THE LAW SOCIETY
OF NEW SOUTH WALES

Our ref: PLC:CBgl031023

3 October 2023

Decennial Liability Insurance Consultation
Policy and Strategy,
Better Regulation Division Department of Customer Service
Locked Bag 2906
LISAROW NSW 2252

By email: BCR@customerservice.nsw.gov.au

Dear Sir/Madam,

Better protection against apartment building defects

Thank you for the opportunity to comment on the Regulatory Impact Statement, Mandating Decennial Liability Insurance (DLI). The Law Society's Property Committee has contributed to this submission. Our responses to the questions raised in the Regulatory Impact Statement (RIS) are provided in the attached comments table.

General comment

The Law Society broadly supports the introduction of mandatory DLI, as it will provide improved consumer protection, particularly in relation to apartment buildings higher than three storeys. As a strict liability approach, and insurance policy of first resort, it should, by its nature, deliver quicker consumer outcomes. It will enable greater focus on the timely remediation of defects, rather than consideration as to which party may be at fault before remediation can commence.

Notwithstanding our support for mandatory DLI, the importance of the development of a mature sustainable DLI market in delivering the intended policy objective cannot be underestimated. This is recognised in the RIS, and we note Appendix D – DLI market maturity evaluation matrix. We therefore support the proposed close monitoring of the development of the market for DLI, and the adjustment of the transitional period to mandatory DLI as may be required.

Additional matters

We wish to raise several additional matters for further consideration as set out below.

Timeline of the DLI policy

The timeline of a DLI policy is discussed on page 16 of the RIS which states:

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> The DLI policy will be taken out between development consent approval and before the *first* Construction Certificate (**CC**) (or Complying Development Certificate (**CDC**)) is issued to assist consumer confidence in the pre-sales market. It will be paid at the first Occupation Certificate (**OC**), and be in force from the issue of the final OC to ensure that the building is covered by a DLI policy before the developer hands over the building to the new building owner/s.

Page 16 of the RIS also states:

> …cover commences from the date final OC is issued (until the end of the decennial period), at which point the insurer can conduct a cumulative assessment of the completed building work. Although **this presents the risk that if DLI is not offered by the insurer at this point** due to non-compliant building work, this would prohibit an OC being issued, preventing the completion of the sale to prospective homeowners, … (**emphasis added**)

It is quite likely that prior to, or during the construction of the building, purchasers would have entered into off the plan purchase contracts. These purchasers would have assumed DLI would be in place when the purchase is completed, and, as mentioned by the RIS, this would likely have been referred to in marketing material for the development (for example, page 102 of the RIS). We are concerned with the impact of an insurer not proceeding with the provision of DLI at this stage on these purchasers. While we appreciate that the final occupation certificate will not issue if DLI is not in place, and this is itself an added consumer protection,[1] the purchasers under these contracts are left in an invidious position. In our view, further consideration needs to be given to the consequences of an insurer not providing DLI at this advanced stage of the construction timeline.

Time limit on the builder to do remediation work at first instance

Page 82 of the RIS states:

> Under DLI, homeowners who identify defects will be encouraged to engage with the builder and NSW Fair Trading to remedy defects in the first instance. The insurer would be notified so that if the dispute could not be resolved between the parties, the policy would operate to protect the homeowner.

We do not support the builder being provided an opportunity to remedy the defects in the first instance and in our view, this dilutes the policy as a policy of first resort and reduces the level of consumer protection afforded. Our preferred position is that, upon a defect manifesting, the building owner makes a claim under DLI, then the insurer organises remediation and the insurer recovers the cost from the developer/builder.

If the builder is to be provided with an opportunity to remedy the defects in the first instance, at the very least there should be a specified timeframe within which the remediation must occur, failing which, the DLI policy will be triggered. Without this mechanism, timely remediation of defects, a primary object of the reforms, is unlikely to be achieved, in our view.

Mixed use developments

We suggest that consideration needs to be given to the operation of the DLI scheme in relation to mixed use developments, containing part residential premises that will be subject to DLI and part commercial premises that will not be subject to DLI. For example, if the premium for DLI is based on a percentage of the contract value of the project (as referred to on page 65 of

[1] Noted on page 52 of the Decennial Liability Insurance Ministerial Advisory Panel Advice to NSW Government, dated August 2022, accessed at: decennial-liability-insurance-discussion-paper - panel.pdf

the RIS), how would the premium be calculated if a significant part of the building was going to be used for commercial purposes?

Strata Hub and DLI

We support the inclusion of information on the Strata Hub as to whether a scheme has a DLI policy in place (as referred to on pages 102–103 of the RIS) and note this will be particularly useful during the transition to mandatory DLI. We would be interested in participating in any consultation on changes being made to the Strata Hub in relation to DLI.

Any questions in relation to this letter should be directed to Gabrielle Lea, Senior Policy Lawyer on (02) 9926 0375 or email: gabrielle.lea@lawsociety.com.au.

Yours faithfully,

Cassandra Banks
President

Encl.

Mandating Decennial Liability Insurance – Regulatory Impact Statement – August 2023
Feedback from the Law Society of NSW

No.	Question	Law Society comments
Options for achieving objectives		
1.	Do you consider there should be an extension of time to enable an insurer to initiate proceedings to protect their right of subrogation against the at-fault party where a claim is made under a DLI policy towards the end of the limitation period? Why?	Yes. In our view, it would be appropriate to provide an extension of time to allow an insurer to initiate proceedings to protect their right of subrogation against the at-fault party where a claim is made under a Decennial Liability Insurance (DLI) policy towards the end of the limitation period. This appears to be a reasonable and fair approach. It should also contribute to the sustainability of DLI, as the absence of such an extension would be a disincentive to an insurer entering the market.
2.	Do you consider 24 months from the time the claim is made under the policy is reasonable? Why?	Given the experience of insurers, we expect that a 12-month extension of time, rather than 24 months, would be sufficient where a claim is made under a DLI policy towards the end of the limitation period. In our view, a period of twelve months should be sufficient for the insurer to make all necessary investigations and commence proceedings. We also suggest that precision is required in defining the period that would be regarded as "towards the end of the limitation period". We suggest that within the last six months of the 10-year limitation period would be an appropriate approach. We note that under s 18E(1)(e) of the *Home Building Act 1989*, if the breach of warranty becomes apparent within the last six months of the warranty period, proceedings may be commenced within a further six months after the end of the warranty period. In our experience, this approach has worked reasonably well, and given the broad similarities between the two contexts, it would be an appropriate approach for DLI.
3.	What impacts do you consider the extension of time to initiate proceedings will have upon practitioners in the industry?	Any extension will impact the premium practitioners pay for professional liability insurance, the need to obtain lengthier run-off cover, and the time during which records must be retained, as referred to on page 37 of the Regulatory Impact Statement (RIS).
Mandatory DLI - DLI is mandated after a transitional period		
6.	Do you consider any other indicators are necessary for the assessment of market maturity? If so, please specify what these are.	When considering whether adequate DLI is being provided by the market, we suggest that consideration should also be given to the exclusions in available policies. It may also be appropriate to consider prescribing minimum standards or prohibiting certain policy exclusions, to ensure the intended level of consumer protection is in fact provided. However, this will need to be balanced with the need to encourage insurers to enter the DLI market.
7.	Do you agree that if performance against the evaluation matrix indicates the market is not ready to transition to a mandatory model, then mandatory DLI be deferred for an extended transitional period?	We agree that if the DLI market is not sufficiently mature, mandatory DLI should be deferred for an extended transitional period. We note that there are a number of significant transitional issues in moving from the current Strata Building Bond Inspection Scheme (SBBIS) to DLI that will require adjustment if the transition period is extended.

No.	Question	Law Society comments
Voluntary DLI – DLI as a voluntary option after transitional period		
8.	Do you consider there are any other risks in proposing mandatory DLI, that have not been explored in the RIS? What are they?	We suggest consideration should be given to the risk of insolvency of one or more of the insurers. The consequences for the scheme if a particular insurer becomes insolvent should be considered before proceeding. Although this is linked to the questions of market maturity, in particular the number of insurers, the consequences of an insolvent insurer on the operation of the scheme and impacted consumers should be considered in our view.
Proposed exemptions		
9.	Do you agree the building types outlined above should be exempted from the DLI scheme? Why?	Generally, we support the proposed exemptions. We note that a number of the exemptions are based on the original owner remaining the owner beyond 10 years, being the limitation period that would apply if DLI was in place. This is appropriate as the original owner does not need the same protections afforded by DLI. However, we suggest further consideration needs to be given to the circumstances where, unexpectedly, ownership changes before the expiry of 10 years, and DLI is not in place due to an exemption. We query whether the original owner should be obliged to seek DLI for the balance of the 10-year period, assuming an insurer was willing to provide such cover, or whether this should be dealt with as a matter of vendor disclosure, such that the vendor is obliged to disclose to the purchaser that DLI cover has not been taken out in respect of the property. We suggest that it would be unlikely that an insurer would be willing to provide DLI in these circumstances, and that vendor disclosure is a more realistic approach. A useful parallel can be drawn with the disclosure obligations that apply when an owner-builder sells a property that does not have the benefit of insurance under the *Home Building Act 1989* (HBA), within seven years and six months after the owner-builder permit issued. Under s 95(2) of the HBA, the contract for the sale of such land must contain a conspicuous consumer warning that an owner- builder permit was issued in relation to the land, and that work done under an owner-builder permit is not required to be insured under the HBA (unless done by a contractor to the owner-builder). Essentially the purchaser is alerted to the fact that insurance that the purchaser may mistakenly assume would apply does not actually apply. A similar approach is appropriate, in our view, in relation to properties exempted from DLI where ownership changes before the expiry of 10 years. **Build-to-rent properties** As described on page 105 of the RIS, the exemption would apply to build-to-rent properties where the building does not include a Class 2 component subject to strata title, and the property is required to be held for at least 15 years. The consumer protections afforded by DLI or SBBIS are not needed in such a case, as the original owner can seek direct recourse in relation to any emerging defects. We support the exemption provided the *original owner is still the owner* of the property during the period in which

No.	Question	Law Society comments
		DLI or SBBIS would otherwise apply. Care needs to be taken regarding the terminology used, as the vehicles and structures for build-to-rent properties can be quite varied and complex. We note that the eligibility criteria for this exemption also includes that "the build-to-rent model must comprise at least 50 self-contained dwellings used specifically for the purpose of build-to-rent that are made available for use as affordable housing or social housing for a continuous period of 15 years". Neither the NSW Treasurer's Guidelines[1] nor Revenue Ruling G 014[2] mandate the criteria that the 50 plus self-contained dwellings used specifically for the purpose of build-to-rent must also be available for use as affordable housing or social housing. The properties can be used for affordable housing or social housing if so designated, but they do not necessarily have to be used in that way to qualify for the exemption. That is, it is sufficient if at least 50 self-contained dwellings are used specifically for the purpose of build-to-rent. We do not support the build-to-rent exemption being further limited, as seems to be the intent, and we suggest that in any event this should be clarified. As discussed above, consideration needs to be given to the consequences of a change in circumstance, such as sale prior to the expiry of the required 15 year holding requirement. **Social housing that is held by a social housing provider for 10 years** We similarly support the proposed exemption for "social housing that is held by a social housing provider for 10 years after occupation, provided that the properties are not subject to strata during this time" as referred to on page 105 of the RIS. We query whether this should be limited to the situations where the social housing provider is the original owner and remains the owner for 10 years. **Smaller Class 2 buildings** We support the proposed initial exemption for smaller Class 2 buildings until DLI is mandated and note that these properties will remain subject to the Home Building Compensation Fund (HBCF) until then. We further note that developers of smaller Class 2 buildings who elect to take out a DLI policy before DLI is mandated, will not be required to take out HBCF insurance in addition to DLI. This is an appropriate approach in our view, as it supports the transition to mandatory DLI. **Change of use** We support the proposed exemption for buildings that become class 2 through change of use, outlined on page 106. We also support the Panel's recommendation that change of use applications during the first 10 years of a building's life be required to obtain DLI for the balance of the 10-year period after the final OC issued for the original building. However as flagged above, there may be difficulties obtaining such insurance.

[1] Treasurer's Guidelines for the Reduction in Land Value for Certain Build-to-rent Properties, for Land Tax Purposes.pdf (nsw.gov.au), accessed at 19 September 2023.
[2] Build to rent | Revenue NSW, accessed at 19 September 2023.

No.	Question	Law Society comments
		The RIS also notes that the Government will monitor buildings subject to change of use to ensure that this is not used as an avoidance measure, which we support**.** In our view, all of the exemptions should be monitored to ensure that the exemptions are operating as intended and the occupants of exempt buildings are adequately protected in the absence of DLI. On page 106 of the RIS, reference is also made to mandating disclosure in sale and contract material that the property does not have the benefit of the SBBIS or DLI to put prospective homeowners on notice. As mentioned above in the context of change in ownership, we would similarly support such a requirement. We would be pleased to participate in further consultation on possible disclosure requirements where exempted properties are sold prior to the expiry of the 10-year period after the occupation certificate has issued.
10.	Should other building types be exempted from the DLI scheme? If so, which other building types should be exempted and for what reason?	We suggest consideration should be given to an exemption for affordable housing where the building is owned by an affordable housing provider for 10 years after occupation, provided that the properties are not subject to strata during this time. In our view, this exemption should be considered on the same footing as the exemption for social housing.
11.	Should smaller Class 2 buildings be captured by the SBBIS instead of being exempt, during the transitional period?	No, given the issues that have been identified with the SBBIS as a means of consumer protection, we do not support smaller Class 2 buildings being captured by the SBBIS, instead of being exempt during the transitional period. This approach would also increase the administrative burden in continuing to run the SBBIS beyond the transitional period, which seems counterproductive. We further note that these properties will remain subject to the HBCF until DLI is mandated.