



Fair Play for Home Warranty Insurance Pricing for Strata Remedial Works

Strata Community Association (NSW) Submission
September 20 2023

INTRODUCTION

1. Strata Community Association (NSW) Overview

Founded in 1980, Strata Community Association (NSW) was formerly known as the Institute of Strata Title Management. SCA (NSW) serves as the peak industry body for Strata and Community Title Management in New South Wales. The association proudly fulfils a dual role as both a professional institute and consumer advocate.

2. Membership

SCA (NSW) boasts a membership of over 3,000 members, including lot owners, suppliers, and professional strata managers who oversee, advise, and manage a combined property portfolio estimated to be worth over \$450 Billion.

3. Strata and Community Title Schemes in NSW

NSW is home to 89,049 Strata and Community Title Schemes. A significant 95 per cent of these schemes are comprised of residential lots. Altogether, the total number of Strata and Community Title lots in NSW stands at 1,043,690.¹

4. NSW as a Leader in High-Density Living

According to the 2022 Australasian Strata Insights Report, there are 2,501,351 people residing in apartments across Australia. A majority of these apartment dwellers (51 per cent) are in NSW.² NSW also leads the way in the trend to higher density living in Australia and boasts the highest proportion of apartment households relative to all occupied private dwellings, standing at 22 per cent.

5. Employment Impact

Strata is a significant employer, directly providing jobs to 1,413 managers throughout NSW, as well as an additional 1,317 other related employees.³

6. Promoting Professionalism

1. SCA (NSW) is dedicated to fostering a high standard of professionalism in the strata industry with initiatives like the Professional Standards Scheme (PSS), which contributes to ensuring strong consumer outcomes for over 1 million strata residents in NSW.
2. SCA (NSW) membership encompasses a wide range of entities, from large corporate companies to small family businesses to dedicated volunteers. Members possess expertise in all aspects of strata management, service provision, and governance.

For further information about this consultation, please contact Dylan Lin, Policy and Advocacy Officer, SCA (NSW). Dylan.lin@strata.community

¹ Hazel Easthope, Danielle Hynes, Yi Lu and Reg Wade, Australasian Strata Insights 2022, City Futures Research Centre, UNSW, Accessed at https://cityfutures.ad.unsw.edu.au/documents/717/2022_Australasian_Strata_Insights_Report.pdf

² Ibid, p.8-13

³ Ibid, p.8.

HOME OWNER WARRANTY INSURANCE

1. Introduction

In NSW, Home Owner Warranty Insurance (HOWI) is a valuable insurance product that applies when builders face financial troubles, such as insolvency, disappearance, or bankruptcy, ensuring that consumers don't bear the full financial burden of these costs. While HOWI serves as a critical shield for property owners, there is a significant discrepancy when it comes to strata remedial works. The cost of remedial work in strata properties can be as much as five times that of constructing a new house, seemingly without valid justification. This raises questions about fairness and equity in the home insurance system, particularly considering that new housing projects, perceived as riskier by some, are subject to more lenient insurance rates. **Consequently, SCA (NSW) proposes reducing remedial HOWI from the current range of 8-10% of the contract price to a more equitable 1-2% of the contract price in line with new homes.**

2. HOWI Overview

HOWI is a protective measure for homeowners and subsequent buyers in cases of defective or incomplete construction work. It becomes necessary for residential building works with a price exceeding \$20,000 or involving labour and materials worth over \$20,000. The definition of residential building work is intricate, encompassing construction, repairs, and decorations of dwellings, but various works can be considered included or excluded (e.g., a standalone contract for internal painting is excluded).²

The current scheme in place is the Home Building Compensation Fund, which supersedes previous schemes and funding arrangements. It offers coverage when homeowners cannot recover from builders or developers due to certain circumstances. However, HOWI is subject to certain limits, specifically a maximum of \$340,000 per dwelling, along with an excess of \$250 (aggregated, not per lot). The insurance policy ensures that if the contract price (including GST) for the work exceeds \$20,000 multiplied by the number of lots, it provides coverage for each dwelling in the building, with a minimum of \$340,000 per dwelling. Conversely, if the contract price (including GST) falls below the threshold of \$20,000 multiplied by the number of lots, the insurance policy must guarantee a total coverage amount of no less than \$340,000.³ Whilst this formula is useful for new build or

² Bannermans Lawyers, BL. "When Do You Need Home Warranty Insurance?" Bannermans Lawyers, May 3, 2017.

³ Icare, I. "The Home Building Compensation Fund (HBCF)." [www.icare.nsw.gov.au](https://www.icare.nsw.gov.au/government-agencies/our-funds-and-schemes/home-building-compensation-fund). NSW Government, 2023. <https://www.icare.nsw.gov.au/government-agencies/our-funds-and-schemes/home-building-compensation-fund>.

retrofits, it is not suitable for strata remedial works as the risk cover and calculation is not suitable.

3. SCA (NSW)'s Response to HOWI

Strata remedial works incur a significantly higher cost for HOWI, approximately four to five times that of the construction of a new house. This discrepancy seems unwarranted, given that new house construction projects typically pose greater risks to insurers. Compared to the construction of a new house, remedial works have a lower risk of such occurrences, with the last known instance occurring over a decade ago involving Kladis Building Consultancy Services in 2013. This insurance policy only comes into play when a contractor becomes insolvent, disappear, die or have a unpaid NCAT works order against it.. For example, if a waterproofing job for remedial works costs \$100,000, the associated insurance amount paid to the government is \$10,000 (10%), despite the insurance rarely being invoked. So rare that in the last 10 years there would have been no claims. In contrast, building a new house worth \$100,000 incurs an insurance cost of \$2,000 (2%) paid to the government.⁴

The current insurance rate structure places an undue burden on owners corporations for strata remedial works, which should not be the case. **SCA (NSW) believes there is a need for a more equitable approach to pricing this insurance.** The existing formula, which calculates the insurance premium based on whether the contract sum exceeds \$20,000 per lot, results in inflated coverage amounts. For instance, when dealing with five lots with a total value of \$200,000, the insurance coverage of \$340,000 inexplicably balloons to \$1.5 million because it multiplies down when the price of the contract exceeds \$20,000 per lot. This becomes even more problematic when dealing with larger strata schemes that have 20 or more lots. In such cases, each lot is automatically assigned coverage of \$340,000, regardless of the actual risk associated with each lot.

The construction of a new house maintains a more equitable insurance rate structure, typically ranging between 1% and 2% of the contract price. Conversely, for remedial works, which primarily encompass repair and maintenance, the insurance premium can be as high as 8% to 10% of the contract price. SCA (NSW)'s research suggests that the premiums for HOWI on strata remedial works are disproportionately high when compared to the associated risks. This insurance rate structure does not align with the risk profile, as it is not four to five times riskier. Below is a table with several de-identified examples:

⁴ Australian Securities & Investments Commission, A. "Notice ." publishednotices.asic.gov.au. ASIC, March 12, 2013. <https://publishednotices.asic.gov.au/browsesearch-notices/notice-details/KLADIS-BUILDING-CONSULTANCY-SERVICES-PTY-LTD-138283253/08d24836-e2a9-453a-9181-ea32f8879059>.

<u>Home works</u>	<u>Strata Remedial Works</u>
<i>Bathroom renovation</i>	<i>Strata remedial building works</i>
\$32,000 contract price (including GST)	\$216,763.09 (excluding GST)
HOWI = \$347 (1.08%)	HOWI = \$19,498.09 (8.9%)
<i>Renovation works townhouse bathrooms and other works</i>	<i>Cladding and window replacement and painting</i>
\$110,000 (including GST)	\$539,083 contract price
HOWI = \$832 (0.756%)	HOWI = \$43,288.90 (8.03%)
<i>Constructing a new home</i>	<i>Strata Remedial</i>
\$741,875 contract price (including GST)	\$1,386,084.50 contract price (including GST)
HOWI = \$5,000 (0.6%)	HOWI \$80,473 (5.8%)
<i>Constructing a new home</i>	<i>Strata Remedial</i>
\$1,007,485 contract price (including GST)	\$22,862 contract price (including GST)
HOWI \$14, 216.34 (1.4%)	HOWI = \$2,000 (8.75%)
	<i>Strata remedial</i>
	\$534,346.40 contract price (including GST)
	HOWI = \$11,644 (2.16%)

Accordingly, SCA (NSW) strongly recommends a substantial revision in the insurance rate structure of HOWI for remedial works. The association seeks to decrease the current rate, which falls in the range of 8-10% of the contract price, and instead establish a more balanced rate of 1-2% of the contract price, aligning it with the price applicable to new homes.

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