

UNCLASSIFIED

Inquiry into the quality of recently constructed buildings in the ACT

Discussion Paper

Standing Committee on Economic Development and Tourism

UNCLASSIFIED

UNCLASSIFIED

UNCLASSIFIED

UNCLASSIFIED

Contents

Introduction.....	4
Economic Cost	4
Current ACT arrangements	5
Examples of measures in place in other States.....	10
Current issues in the ACT for the inquiry to consider	10

UNCLASSIFIED

Introduction

The ACT has experienced high population growth in recent years, with as many as 5,000 new residents a year. The ACT's population is expected to reach 500,000 by 2032. This will require an additional 40,000 households be built over the coming decade. With so much construction taking place, it is increasingly important to ensure the regulatory framework is robust and adequate.

The resolution establishing the Standing Committee on Economic Development and Tourism (the Committee) charges it with responsibility for economic and business development, and market and regulatory reform. Within this scope, the Committee will inquire into and report on the construction of buildings in the ACT with particular reference to the quality of new buildings and any potential or actual causes of poor building quality in the ACT.

Economic Cost

The economic cost to the ACT and to the ACT Government are highly significant. A report from the University of NSW estimates that for every \$100 million spent on construction, over \$5 million is wasted as a result of poor building quality¹. If this figure applies to the ACT construction industry, over \$114 million would have been spent rectifying the investment in dwellings made in 2016-17². This figure may not include the legal costs the ACT Government faces in pursuing disputes through the tribunal and law courts.

Access Canberra reports they received 305 complaints related to planning laws and 220 complaints related to construction laws in 2016-17. To put this in context, there were 5,524 dwellings approved for the same year³, meaning Access Canberra received complaints on the equivalent of ten per cent of the housing stock approved in 2016-17.

Often regulation is viewed as a burden on businesses that should be avoided where possible. However it is important to note that all of this represents a deadweight loss to the economy that could be avoided, with the resources and money being used for more efficient and meaningful purposes.

The impact of this wastage goes much further than the construction industry. Major industries providing inputs to the construction industry include construction services (42.9 per cent); manufacturing (26.9 per cent); professional, scientific and technical services (7.9 per cent); rental, hiring and real estate services (3.8 per cent); and wholesale trade (3.7 per cent)⁴. Viewed in this

¹ Building Quality Policy, Master Builders ACT

² ABS Cat. No. 5220.0

³ ABS Cat. No. 8731.0

⁴ Source: ABS Cat. No. 5209.0.55.001

UNCLASSIFIED

light, an appropriate regulatory regime can free up resources across the local economy to be diverted into far more productive endeavours than rectifying defects in the construction and building industry.

The economic inefficiencies resulting from poor build quality are a regulatory issue created by the presence of imperfect competition in the housing market. The Directorate has already invested a great deal of time and resources into educating home buyers on their rights when purchasing a home. However, buying a house is not something the average person does on a regular basis, and so the buyer is always at a disadvantage.

The asymmetry of information a buyer of a new home experiences is a key reason why perfect competition is not possible in the housing market. It is for this reason that the market for housing and land are regulated.

However, regulators must regularly revisit the regulatory regime to ensure it is up to date and relevant. This is partly due to the unintended consequences of reform. When one set of loopholes close, it often unintentionally creates another potential set, creating an ever recurring process of reform and review.

Having responsibility for market and regulatory reform, the Committee is best placed to consider the issues around build quality within the construction industry that are creating these economic inefficiencies. In holding a public inquiry into build quality in the ACT, the Committee is able to make recommendations on how reforms might be implemented to deliver an economic dividend to the construction industry in the ACT, and the economy (in addition to improving outcomes for home buyers).

Current ACT arrangements

Construction Occupations Registrar

The Constructions Occupations Registrar (the Registrar) must be a public servant with relevant qualifications or experience in one or more of the following:

- Asbestos assessment;
- Building;
- Building assessment;
- Building surveying;
- Plumbing, draining, gas fitting;
- Electrical;
- Engineering;
- Works assessment;
- Administration of building or construction industry regulatory schemes.

UNCLASSIFIED

UNCLASSIFIED

The functions of the Registrar are:

- Keep registers under the Construction Occupations (Licensing) Act 2004;
- Administer the operational laws, including the Building Act, Water and Sewerage Act, Electricity Safety Act;
- Decide applications for licences;
- Maintain the standard of construction occupations by acting on complaints and providing licensees with information about developments in the construction industry.

The Registrar's oversight of the licensing renewal process has been increased to consider compliance history, including any reported issues around consumer protections, contract disputes, development application documents not being followed, and quality issues. Where a renewal applicant's history demonstrates persistent non-compliance, the Registrar can order director training or specific training for builders depending on the nature of the issue.

The Registrar is also responsible for oversight of the demerit point system. This system allows conditions to be put on licenses that restrict the type of build, add check points for inspection and certification. In time, applicants for renewal with persistent issues may be required to sit the practical exam.

Building Certifiers

A building certifier is licensed by the Registrar. They are to act independently and are appointed by the land owner(s). Their role is to ensure the building is constructed in accordance with the building laws and associated technical requirements including the National Construction Code, Building Code Australia.

The building certifier is responsible for assessing building plans to determine whether the proposal can be constructed in accordance with the approved plans and the applicable legislation and codes.

The building certifier is responsible for inspecting the building work during the construction phase. *The Building Act* identifies a number of stages of building work where an inspection by the building certifier is required. These include:

- The completion of excavation, placement of formwork and placement of steel reinforcing for the footings before any concrete for the footings is poured;
- Completion of the structural framework before the placement of any internal lining;
- Completion of placement of formwork, and placement of steel reinforcing, for any reinforced concrete member before any concrete for the member is poured;
- Final inspection of the building works at completion.

It is the responsibility of the builder to advise the building certifier when each stage is ready for inspection.

UNCLASSIFIED

UNCLASSIFIED

A building certifier is not responsible for checking all aspects of the quality of the work. They are responsible for the build being compliant with the code and plans. The quality of the build is the responsibility of the builder and land owner. Some certifiers might offer additional service at a fee. Specific requirements for quality, finish and products must be agreed to between the purchaser and the builder to be included in the contract.

Certificate of completion

When the builder finishes the building work subject to building approval, the building certifier will undertake a final inspection. This inspection does not confirm all works under the contract such as landscaping, driveways, fences and window furnishings. When the building certifier is satisfied the building work complies with the building approval and associated technical requirements, they will issue a certificate of completion and lodge any final certificates or paperwork with the Registrar.

If the building project includes electrical, plumbing or gas work, those licensees, often contracted by the builder, have the responsibility to ensure they lodge the paperwork with the Registrar. ACT Government inspectors may then inspect the works.

Inspectors from the office of the Registrar may undertake inspections of the installation of electrical and plumbing/gas fitting work.

Once all the inspections are cleared and tested by government and all relevant clearances have been received by the Registrar, the land owner can make an application to the Registrar for a certificate of occupancy and use. The certificate will be issued by the Registrar once all clearances are received and there are no outstanding issues.

The certificate of occupancy and use indicates that, based on the information provided by the building certifier and results of any government inspections of the electrical, gas or plumbing work, the building is fit for use in the class which is stated on the certificate.

It is illegal in the ACT to occupy a premise where the certificate of occupancy and use hasn't been issued.

Construction Occupation Licensing

There are currently 50 classes of license in the ACT. Residential building licenses are mainly based around the following categories:

- Class A – single storey dwelling;
- Class B – up to 3 storeys; and
- Class C – everything except work that requires a specialist license.

UNCLASSIFIED

UNCLASSIFIED

There are qualifications requirements relevant to each category that a licensee must hold and maintain. Regardless of the type class, an applicant must be able to demonstrate two years relevant documented experience to be eligible for a license.

Under the Construction Occupations (Licensing) Act 2004 all builders and building surveyors (building certifiers) must be licensed by the Registrar. Unlike some other Australian jurisdictions, the ACT does not currently licence:

- Architects;
- Engineers;
- Designers;
- Water proofers;
- Fire proofers;
- Carpenters;
- Painters;
- Concreters.

To obtain a licence individuals are required to demonstrate they have the relevant qualifications, experience and, in most cases, access to adequate financial resources in order to undertake the works authorised under the licence. The Registrar is responsible for assessing licence applications, issuing licences and ensuring licensees continue to meet the required laws relating to building and licensing in the ACT.

The ACT has recently introduced a practical examination for new Class C license applicants. It is the only jurisdiction to do so while others require competency based testing. The exam in the ACT will gradually be introduced for Class A and B applicants.

Interstate transfers cannot be made contingent on ACT licensing requirements. Therefore an applicant who holds a license issued in another jurisdiction will not be required to sit the exam.

Building Disputes

Disputes between builders, trade contractors, architects, designers and consumers may occur for a number of reasons, including:

- inaccurate or insufficient documentation;
- poor communication;
- poor quality of work;
- delays in supply and construction;
- lack of knowledge or experience in the building process.

UNCLASSIFIED

UNCLASSIFIED

Where issues are of a technical compliance nature, the building certifier should be engaged and a complaint can be made to the Registrar. Where the issue is contractual, such as relating to payments, quality of inclusions, communications etc. there is a dispute resolution service available. Alternatively, the dispute can be heard either by a tribunal or court proceedings.

Statutory warranties

As per the Building Act, every contract for the sale of a residential building and every contract to carry out residential building work is taken to contain a warranty except if the building work is exempt from requiring building approval and/or the cost of works is less than \$12,000.

Under these provisions the builder warrants the following:

- That the residential building work has been or will be carried out in accordance with the Building Act.
- That the work has been or will be carried out in a proper and skilful way and:
 - in accordance with the approved plans; or
 - if the work involves or involved handling asbestos or disturbing friable asbestos – in accordance with approved plans that comply with the Building Act in relation to asbestos.
- That good and proper materials for the work have been or will be used in carrying out the work.
- If the work has not been completed, and the contract does not state a date by which, or a period within which, the work is to be completed – that the work will be carried out with reasonable promptness.
- If the owner of the land where the work is being or is to be carried out is not the builder, and the owner expressly makes known to the builder, or an employee or agent of the builder, the particular purpose for which the work is required, or the result that the owner desires to be achieved by the work, so as to show that the owner is relying on the builder's skill and judgement – that the work and any material used in carrying out the work is or will be reasonably fit for the purpose or of such a nature and quality that they might reasonably be expected to achieve the result.

The period for which statutory warranty operates is:

- six years after the completion day for the work for residential building work in relation to a structural element of a building; and
- two years after the completion day for the work for residential building work in relation to a non-structural element of a building.

The completion day is taken to be the day the work is completed or the day the contract relating to the work ends, whichever is the later.

UNCLASSIFIED

UNCLASSIFIED

Residential building insurance

Prior to a building certifier being able to issue a commencement notice to allow building work to be undertaken on the land, they must be satisfied the application for a commencement notice contains:

- a residential building insurance policy for the work;
- a certificate issued by an approved insurer (currently QBE Insurance) stating that the insurer has insured the work under a residential building insurance policy; or
- a fidelity certificate for the work issued by the trustees of an approved scheme (currently the Master Builders Association Fidelity Fund).

It is the responsibility of the builder to obtain the appropriate insurance.

Examples of measures in place in other States

All other States, with the exception of Tasmania and the NT, have in place a minimum threshold for the value of residential building work where a tradesperson or builder carrying out work above that value must be licensed. The thresholds range from as low as \$3,300 in Queensland (\$1,100 if it involves hydraulic services design) to \$20,000 in WA.

A number of States maintain a list of required qualifications and/or experience that licensees must hold and keep up to date in order to remain licensed. This list is regularly reviewed in light of legislation, education providers and industry requirements. Some States also have a continuing professional development requirement as part of their licensing requirements.

SA offers an extended statutory warranty, where claims can be made for up to five years after the work was completed, and builders may be liable for defective building work for ten years.

Queensland is the only State or Territory to apply a comprehensive registration system for engineers, recognising the position of trust and responsibility engineers hold in the community. The Queensland system applies extraterritorially, requiring professional engineering services carried out interstate or overseas but destined for Queensland to comply with the standard.

While many States fine licensees for not rectifying work, the Queensland system has a demerit point system, where failure to comply with a direction from the regulator may result in the issuing of demerit points. This system means that consistent poor quality work will result in the loss of license.

Current issues in the ACT for the inquiry to consider

Licensing System

In response to a recommendation of the Building Quality in the ACT Report, the ACT Government committed to undertake a policy review of the ACT *Building Act 2004* (the Act) and the associated

UNCLASSIFIED

UNCLASSIFIED

regulatory and administrative system. The ACT commenced this process in November 2015 with the release of the discussion paper *Improving the ACT Building Regulatory System*. This paper canvassed reform options that would strengthen the capacity of building regulation in the ACT to protect the health, safety and wellbeing of the public as well as those involved in the construction process from incompetent or unfair practices.

The consultation covered a broad spectrum of the community including construction industry professionals and associations, training bodies, consultants, civil engineers, owner-occupiers, landlords and advocacy groups. Most submissions from industry and community members support the ACT Government's intentions to improve the ACT building regulatory system.

The review did note that in order to pursue these objectives, the current legislation must first make the operation and understanding of the current system more clear. The reforms taken to date have done just that. The *Building and Construction Legislation Amendment Act 2016* seeks to make current obligations clear. Further reform is yet to be undertaken.

Parties within the industry have raised the view the licensing regime should be extended to include other professions within the industry. The design of the existing system is to place the onus on the builder, having responsibility for coordinating the worksite and the timing of various trades completing their work.

This model may currently be under pressure with the prevalence of what is known as phoenix activity, where the assets from an indebted company are transferred to a new one to avoid paying its liabilities. In the case where phoenixing occurs, the purchaser is often left with no recourse as the trading company they are chasing for rectification has been dissolved. In some cases, the liability may fall onto the certifier, being the last one standing after the builder and developer have disappeared.

There are examples in other States of expanded licensing regimes that include professions such as water proofers, fire proofers, architects, carpenters, and engineers. Consideration could be given to how these systems work, and whether they have been able to address some of the issues being faced in the ACT.

Potential for conflict of interests in building certification

Currently there are potential conflicts of interests within the building certification regime in the ACT. Certifiers being paid directly by the builder may present one example. This type of direct payment in a regulatory framework can result in unwanted outcomes, and the inquiry should consider whether this is the most appropriate model for transparency and accountability within the certification process.

UNCLASSIFIED

UNCLASSIFIED

The inquiry could consider how the payment of certifiers can be done in a way that removes this potential conflict. The ACT is the only jurisdiction with fully privatised certifiers. Consideration could be given to models in other States such as randomly assigning certifiers to projects, as some other States do, or having a small number of government certifiers who a buyer can request in place of a private certifier.

Perhaps the largest conflict is in second buyer scenarios, or when home buyers are purchasing off-the-plan. In this scenario the developer also acts as the purchaser, meaning the developer has the right to select the certifier themselves to represent the final buyers who will purchase properties from the developer, with the developer profiting of these sales.

Build quality requirements

Currently build quality is not the responsibility of the independent certifier. A purchaser seeking a certain degree of quality on any or all of the building and fixtures must negotiate this with the builder and have it included in the contract. Many home buyers are likely to be unaware of this, or are not skilled or prepared to negotiate.

Again the most striking example is in the case of off-the-plan projects where the developer is the purchaser. This means the developer is again responsible for any build quality requirements, while at the same time, profiting directly from the project.

How the relationship between builder and developer operates is an area that may be a key target in addressing these issues. Finding ways of reducing the rent a developer can extract on a development might put less cost pressure on the builder, who might then be less inclined to reduce costs. This might go some way towards levelling the bargaining towards the purchaser, and improve the quality of builds.

There are examples in other States of standard contracts and statutory requirements in contracts, which are designed to ensure greater compliance on the part of developers and builders.

Regulator and alternative dispute mechanisms

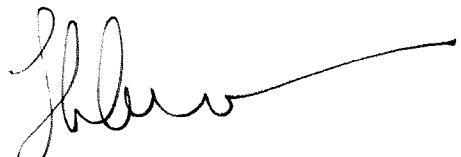
Currently the process of obtaining a rectification order, or similar recourse, is difficult, costly and may require extensive litigation. The cost to the individuals and companies involved, the ACT Government and the economy is significant, using money that could be better spent elsewhere, creating an economic dead weight.

The system also propagates the potential for market failure, as purchasers are likely to be ill-informed on the mechanisms available to them in resolving a dispute. This creates asymmetric information on the part of an actor within the market, restricting the ability for the market to achieve efficient outcomes.

UNCLASSIFIED

UNCLASSIFIED

The inquiry will seek to consider what oversight might resolve these economic problems. Offering a simpler, easily accessible method of dispute resolution that can readily enforce compliance will only improve the economic efficiency of the construction industry and the broader economy.



Jeremy Hanson MLA

Chair

9 April 2018

UNCLASSIFIED

