50	$ 77.55	$ 853.05	$ 1,125.00	$ 112.50	$ 123.75	$ 1,361.25
Over $100,001	POA				POA				POA			

Victorian Domestic Building Insurance Rate Chart

Multiple Building Works (MBW) - Structural

	CAT A Base	CAT A GST	CAT A Stamp Duty	CAT A Total	CAT B Base	CAT B GST	CAT B Stamp Duty	CAT B Total	CAT C Base	CAT C GST	CAT C Stamp Duty	CAT C Total
$12,000	$ 489.00	$ 48.90	$ 53.79	$ 591.69	$ 575.00	$ 57.50	$ 63.25	$ 695.75	$ 919.00	$ 91.90	$ 101.09	$ 1,111.99
$12001 - $25,000	$ 504.00	$ 50.40	$ 55.44	$ 609.84	$ 594.00	$ 59.40	$ 65.34	$ 718.74	$ 950.00	$ 95.00	$ 104.50	$ 1,149.50
$25,001 - $50,000	$ 536.00	$ 53.60	$ 58.96	$ 648.56	$ 625.00	$ 62.50	$ 68.75	$ 756.25	$ 1,006.00	$ 100.60	$ 110.66	$ 1,217.26
$50,001 - $75,000	$ 552.00	$ 55.20	$ 60.72	$ 667.92	$ 647.00	$ 64.70	$ 71.17	$ 782.87	$ 1,037.00	$ 103.70	$ 114.07	$ 1,254.77
$75,001 - $100,000	$ 600.00	$ 60.00	$ 66.00	$ 726.00	$ 701.00	$ 70.10	$ 77.11	$ 848.21	$ 1,125.00	$ 112.50	$ 123.75	$ 1,361.25
$100,001 -$150,000	$ 694.00	$ 69.40	$ 76.34	$ 839.74	$ 812.00	$ 81.20	$ 89.32	$ 982.52	$ 1,302.00	$ 130.20	$ 143.22	$ 1,575.42
$150,001 - $200,000	$ 836.00	$ 83.60	$ 91.96	$ 1,011.56	$ 981.00	$ 98.10	$ 107.91	$ 1,187.01	$ 1,569.00	$ 156.90	$ 172.59	$ 1,898.49
$200,001 - $250,000	$ 1,026.00	$ 102.60	$ 112.86	$ 1,241.46	$ 1,204.00	$ 120.40	$ 132.44	$ 1,456.84	$ 1,925.00	$ 192.50	$ 211.75	$ 2,329.25
$250,001 - $300,000	$ 1,182.00	$ 118.20	$ 130.02	$ 1,430.22	$ 1,387.00	$ 138.70	$ 152.57	$ 1,678.27	$ 2,225.00	$ 222.50	$ 244.75	$ 2,692.25
$300,001 - $350,000	$ 1,341.00	$ 134.10	$ 147.51	$ 1,622.61	$ 1,575.00	$ 157.50	$ 173.25	$ 1,905.75	$ 2,519.00	$ 251.90	$ 277.09	$ 3,047.99
$350,001 - $400,000	$ 1,499.00	$ 149.90	$ 164.89	$ 1,813.79	$ 1,762.00	$ 176.20	$ 193.82	$ 2,132.02	$ 2,819.00	$ 281.90	$ 310.09	$ 3,410.99
$400,001 - $450,000	$ 1,657.00	$ 165.70	$ 182.27	$ 2,004.97	$ 1,944.00	$ 194.40	$ 213.84	$ 2,352.24	$ 3,112.00	$ 311.20	$ 342.32	$ 3,765.52
$450,001 - $500,000	$ 1,732.00	$ 173.20	$ 190.52	$ 2,095.72	$ 2,037.00	$ 203.70	$ 224.07	$ 2,464.77	$ 3,262.00	$ 326.20	$ 358.82	$ 3,947.02
$500,001 - $750,000	$ 1,890.00	$ 189.00	$ 207.90	$ 2,286.90	$ 2,225.00	$ 222.50	$ 244.75	$ 2,692.25	$ 3,562.00	$ 356.20	$ 391.82	$ 4,310.02
$750,001 - $1,000,000	$ 2,049.00	$ 204.90	$ 225.39	$ 2,479.29	$ 2,412.00	$ 241.20	$ 265.32	$ 2,918.52	$ 3,850.00	$ 385.00	$ 423.50	$ 4,658.50
Over $1,000,001	$ 2,149.00	$ 214.90	$ 236.39	$ 2,600.29	$ 2,531.00	$ 253.10	$ 278.41	$ 3,062.51	$ 4,050.00	$ 405.00	$ 445.50	$ 4,900.50

Multiple Building Works (MBW) - Non Structural

	CAT A Base	CAT A GST	CAT A Stamp Duty	CAT A Total	CAT B Base	CAT B GST	CAT B Stamp Duty	CAT B Total	CAT C Base	CAT C GST	CAT C Stamp Duty	CAT C Total
$12,000	$ 141.00	$ 14.10	$ 15.51	$ 170.61	$ 167.00	$ 16.70	$ 18.37	$ 202.07	$ 266.00	$ 26.60	$ 29.26	$ 321.86
$12001-$25000	$ 156.00	$ 15.60	$ 17.16	$ 188.76	$ 185.00	$ 18.50	$ 20.35	$ 223.85	$ 296.00	$ 29.60	$ 32.56	$ 358.16
$25,001 - $50000	$ 165.00	$ 16.50	$ 18.15	$ 199.65	$ 195.00	$ 19.50	$ 21.45	$ 235.95	$ 311.00	$ 31.10	$ 34.21	$ 376.31
$50,001 - $75000	$ 172.00	$ 17.20	$ 18.92	$ 208.12	$ 204.00	$ 20.40	$ 22.44	$ 246.84	$ 326.00	$ 32.60	$ 35.86	$ 394.46
$75,001 -$100,000	$ 189.00	$ 18.90	$ 20.79	$ 228.69	$ 222.00	$ 22.20	$ 24.42	$ 268.62	$ 355.00	$ 35.50	$ 39.05	$ 429.55
$100,001 -$150,000	$ 204.00	$ 20.40	$ 22.44	$ 246.84	$ 240.00	$ 24.00	$ 26.40	$ 290.40	$ 385.00	$ 38.50	$ 42.35	$ 465.85
$150,001 - $200,000	$ 236.00	$ 23.60	$ 25.96	$ 285.56	$ 277.00	$ 27.70	$ 30.47	$ 335.17	$ 444.00	$ 44.40	$ 48.84	$ 537.24
$200,001 - $250,000	$ 284.00	$ 28.40	$ 31.24	$ 343.64	$ 332.00	$ 33.20	$ 36.52	$ 401.72	$ 531.00	$ 53.10	$ 58.41	$ 642.51
Over $250,001	POA				POA				POA			

As at 01/07/2013
Version 1.0

APPENDIX C JURISDICTIONAL COMPARISONS

TABLE C.1 SUMMARY OF BUILDERS WARRANTY INSURANCE — NATIONAL

	Eligibility conditions for builders	Type of scheme[a]	Min value of works	Max value payable	Coverage period	Premiums	Underwriting and number of insurers	Owner builders
NSW *Home Building Act 1989* *Home Building Regulation 2004* *Home Building Amendment Act 2011*	All licensed domestic builders must be eligible. Exemptions granted under special license where contract price does not exceed $20 000. DBI must be purchased if contract price is greater than $20 000.	Last resort	$20 000	$340 000 or 20% of contract value	Non-structural 2 years. Structural up to 7 years from completion, maximum of 10 years from issue of policy. Up to 12 months for incomplete work.	Premiums are set by insurers based on risk assessment and value of project.	NSW Home Warranty Insurance Fund, underwrites policies issued by QBE and Calliden insurance agents via approved brokers.	Required by law on sale of property if within 6 years of completion of building works
QLD *Queensland Building Services Authority (BSA) Act 1991*	All contractors must be licensed with BSA, for contract value greater than $3 300.	First resort	$3 300	$400 000	Non-structural 6 months. Structural 6 years and 6 months.	Contract price is the basis for determining premium. Premiums set by BSA.	Queensland Home Warranty Scheme - Building Services Authority (BSA)	Exempt
VIC *Building Act 1993* *Domestic Building Contracts Act 1995*	All licensed domestic builders must be eligible. DBI must be purchased where contract price exceeds $12 000.	Last resort	$12 000	$200 000 or 20% of contract	Non-structural 2 years. Structural 6 years from the date of completion.	Premiums are set by insurers based on risk assessment and value of project	VMIA and Calliden via approved brokers.	Required by law on sale of property if within 6 years of completion of building works

	Eligibility conditions for builders	Type of scheme[a]	Min value of works	Max value payable	Coverage period	Premiums	Underwriting and number of insurers	Owner builders
SA *Builders Licensing Act 1986*	All licensed domestic builders must be eligible or provide evidence of at least $100 000 in tangible net assets and solvency.	Last resort	$12 000	$80 000	3 months from handover until 5 years from completion.	Premiums are set by insurers based on risk assessment and value of project	QBE and Calliden via approved brokers.	Required by law on sale of property if within 5 years of completion of building works
NT *Building Amendment (Registration and other matters) Act* 2012 *Building Amendment (Residential Building Consumer Protection) Act* 2012	Eligibility is required for registration. Insurance Certificate is required before completion is approved by certifier. Builder registration requires $50 000 in net assets be maintained as part of pending legislation.	Pending legislation introduces Last resort and includes dispute resolution to close gap between first and last resort.	$12 000	$80 000	6 years from completion for structural, 2 years for non-structural	Premiums are set by Insurers based on risk assessment and value of project	HIA – brokerage services (underwritten by QBE) and MBA (Fidelity Fund) are the proposed administrator	
WA *Home Building Contracts Act (1991)*	All licensed domestic builders must be eligible.	Last resort	$20 000	$100 000	6 years from date of completion.	Premiums are set by Insurers based on risk assessment and value of project	QBE and Calliden via approved brokers.	Required by law on sale of property if within 6 years of completion of building works

	Eligibility conditions for builders	Type of scheme[a]	Min value of works	Max value payable	Coverage period	Premiums	Underwriting and number of insurers	Owner builders
TAS *Building Act (2000)* *Housing Indemnity Amendment Act 2008* Residential Building Work Quality (Warranties and Disputes) Bill 2012	Public liability insurance and contract works insurance is a requirement for accreditation as a builder. The *Housing Indemnity Amendment Act 2008* removed the mandatory requirement for domestic builders to purchase DBI. Bill setting up consumer protection and dispute resolution framework introduced into parliament.	Purchase of insurance is voluntary. Residential Building Work Quality (Warranties and Disputes) Bill 2012 enables dispute resolution process.						Register is maintained by Director of Building Control. Require details of workers compensation and public liability insurance.
ACT *Building Act 1972*	Eligibility required for registration.	Last resort	$12 000	$85 000	Non-structural 2 years, Structural 6 years from the date of completion.	Premiums are set by Insurers based on risk assessment and value of project	Master Builders Fidelity Fund underwrites insurance policies issued through MBA and HIA brokers	Must be licensed. Fidelity certificate is valid from sale/transfer up to a period of 5 years from Certificate of occupancy being issued

[a] First Resort Schemes cover defects and workmanship and operate like normal insurance contracts; Last resort schemes only come into effect if a builder dies, disappears or becomes insolvent

APPENDIX D SUMMARY OF DOMESTIC BUILDING CONSUMER PROTECTION REFORMS

Fact sheet

Domestic building consumer protection reform

Why are domestic building reforms necessary?

The Government recognises the importance of the domestic building industry to the Victorian economy, Victorian families and the small businesses that largely comprise the sector.

The current framework provides only modest levels of protection for consumers. It imposes additional costs on consumers and building occupations and has significant gaps that must be addressed.

What are the key components of the reforms?

Reforms in the domestic building industry will improve the framework to provide more effective consumer protection and industry oversight.

In relation to regulatory arrangements, the strategy will:

- improve registration/ licensing and re-registration standards;
- expand the scope of regulation to include corporations and partnerships;
- expand the disciplinary powers of the regulator; and
- improve oversight of building surveyors and the building permit system.

To improve consumer protection, the reform strategy will:

- create a central point for accessing consumer information;
- permit a binding Rectification Order where building work is assessed as defective or incomplete by a VBA inspector;
- refine the range and depth of consumer information;
- provide accessible information about building practitioners and building practitioner corporations' relevant disciplinary history; and
- extend the coverage of mandatory insurance to include payment of claims where a builder has failed to comply with a binding Rectification Order or VCAT ruling before the end of the building project.

To improve builder protection, builders as well as consumers will be able request an inspector to adjudicate a building dispute and Rectification Orders will be able to require payment by a consumer to the builder or into a trust account.

What improved outcomes are expected to result from the reforms?

Over time the reforms are expected to reduce the number of building disputes and when disputes do arise, to help them to be resolved quickly, fairly and cost efficiently.

The reforms are focussed on limiting the incidence of sub-standard building work by some practitioners through providing greater scrutiny in registration and oversight and greater certainty and speed in the dispute resolution process, and through creating disincentives for builders to produce incomplete or defective building work.

When will the reforms come into effect?

The reforms will be implemented during 2013 and 2014. The implementation of the reforms will be staged to allow consumers, builders and insurers time to modify their practices.

How can I get further information about the reforms?

An education campaign will inform consumers and builders of the new regulatory and insurance arrangements, and their new rights and obligations, as the relevant reforms are introduced.

For further information, and to download a copy of the *Victorian Domestic Building Consumer Protection Reform Strategy* visit www.dtf.vic.gov.au.