THE LAW SOCIETY
OF NEW SOUTH WALES

Our Ref: MM:LJB
Direct Line: 9926 0202
Email: liza.booth@lawsociety.com.au

1 September 2010

Ms Kye Tran
Legal Services Division
Land and Property Management Authority
GPO Box 15
SYDNEY NSW 2001

email: kye.tran@LPMA.nsw.gov.au

Dear Ms Tran,

Review of Vendor Disclosure for Residential Property Sales in NSW by Matt Brown MP – Discussion Paper

The Law Society appreciates the opportunity to be involved in the consultation process for the review of vendor disclosure for residential property sales in New South Wales by Matt Brown MP.

The Society's Property Law Committee (Committee) has considered the issues in the LPMA's Discussion Paper: 'Review of Vendor Disclosure for Residential Property Sales in NSW' by Matt Brown MP.

Purpose of the Review

The Discussion Paper states that it is proposed to investigate the practical and legislative aspects of stipulating that pre-purchase reports (including building inspection and pest inspection reports) must be provided by vendors to potential purchasers prior to auction or sale by private treaty of real property in NSW.

Vendor Disclosure Regime

The Committee believes the existing regulatory regime has worked well over a period in excess of 20 years, is well-understood by stakeholders in conveyancing, provides an appropriate balance between the competing interests of vendor and purchaser and has generated relatively little litigation.

The underlying rationale for a vendor disclosure regime is that there are a number of topics which are of such fundamental importance to all (or most) prospective purchasers that they should be addressed in a document attached to (or notice forming part of) the proposed Contract. The issue can then be squarely placed before the proposed purchasers prior to their signing and binding themselves contractually.

The current regime prescribes vendor disclosure documents for contracts for sale of all land whether vacant, residential, strata or otherwise. If a vendor fails to attach one of the prescribed documents to a contract for sale of land, the purchaser may rescind the contract within 14 days after the making of the contract (clauses 16 and 17 of the *Conveyancing (Sale of Land) Regulation 2010*).

The documents that currently form part of the vendor disclosure regime in NSW have the following characteristics:

- They are issued by monopoly providers,(e.g. LPMA, local councils, sewerage authorities);
- They are authoritative rather than qualitative or subjective;
- They are relatively inexpensive (around $200 per transaction).

The Committee does not consider that any benefits to potential purchasers of requiring the vendor to provide access to one or more of the reports identified in the Discussion Paper outweigh the additional cost or other factors explored in more detail below.

Terms of Reference

The Committee commented on each of the items listed under the terms of reference as follows:

1. *Investigate the information provided to prospective purchasers relating to the physical condition of the building for residential real property in NSW*

It is the experience of Committee members that most purchasers of non-strata properties obtain pest and building reports. In relation to strata properties, it is usual to recommend an inspection of the owners corporation records be obtained and the majority of purchasers appear to do so. These documents are obtained by prospective purchasers at their own expense. Where a cooling off period applies to a transaction, the documents tend to be obtained during the cooling off period. Where there is no cooling off period for any reason, the reports must be obtained prior to exchange.

Lenders do not inquire about, or are not interested in obtaining, these quality reports. Some lenders will commission valuations at the borrower's expense, but these usually involve a cursory visual inspection and do not normally deal with the physical condition of the property.

In exceptional circumstances, some quality reports obtained may indicate the need to get more specialised reports, e.g. geotechnical reports.

2. *Compare the information required to be provided to purchasers of real property in NSW with other comparable jurisdictions, in particular, the ACT.*

Introduction

The Committee notes that there has been some consideration in the Discussion Paper and in other forums about adoption of some aspects of the disclosure model which operates in the ACT. The Committee believes that the variations in the geography (and in particular the relative areas - what may be appropriate in a region with an area of 2,358 sq km may be entirely inappropriate in a State with an area in excess of 800,000 sq km), regulatory history and conveyancing and titling procedures in the two jurisdictions are so substantial that it would be entirely inappropriate to use the ACT

procedures as a template for the NSW regime. More detailed commentary about the ACT model is set out below.

The legislative scheme

The vendor disclosure provisions in the ACT are contained in the *Civil Law (Sale of Residential Property) Act* 2003 and the *Civil Law (Sale of Residential Property) Regulation* 2004. References in this section of the submission to sections and clauses refer to that Act and the Regulation respectively unless the contrary is indicated.

The key vendor disclosure provisions are in Part 2 of the Act. Section 7 introduces, among other things, the concepts of:

- Building and compliance inspection report (BCIR)
- Building conveyancing inquiry documents
- Lease conveyancing inquiry documents
- Pest inspection report

Each of these categories is defined by prescription; a detailed definition of each appears in clauses 7 to 10 of the Regulation. The BCIR and pest inspection report are defined by reference to an Australian Standard – AS 4349.1 (*Inspection of buildings – Pre-purchase inspections – Residential Buildings*) and AS 4349.3 (*Inspection of buildings – Timber pest inspections*) respectively. Each is required to be attached to the contract for sale of a residence, except in certain limited circumstances, for example:

- The BCIR and building conveyancing inquiry documents are not required for most strata properties, new residences and off-the-plan purchases (section 9(2)(a));
- Pest reports are not required for most strata properties (section 9(2)(b));
- If the seller cannot obtain any document "after taking all reasonable steps to obtain it", the document does not have to be attached to the contract (section 9(2) (c)).

The BCIR and the pest report must be no more than 3 months old at the time of first advertising or listing of the property. To prevent "inspector-shopping", the vendor must attach any BCIR obtained in that 3 month period, and any pest inspection report obtained in the 6 months before first advertising or listing (section 9(1) (h)).
Section 9(1) (i) and (j) require either a current asbestos assessment report (if available) or an asbestos advice (if the report is not available) to be attached. Each of these documents is defined in the *Dangerous Substances Act* 2004 (ACT), sections 47K and 47J respectively.

There is a prohibition on reports being prepared by an inspector related to the vendor, the vendor's agent or the vendor's lawyer (section 9(3)).

The marketing of a property without the required documents being available for inspection is an offence, attracting a maximum penalty of $1000 for an individual and $5000 for a corporation (section 10(1)). There is also an implied term stating that the required documents form part of the contract (section 11(1) (i)). Interestingly, there does not seem to be anything in the Act or Regulation which gives a purchaser the right of rescission (or for that matter explicitly gives any contractual right to the purchaser) if a required document is not attached to the contract.

Section 18 entitles the vendor to be reimbursed for the cost of (the latest) BCIR and pest report. The section does not appear to restrict reimbursement to a prescribed or reasonable amount; nor does the section indicate the existence of any review or assessment mechanism.

Section 19 overcomes the privity of contract difficulty.

Part 3 of the Act deals with energy efficiency ratings. The advertising of residential premises without stating the energy efficiency rating of the habitable part of the premises (or misstating the correct details in a material particular) is an offence (s 20)). Section 23 provides that the vendor must give an energy efficiency rating statement (EERS) to the prospective buyer (for example, by attaching it to the contract) and receive written confirmation from the purchaser that he or she has received it (for example, by an acknowledgement in the contract). If the vendor fails to comply, the seller must pay 0.5% of the price to the purchaser (section 23(3)).

The parties cannot contract out of the Act (section 36).

If a person knowingly or recklessly makes a statement or omission in a EERS, a BCIR or a pest inspection report which makes the report materially false or misleading, they commit an offence with a maximum penalty of $50,000 - $10,000 if not a corporation (section 37). Giving a false or misleading document to someone else is likewise an offence (section 38).

The practice in the ACT

The Committee has made informal inquiries from a number of practitioners about how the ACT system operates in practice. The responses indicate that, for a "typical" transaction:

- The cost to the vendor of obtaining title and zoning material is of the order of $200.
- The cost of obtaining a BCIR and pest inspection report (paid by the vendor but recoverable from the purchaser) is of the order of $800 to $900.
- Where the property is strata title, the vendor incurs a further cost which could range between $88 and $400, of which $88 is recoverable from the purchaser.
- Where a building report is to be updated, the cost of doing so is $300. The statute does not deal with the issue of who bears the cost of updating the report – one practitioner indicated that "usually there is a squabble but the purchaser pays a 'standard 1 off' amount – balance is absorbed by the seller". The Committee notes that in one contract it sighted there were three "very strong recommendations" that an update be obtained rather than relying on the report attached to the contract.

Asbestos Inspection Reports

The Committee recognises the dangers associated with disturbing asbestos-based building materials, and the possibility that a purchaser may undertake some renovations (possibly minor and / or without engaging a builder who has expertise in identifying those properties which are likely to be affected by asbestos).

However, in the light of the difficulties in identifying who would be qualified to give such a certificate or what the certificate should contain (and further difficulties such as there being no indication of the likely cost of such a certificate), the Committee does not believe that an "asbestos inspection" report should be a compulsory annexure to a contract for sale of land.

The Committee notes that the ACT Contract for Sale contemplates the provision by the vendor of either "Asbestos Advice" or a "Current Asbestos Assessment Report". If there is to be any information provided about asbestos at all, the Committee considered that a short generic form of notice would be the most appropriate means of doing so – in effect, doing for asbestos what has been done for smoke alarms. Any such notice should be drafted after consultation with WorkCover as the body with greatest expertise with issues relating to asbestos removal.

"Comparable" jurisdictions

The Committee observes that there a number of significant differences between the ACT and NSW titling and conveyancing systems:

- As title in the ACT is historically leasehold rather than freehold, there have been more effective controls over the construction of improvements (including records of approvals) in the ACT than is the case in NSW.
- Because the founding of the ACT occurred later than the settlement of NSW, the documentary history of a property is more likely to be available in the ACT – records in NSW are more prone to loss or destruction. The "tradition" of effective record-keeping in the ACT is exemplified by the requirement that information about preparation of a BCIR and pest inspection report is to be kept in a publicly available government register (clause 12).
- The number of government authorities which regulate building works in the ACT is far fewer than exist in NSW. It is understood that for most parts of the Territory, there is effectively a single regulator, ACTPLA. By contrast, NSW has in excess of 140 local councils, each with their own slightly different procedures, and numerous other government authorities regulating building work (the Discussion Paper issued by LPMA earlier this year as part of the review of the *Conveyancing (Sale of Land) Regulation 2005* itself identifies several departmental stakeholders; other stakeholders include, for example WorkCover).
- The comparative area of the two jurisdictions means that the obtaining of expert quality reports is easier and cheaper in the ACT than would be the case in many parts of NSW.

In summary, the Committee believes that the ACT cannot truly be considered to be a "comparable jurisdiction" to borrow the terminology of the terms of reference.

3. *Investigate the types of reports that are available to help inform a potential purchaser of the physical condition of the building, including, but without being limited to, pest and building reports.*

The Committee believes that any proposed extension of the vendor disclosure regime to pest reports and building reports may raise sufficiently similar issues that they can be discussed together.

A standard building inspection report is generally a visual inspection only and may not identify major structural defects or other hidden problems. If a buyer has concerns about specific problems, he or she might obtain an additional assessment of the property from a suitable specialist. Similarly, a pest inspection report is given by a person who physically inspects a property and reports on the presence or absence of various pests. While the building inspection report should identify any visual damage that may have been caused by insect infestation, a pest report is directed to identify any pest related risk and will highlight past and present pest activity and steps to address to future pest activity.

Suppliers of pest and building certificates are unlicensed and unregulated. Any regime requiring the supply of reports by such persons faces the problem of the "tame" supplier. If suppliers are not regulated (even if only by a "negative licensing" regime) there is little that can be done at the supply end. Presumably, it could be made an offence for a vendor to fail to disclose that a report provider is in some way "related" to the vendor (or to provide a report where the provider is a related party) but how that would be policed and how related parties would be detected by the purchasers, seems all but insurmountable in the absence of a publicly available Government supplied register of reports, as exists in the ACT.

Pest and building reports are usually carried out before the sale contract becomes unconditionally binding on the purchaser. In those sales of residential property where the purchaser has the benefit of a cooling off period, it is common for that inspection to be conducted during the cooling off period. Indeed, the statutory duration of the cooling off period was chose to allow sufficient time for a purchaser to obtain appropriate quality reports within the cooling off period. In cases where no cooling off period applies, the inspections are carried out and reports obtained before exchange. The reports are thus current at the time the decision is made to purchase the property.

The length of time for which a report would remain valid is problematic in the event that such a report was a vendor disclosure requirement and attached to the contract. In very many cases, a purchaser would choose to either obtain their own report or need to update any report attached to the contract. There would appear to be little, if any, cost saving to the purchaser in such a system.

The existing system allows a prospective purchaser to choose their preferred building or pest inspector, to be present when the inspector inspects the property and negotiate the fee charged by the inspector. Were the vendor to arrange such reports those benefits would be lost (unless the purchase incurs the cost of their own reports). The Committee has concerns relating to attempts to pass on the cost of such reports to the purchaser – should these costs be capped, or regulated in some other way?

Pest and building reports are not usually obtained for strata properties although they are appropriate for some, for example, two lot strata sub divisions where each dwelling is constructed wholly within the lot boundaries.

The Committee believes any discussion about mandatory inclusion of reports should deal with strata inspection reports on an equal footing with pest and building reports. Although strata inspection reports do not involve a physical examination of the property, they normally disclose the owners' corporation's knowledge at the time of the last general or executive committee meeting of any physical defects in the common property. In addition, strata inspection reports deal with a number of other issues relevant to purchasers such as the state of finance s of the strata scheme and harmony issues between the occupiers.

4. Consider the cost and benefit of requiring the vendor to provide potential purchasers with access to one or more of the reports identified above.

The Committee considers that the disadvantages of such a system far outweigh any perceived advantages.

Purchasers, in the Committee's view, would benefit and receive more value in obtaining their own reports. Even though an unsuccessful bidder at auction may be put to some cost in obtaining their own pest and building reports, the Committee believes that cost does not justify making those reports compulsory vendor disclosure documents.

As stated earlier in this submission, any regime requiring the supply of reports where the supplier is unlicensed and unregulated faces the problem of the "tame" supplier. The absence of a licensing regime and compulsory indemnity insurance, coupled with minimal educational requirements for inspectors remains a drawback for making these reports compulsory.

The risk of a vendor "shopping around" to find a report which shows the property in the most favourable light also detracts from the concept that making these documents compulsory benefits purchasers. The Committee notes that, even if such a system were to be introduced, purchasers will in all probability be advised to continue to commission their own pest and building reports. This would not only be necessary to "update" the reports, if obtained some time from the date of exchange of contracts. The Committee notes that in the ACT, a purchaser is given a "very strong recommendation" (in one contract the Committee has viewed, the phrase is used at least three times) to obtain their own report.

There is an existing and tested vendor disclosure scheme operating in NSW. That regime applies penalties for failure to have the prescribed documents available to prospective purchasers where the property is "residential property". and more generally provides a remedy where the prescribed documents are not attached to the contract prior to signature by the purchaser. While it is an offence under the ACT legislation not to supply the documents, a purchaser has no rights in relation to the contract arising from the failure to attach the documents to the contract (except a limited remedy for the lack of an EERS). It would be necessary, if an "ACT style regime" was to be adopted, to have two parallel vendor disclosure regimes operating. This would lead to confusion and would not assist purchasers.

The only perceived advantage for purchasers in the supply of these documents is cost. Given that, even in the ACT, purchasers are strongly recommended to obtain their own reports, it would appear that this perceived advantage does not really benefit a purchaser.

5. Consider whether the same requirements may apply to property offered by auction and/or private treaty.

The Committee has already outlined its reasons for opposing a proposal that vendors be required to supply building and/or pest reports by attaching them to contracts for the sale of land.

The Committee does consider, however that there is arguably some merit in requiring the availability of those reports for some sales by auction because no cooling off period

is available. The Committee does not agree that the documents should be attached to the contract but consideration could be given to amending the *Property Stock and Business Agents Act 2002* (and the accompanying regulations) to require the real estate agent engaged to act in respect of the sale by auction to make available to bidders identified quality reports. The Committee noted that the Act currently requires the agent to take all reasonable steps to make an approved consumer guide available (section 71(2)). A similar provision relating to quality reports would be far preferable to making those reports prescribed vendor disclosure documents for attachment to the contract for sale.

Conclusion

The Committee does not consider that a cost/benefit analysis justifies altering the existing vendor disclosure regime to require vendors to supply building and/or pest reports by attaching them to contracts for the sale of land.

As Chair of the Committee, I am happy to discuss the Committee's concerns further if required.

Yours sincerely,

Mary Macken
President