

# Victoria's Consumer Protection Framework for Building Construction





VICTORIA

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Victorian  
Auditor-General

# Victoria's Consumer Protection Framework for Building Construction

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President  
Legislative Council  
Parliament House  
Melbourne

The Hon. Telmo Languiller MP  
Speaker  
Legislative Assembly  
Parliament House  
Melbourne

Dear Presiding Officers

Under the provisions of section 16AB of the *Audit Act 1994*, I transmit my report on the audit *Victoria's Consumer Protection Framework for Building Construction*.

This audit examined the performance of the Victorian Building Authority, the Building Practitioners Board, Consumer Affairs Victoria (CAV) and the Victorian Managed Insurance Authority as they provide functions key to building regulation and to the consumer protection framework in domestic building.

I found that the existing framework does not adequately protect consumers and that there is a pressing need to improve consumer understanding of the system. The registration system does not ensure that the only practitioners who are registered are qualified, competent and of good character and the disciplinary system is not protecting consumers, as current sanctions are ineffective in deterring practitioner misconduct.

CAV's conciliation and dispute resolution functions provide only limited consumer protection because it cannot compel parties to conciliate or enforce compliance with conciliation outcomes. Domestic building insurance is widely misunderstood, provides only limited protection for consumers and is significantly more costly than it needs to be.

I have made recommendations to all the relevant agencies and to the Department of Environment, Land, Water & Planning and the Department of Treasury and Finance to improve the framework and its implementation. Prompt action is required to ensure domestic building consumers are appropriately protected.

Yours faithfully



John Doyle  
*Auditor-General*

28 May 2015



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# Auditor-General's comments



John Doyle  
*Auditor-General*

Building or renovating a house involves a significant financial and emotional investment for consumers and is often the most expensive investment that people make in their lifetime.

Yet in the 2011 *Australian Consumer Survey* report nearly one in three building consumers reported experiencing a problem, mainly to do with poor workmanship. Throughout this audit, I have received correspondence from consumers highlighting the issues that they have faced and the personal, sometimes profound, impact that trying to resolve these issues has had on their lives.

Given these impacts, and the significance of the building industry to the Victorian economy, Victorians are entitled to a consumer protection framework for domestic building construction that provides appropriate protection when they need it. This is not just important for consumers, but also for builders themselves who have an interest in maintaining a personal and industry reputation for quality workmanship, professionalism and value for money.

At a minimum, an effective building consumer protection framework should include the following features:

- consumers are able to easily understand and navigate the system
- assurance that only competent practitioners are involved in building works
- confidence that buildings are constructed to required standards and that where standards are not met this is detected and addressed early
- scope to hear and resolve any disputes in a timely manner by an authority with power to require conciliation and enforce outcomes
- recourse to an appropriate safety net of insurance protection where a builder does not fulfil their obligations.

My audit found few of these features are in the existing framework and as a consequence Victorian consumers are not receiving the protection they deserve.

The Victorian consumer protection framework for building construction is far too complex with multiple agencies responsible for different elements. While there is a lot of information, it can be very difficult for consumers to navigate the system and to find timely and cost effective solutions.

The current registration and discipline regimes do not ensure that the only practitioners who are registered are qualified, competent, and of good character. Current dispute resolution services, consisting of voluntary conciliation with unenforceable outcomes, provide only minimal protection. Oversight of building surveyors is also deficient and monitoring and compliance activities do not yet provide assurance that domestic building construction complies with minimum standards.

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The 'last resort' domestic building insurance scheme provides only limited protection for consumers and is significantly more costly than it needs to be—costing consumers an estimated additional \$21 million over the past four years. It is questionable whether this provides value for money for consumers who otherwise have no alternative recourse.

For more than a decade, the glaring shortfalls and weaknesses in the framework have been well known. VAGO's 2011 *Compliance with Building Permits* audit highlighted the pervasive failures of the then Building Commission, especially its fundamental failure to effectively discharge its legislative and regulatory responsibilities. In 2012, the Ombudsman also raised concerns with the 'vulnerability, integrity and administration of the registration system for building practitioners.' However, key agencies have failed to take sufficient, timely action to address these and other deficiencies.

Successive governments have consistently and regularly received advice about potential legislative and policy improvements to the consumer protection framework. However, recent proposed legislative and policy reforms failed to comprehensively address all of the issues and have again stalled, and consumers are paying the price. These issues now require urgent attention.

While there is no doubt that legislative reform is needed, agencies and regulators have sometimes been too quick to point to the technical boundaries and limits of their responsibilities and too slow to work together to ensure the existing consumer protection framework, flawed as it is, works as well as it can to protect consumers.

I have made a series of recommendations that focus on the key areas requiring improvement—practitioner registration and discipline, monitoring and compliance, dispute resolution and conciliation, consumer awareness, and the provision of builders warranty insurance. Addressing these recommendations will go a long way to providing an appropriate level of consumer protection and tackling the well acknowledged gaps and issues in the current framework.

In this audit, agencies themselves have not disputed my findings and I am pleased that they have accepted my recommendations and outlined actions to address them. I intend to revisit the issues identified in this report to examine progress.

I want to thank the staff from the agencies involved in the audit and the consumers and industry stakeholders who took the time to share their perspectives.



John Doyle  
*Auditor-General*

May 2015

# Audit summary

Building or renovating a house is typically the single biggest investment an individual consumer will make in their lifetime. While most consumers do not experience significant issues and problems with their builder, a significant number do. Consumers may be ill-equipped to manage a building contract and resolve building construction issues. For those consumers that do experience problems, the impacts can be profound—ranging from significant additional costs and time delays to extreme frustration, stress and anxiety.

A 2011 analysis published in the *Australian Consumer Survey* report found that 28 per cent of building and renovating consumers in Victoria reported experiencing problems, with the most common problem reported across Australia being poor workmanship, accounting for 63 per cent of problems. Throughout this audit, consumers told us of the personal impact that building disputes had on their lives.

A well-functioning customer protection regime is essential to ensure that both the incidence and impacts of building disputes and issues are minimised. It benefits not just consumers but also builders operating in the market who want to maintain an industry reputation for quality, service and integrity.

An effective consumer protection framework for building construction should have a number of critical features:

- Consumers and building practitioners should be aware of and have access to clear, comprehensive and timely information and advice on their rights and obligations.
- Rigorous registration, monitoring and disciplinary processes should ensure that only qualified, competent and suitable practitioners are allowed to operate.
- Independent, consistent and thorough monitoring of compliance with building standards and codes should enable the early identification and addressing of defects.
- Dispute handling processes should be easily navigable, low cost, simple and timely, and should achieve binding and enforceable resolutions.
- Consumers should have recourse to appropriate insurance which protects them in circumstances where they cannot otherwise achieve a timely and effective resolution of building defects and issues.

The current Victorian building consumer protection framework does not possess these features, and needs strengthening. Successive governments, reviews, inquiries and audits have acknowledged that the current framework has failed to provide adequate protection to consumers.

This audit examined whether the key elements of the current building consumer protection framework are effectively managed by relevant entities.

## Conclusions

The consumer protection framework for building construction does not adequately protect consumers. While critical weaknesses in the framework are well understood, proposed legislative and policy reforms have stalled and this has delayed the resolution of these weaknesses and compounded the detriment suffered by consumers. Key agencies have failed to take sufficient, timely action to address deficiencies identified in VAGO's 2011 *Compliance with Building Permits* audit, and numerous other investigations and inquiries.

There is a pressing need to improve understanding of the consumer protection framework, and awareness of the available tools and assistance, so that consumers and building practitioners alike have access to straightforward and timely information, and can understand their rights and obligations.

The current framework does not ensure that the only practitioners who are registered are qualified, competent and of good character because of the weaknesses of the registration system and the Building Practitioners Board's (BPB) ineffective management of both its registration and discipline regimes. Deficiencies in the Victorian Building Authority's (VBA) oversight of building surveyors, and a lack of coordination of monitoring and compliance activity across agencies, mean there is little assurance that domestic building construction complies with minimum standards. However, since its inception in July 2013, VBA has begun to address a number of VAGO's 2011 audit recommendations and to establish an appropriate governance framework in collaboration with BPB.

Existing dispute resolution services provide minimal consumer protection because parties cannot be compelled to undergo conciliation, and Consumer Affairs Victoria (CAV) cannot enforce the negotiated outcomes. Ultimately, it is unclear whether CAV's activities are reducing overall consumer detriment because it does not have performance measures that focus on outcomes.

Domestic building insurance (DBI) provides only limited protection for consumers and is significantly more costly than it needs to be. Government intervention in 2010 to direct the Victorian Managed Insurance Authority (VMIA) to provide DBI addressed the immediate risk associated with insurers withdrawing from the Victorian DBI market. However, this did not improve the level of protection for consumers and resulted in a more expensive, broker driven model for the provision of insurance. This higher-cost model has been in place for almost five years due to ongoing uncertainty about VMIA's future role in DBI, and has cost consumers an estimated additional \$21 million between July 2011 and July 2015. Decisions are needed on the future provision of and model for DBI.

While extensive, the 2013 *Victorian Domestic Building Consumer Protection Reform Strategy* and associated *Building Legislation Amendment Bill 2014* were not framed to address some of the fundamental deficiencies in the current building consumer protection framework. This includes the adverse impact of having non-mandatory conciliation on the capacity for early resolution of building disputes, and the fundamental conflict private building surveyors face between performing their statutory roles and looking after their business interests.

Successive governments have consistently and regularly received advice about potential improvements to the consumer protection framework, including resolving these issues. However, these issues have failed to be adequately addressed and now require urgent attention as part of deliberations on any future reforms to improve the overall effectiveness of Victoria's consumer protection framework for building construction.

## Findings

### Registration and discipline of building practitioners

The practitioner registration system administered by the BPB does not ensure that only practitioners who are qualified, competent and of good character are registered. This issue is compounded by the permanent nature of building registrations and the lack of effective triggers or mechanisms for reviewing practitioner competence.

The practitioner discipline system is critical to addressing practitioner misconduct and competence issues that may arise. However, the system is not operating effectively to protect consumers and current sanctions are not effective in deterring practitioner misconduct. Despite the critical role that building surveyors play in monitoring and enforcing building standards, they are over-represented in disciplinary inquiries, registration suspensions and cancellations, and reoffending. Yet, BPB does not systematically record, analyse or share the outcomes of its disciplinary system with other agencies to inform training or compliance programs which may reduce offending.

### Monitoring and compliance

VBA's performance and building permit levy audits are effectively the only forms of proactive, direct monitoring of building practitioner compliance, particularly for surveyors. However, longstanding legislative limitations to the effective administration of the building levy remain. The current regulatory framework also entrenches a long-recognised conflict of interest for private building surveyors who are assessing the compliance of other building practitioners while often also relying on them for work. This undermines the building surveyors' statutory role.

The effectiveness of VBA's monitoring programs in achieving the objectives of the *Building Act 1993* cannot be measured because VBA, like its predecessor the Building Commission, operates without an effective monitoring and evaluation framework. However, VBA has commenced action over the past year to address several of the recommendations from VAGO's 2011 audit report.



## Dispute handling

Participation in conciliation for domestic building disputes is voluntary, and its outcomes are unenforceable. CAV's building conciliation and dispute resolution functions provide only limited consumer protection due to CAV's inability to compel parties to undergo conciliation or to enforce compliance with the negotiated outcomes.

CAV is aware of the legislative limitations it faces and the extent to which these mitigate its effectiveness. It has repeatedly advised government and departmental heads about potential improvements to the consumer protection framework—including the need for mandatory conciliation and binding rectification orders.

CAV has also taken positive steps to address these limitations focusing on education and information programs that aim to help consumers avoid detriment and reduce noncompliance before it occurs.

A lack of relevant and appropriate performance measures for both CAV's and VBA's activities means that their effectiveness is not clear. CAV cannot be assured that all of its conciliation services are actively assisting consumers and reducing detriment.

Correspondence to the Auditor-General from building consumers indicates that CAV's functions are not well understood and are perceived as ineffective.

## Domestic building insurance

While government intervention in 2010, directing VMIA to provide DBI, addressed the risks to ongoing DBI provision associated with insurers withdrawing from the Victorian market, it did not improve the level of protection for consumers, indeed it added significantly to the cost of providing the insurance.

There was no comprehensive implementation plan in place before the government announced its intervention in the DBI market. This resulted in VMIA adopting a high-cost DBI delivery model as an interim measure and this has continued for almost five years as a result of ongoing uncertainty about its future role. The additional costs of this model, which we estimate at around \$21 million between July 2011 and July 2015, have ultimately been borne by consumers for little, if any, tangible benefit. An alternative delivery model would enable consumers to benefit from lower premiums and/or better coverage.

While VMIA's processes for managing DBI arrangements are robust, it has not fully exercised its rights under the agreement to assure itself about the adequacy of the systems and performance of the agent it appointed to manage many aspects of DBI provision, including the interface with brokers, assessing applications for DBI and recording details of all DBI policies issued.

The Department of Treasury and Finance (DTF) has overseen and supported VMIA's involvement in providing DBI. DTF and VMIA need to provide comprehensive advice to government on opportunities to improve the cost efficiency and consumer protection offered by DBI, or any replacement scheme.

## Information sharing and agency coordination

There is insufficient coordination and information sharing between agencies involved in the domestic building consumer protection framework. This means that despite the large volume of education and information provided, it is difficult for consumers to locate and use it.

CAV and VBA should, at a minimum, make the disciplinary register and other tools more prominent and linked between their websites to assist in educating consumers and reducing consumer detriment.

Systematic information sharing between all organisations could also assist others in identifying practitioners and businesses which represent potential compliance risks and in identifying trends in noncompliance.

Currently CAV shares information with VBA and BPB on a case by case basis, but there is no systematic exchange of intelligence between CAV, VBA and BPB on respective compliance activities, including practitioners who are party to a conciliation, currently under investigation, or are awaiting a disciplinary hearing.



A more coordinated approach to exchanging intelligence about practitioners would enable CAV to assist BPB and VBA to target their practitioner monitoring functions more effectively.

## Recommendations

Number	Recommendation	Page
1.	That the Department of Environment, Land, Water & Planning and the Building Practitioners Board, in consultation with the Victorian Building Authority, reviews the practitioner registration and discipline regimes, and advises government accordingly, so that: <ul style="list-style-type: none"> <li>only qualified, competent and suitable practitioners are allowed to trade</li> <li>practitioners have necessary building, business and financial skills and experience, appropriate resources and character, and fully understand their responsibilities and obligations</li> <li>monitoring provides assurance that practitioners maintain and update their skills over time and as building practices evolve</li> <li>practitioners' suitability for registration can be reassessed at the expiration of a finite registration period</li> <li>disciplinary systems and sanctions ensure that there is sufficient disincentive to engage in misconduct and that registered practitioners who do so can be excluded from trading</li> <li>data from registration and discipline regimes is collected and analysed to inform system improvements.</li> </ul>	41
2.	That the Department of Environment, Land, Water & Planning reviews the regulatory arrangements governing the engagement of building surveyors to ensure they support the independent and objective performance of their function to provide appropriate independent oversight of building and the building system.	41
3.	That the Victorian Building Authority reviews its monitoring and compliance framework, and takes action, including advising the Department of Environment, Land, Water & Planning where necessary, to: <ul style="list-style-type: none"> <li>identify poor practitioner performance and appropriately prosecute and/or refer for discipline</li> <li>prioritise the monitoring and enforcement oversight of relevant building surveyors</li> <li>clarify respective agency responsibilities for monitoring and compliance including expediting the establishment of a memorandum of understanding to clarify the roles of the Victorian Building Authority and councils for monitoring and enforcing compliance with the <i>Building Act 1993</i></li> <li>effectively administer the building permit levy including expediting the establishment of arrangements to allow the Victorian Building Authority to reassess and recoup underpaid levies, and require surveyors to remit levies promptly.</li> </ul>	41



## Recommendations – *continued*

Number	Recommendation	Page
4.	That Consumer Affairs Victoria reviews its dispute resolution and conciliation activities and advises government on options to improve their effectiveness, so that they are: <ul style="list-style-type: none"> <li>• easy to access</li> <li>• low cost, simple and timely</li> <li>• objective and outcome focused</li> <li>• supported by necessary powers to compel participation in conciliation and enforce compliance with negotiated outcomes</li> <li>• underpinned by relevant and appropriate performance measures and effective monitoring, reporting and evaluation to demonstrate effectiveness.</li> </ul>	60
5.	That Consumer Affairs Victoria and the Victorian Building Authority review their consumer education and awareness activities to ensure consumers have access to straightforward and timely information and advice aimed at enabling consumers and builders to: <ul style="list-style-type: none"> <li>• understand their rights and obligations under building contracts</li> <li>• understand the consumer protection framework and access required information to make informed decisions</li> <li>• be aware of the services available to assist with addressing consumer issues, and their limitations.</li> </ul>	60
6.	That the Department of Treasury and Finance works with the Victorian Managed Insurance Authority to review the adequacy and cost of the current domestic building insurance scheme and provide advice to government on options to lower premiums and/or enhance coverage for consumers.	85
That the Victorian Managed Insurance Authority:		
7.	obtains certainty about its ongoing role in domestic building insurance provision and implements the most efficient delivery model	85
8.	alters the domestic building insurance policy certificate to show the base premium amount	85
9.	enhances the performance indicators and level of assurance gained on its agent's performance.	85

## Submissions and comments received

We have professionally engaged with the Victorian Building Authority, Building Practitioners Board, Department of Justice & Regulation (Consumer Affairs Victoria), Victorian Managed Insurance Authority, Department of Environment, Land, Water & Planning, Department of Treasury and Finance, and the Essential Services Commission throughout the course of the audit. In accordance with section 16(3) of the *Audit Act 1994* we provided a copy of this report to those agencies and requested their submissions or comments.

We have considered those views in reaching our audit conclusions and have represented them to the extent relevant and warranted. Their full section 16(3) submissions and comments are included in Appendix B.

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# 1 Background

## 1.1 Introduction

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Domestic building is a significant area of economic activity. In 2013–14, over 101 000 permits were issued for building works in Victoria with an estimated value of more than \$25.3 billion. Domestic building work made up around 82 per cent of all permits and accounted for half of this value.

For individual consumers, the construction or renovation of a house is often the single largest investment in their lifetime. They may be ill-equipped to resolve building quality or contractual issues that may arise. The process of seeking to resolve such issues can be confusing, long and expensive and, for some consumers, can have serious financial and personal consequences. As a result, a robust consumer protection framework is important to minimise these potential adverse consequences.

A significant number of Victorian consumers experience problems with domestic building. Research published by Consumer Affairs Victoria (CAV) in 2009 estimated that 16 per cent of consumers in the Victorian domestic building market sector experienced problems. This sector had the highest proportion of consumers reporting detriment across all market sectors. More recently, the Commonwealth and state Governments' 2011 *Australian Consumer Survey* report indicated that 28 per cent of consumers in Australia had experienced a problem related to building or renovating—with the most common problem reported, accounting for 63 per cent, being poor workmanship.



Victoria's current building consumer protection framework has been in place and largely unchanged since 2002. In addition to general consumer protection laws, the framework consists of the building practitioner registration system, building regulations, practitioner discipline system, a dispute conciliation service, access to the Victorian Civil and Administrative Tribunal (VCAT) and a 'last resort' mandatory insurance scheme.

Successive governments have acknowledged that consumer protection policies in domestic building have not provided adequate protection for consumers. A series of reviews, inquiries and audits since 2000 have identified weaknesses in both the design and implementation of the current consumer protection framework. While the previous government initiated a reform process to address weaknesses in the framework to improve the level of protection for consumers, those reforms were not enacted and it is unclear at this stage what reforms, if any, will progress.

The Victorian Competition and Efficiency Commission's 2005 inquiry into *Housing regulation in Victoria: building better outcomes* identified the importance of an effective consumer protection regime for building construction in Victoria. It noted that while most markets feature information asymmetries—where information is known to some people but not others—these are 'relatively more significant for housing construction markets'. The reasons for this include:

- the long-lived nature of housing means that flaws may only become apparent years after construction is complete
- consumers are infrequent purchasers of building services and so lack the experience to monitor the quality and cost of work
- consumers are not well qualified to compare the quality and cost of building services from different suppliers
- many decisions about houses involve technical considerations and are therefore made by builders rather than consumers.

The Victorian Competition and Efficiency Commission highlighted the important role that government intervention and effective regulation could play in addressing the potential costs, equity issues and significance of market failures in housing construction.

## 1.2 The framework and key agencies

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The building consumer protection framework comprises protections aimed at:

- preventing disputes from arising, and limiting the time taken and cost to resolve those disputes where they do arise
- providing a safety net for consumers, where there is no longer a builder to pursue, for a structural defect or for non-completion of the building project.<sup>1</sup>

This framework is established by legislation which sets out roles and responsibilities for a number of government agencies.

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<sup>1</sup> Victorian Domestic Building Consumer Protection Framework Public consultation paper April 2012

## 1.2.1 Agency roles and responsibilities

The current building consumer protection framework involves a range of entities with functions extending from protections, including the registration and monitoring of building practitioners, to dispute handling and the provision of domestic building insurance (DBI).

### Victorian Building Authority (successor to the Building Commission)

Amendments to the *Building Act 1993* (the Act) established the Victorian Building Authority (VBA) on 1 July 2013 as the statutory agency responsible for regulating the state's building and plumbing industries. These amendments integrated functions of the former Building Commission and Plumbing Industry Commission into VBA.

VBA's functions most relevant to consumer protection include:

- monitoring and enforcing compliance with the Act and the *Building Regulations 2006* (the Regulations)
- providing information—including to consumers—on matters relating to:
  - building standards and plumbing standards
  - the regulation of buildings, building work and building practitioners
- providing information and training to assist people and bodies to carry out functions under the Act and the Regulations
- promoting the resolution of consumer complaints
- conducting or promoting research relating to the regulation of the building and plumbing industries in Victoria
- monitoring the collection of the building permit levy and administering the VBA Fund.

VBA's functions are funded by consumers through a levy on building permits, registration fees paid by practitioners and fines and costs levied through the practitioner discipline system. In 2013–14 the total permit levy collected was \$24.5 million. Around \$8 million of this levy income was paid to CAV to fund its domestic building activities.

### Building Practitioners Board

The Building Practitioners Board (BPB) is an independent statutory body established under the Act. It administers the practitioner registration and discipline systems and monitors the conduct and ability of registered building practitioners. This role is critical to maintaining the quality and performance of practitioners in the building industry.

BPB has no independent dedicated staff or resources. VBA provides administrative and other support to BPB in the performance of its functions.

### Building Appeals Board

The Building Appeals Board (BAB) is an independent statutory body established under the Act. BAB is empowered to determine any matter relating to the Regulations, the Building Code of Australia and specified provisions of the Act.

Specifically, BAB hears appeals and disputes in relation to building control matters and can waive, modify or vary the provisions of particular regulations based on the particular case.

Before July 2013, BAB was also the forum for reviewing BPB's decisions. This function was transferred to VCAT under amendments to the Act.

### Local government

Under the Act, councils are responsible for the administration and enforcement of Parts 3, 4, 5, 7 and 8 and the Regulations within their municipal district.



### Consumer Affairs Victoria

CAV is the state's consumer affairs regulator. At 30 June 2014, CAV was responsible for administering 29 Acts of Parliament. CAV's role is to:

- review and advise the government on the consumer protection framework
- provide information and advice to consumers, tenants, businesses and landlords on their rights, responsibilities and changes to relevant laws
- register and license businesses and occupations
- enforce and ensure compliance.

CAV aims to assist Victorian builders, owner-builders and consumers to avoid home building disputes by providing information about domestic building contracts and through its compliance activities, including the Better Business Initiative. It aims to assist consumers and builders to work together to solve building disputes. Its services include advice and conciliation.

CAV has administrative responsibility for the *Domestic Building Contracts Act 1995* (the DBCA). The objects of the DBCA are to:

- provide for the maintenance of proper standards in the carrying out of domestic building work in a way that is fair to both builders and building owners
- enable disputes involving domestic building work to be resolved as quickly, as efficiently and as cheaply as is possible having regard to the needs of fairness
- enable building owners to have access to insurance funds if building work under a major domestic building contract is incomplete or defective.

The DBCA provides for CAV's conciliation services in relation to domestic building disputes. CAV is constrained by the DBCA to only accept complaints or disputes for conciliation which are reasonably likely to be resolved. Under the DBCA, participation in conciliation is voluntary and CAV cannot enforce conciliation outcomes.

While the DBCA aims for timely low cost dispute resolution, in practice some building disputes are either not accepted for conciliation or not satisfactorily resolved through the conciliation process. In these cases the consumer or building practitioner's only remaining options are to pursue the matter through VCAT or court.

### Victorian Civil and Administrative Tribunal

VCAT is established under the *Victorian Civil and Administrative Tribunal Act 1998*. It has two main areas of involvement in the framework:

- a domestic building list for disputes between home owners, builders, subcontractors, architects, engineers and other building practitioners
- hearing appeals of BPB's practitioner registration and disciplinary decisions.

### Victorian Managed Insurance Authority

The Victorian Managed Insurance Authority (VMIA) is a statutory authority established by the *Victorian Managed Insurance Authority Act 1996*. VMIA assists government departments and agencies in the area of risk management and acts as an insurer for departments, agencies and related bodies.

DBI has been a mandatory feature of Victoria's consumer protection framework since 1996. The original DBI scheme was 'first resort', allowing consumers to lodge a claim regardless of their builder's status. In 2002, DBI was changed to a 'last resort' scheme to keep remaining insurers in the market following the collapse of the HIH insurance group.

VMIA has provided DBI since mid-2010 in accordance with a direction from government. DBI is an important part of the building consumer protection framework. The Act requires that building practitioners must be eligible for DBI to gain registration and must possess DBI cover when undertaking domestic building works over \$16 000 in value.

The Essential Services Commission monitors the VMIA's pricing and performance in delivering DBI, and reports on these publicly and to the Minister for Finance.



## Department of Treasury and Finance

Department of Treasury and Finance led the development of the government's 2013 *Domestic Building Consumer Protection Reform Strategy*.

Department of Treasury and Finance also supports and provides advice to the Minister for Finance on his portfolio responsibilities including for insurance policy.

## Department of Environment, Land, Water & Planning

The Department of Environment, Land, Water & Planning (DELWP) is responsible for providing advice to the Minister for Planning on building and plumbing policy, legislation, regulation and standards. This includes working with portfolio agencies, industry bodies and other stakeholders. Through the machinery-of-government changes effective 1 January 2015, DELWP became responsible for building policy and legislation in Victoria. Previously it was the responsibility of Department of Transport, Planning and Local Infrastructure (and formerly the Department of Planning and Community Development).

### 1.2.2 Operation of the framework

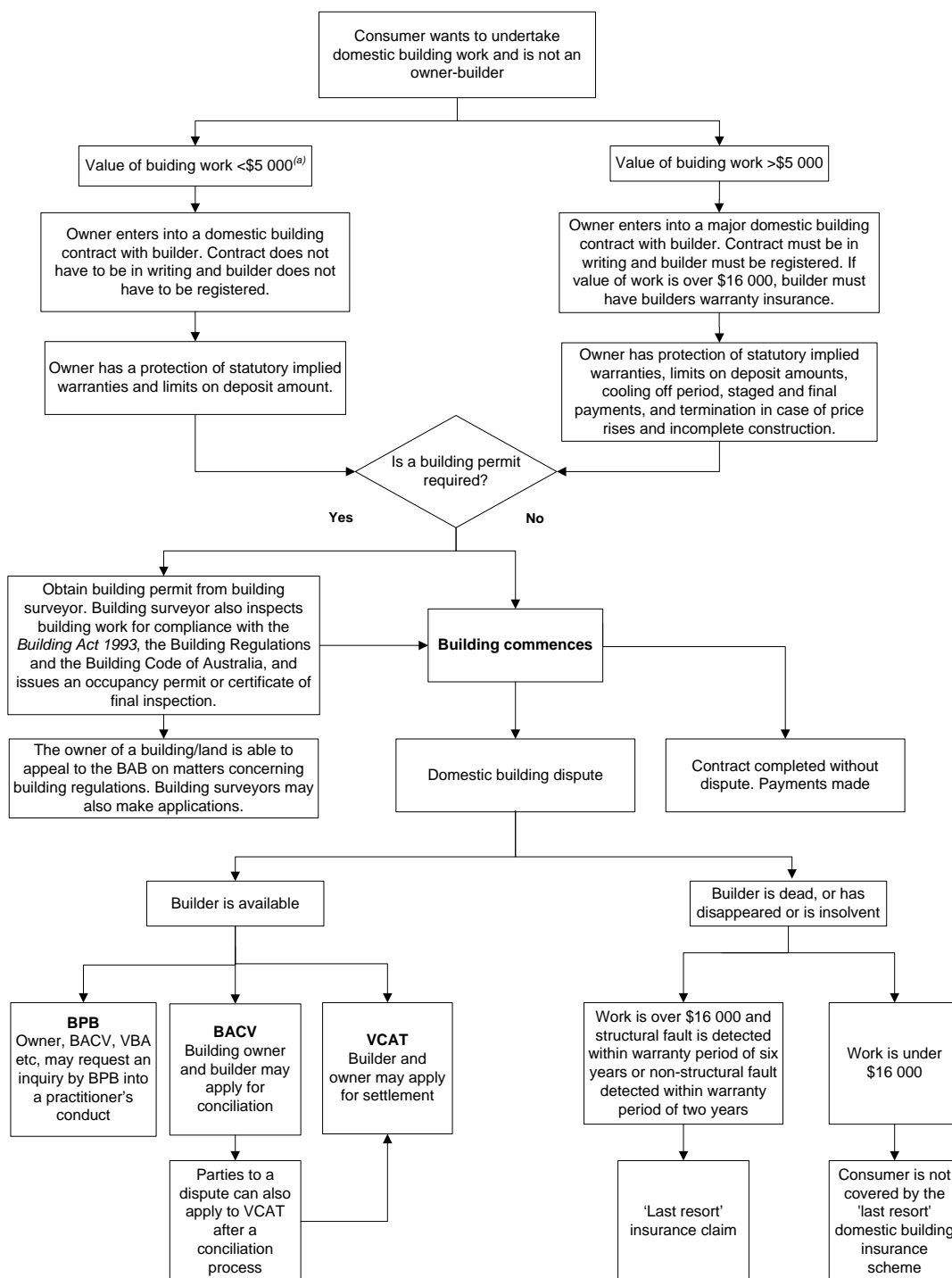
Figure 1A shows the steps that a consumer who is not an owner-builder follows when undertaking building work under the current building consumer protection framework.

The key consumer protections under the current framework are:

- the contractual protections and statutory checks protecting consumers against faulty or incomplete work—critical to the effectiveness of these protections are:
  - consumers understanding their rights and the terms and implications of the contracts they sign
  - builders applying the skills and required financial resources to complete works as intended and to applicable standards
  - building surveyors properly reviewing works and taking appropriate action to have faults addressed
- complaint handling and dispute resolution processes, where it is critical that:
  - consumers understand how to pursue and resolve a claim
  - dispute resolution is capable of reaching a fair outcome
  - regulatory and professional bodies are able to detect and address poor practices by surveyors and builders
  - insurance is effectively and efficiently applied where the builder is dead, has disappeared or is insolvent.



**Figure 1A**  
**Domestic building process**

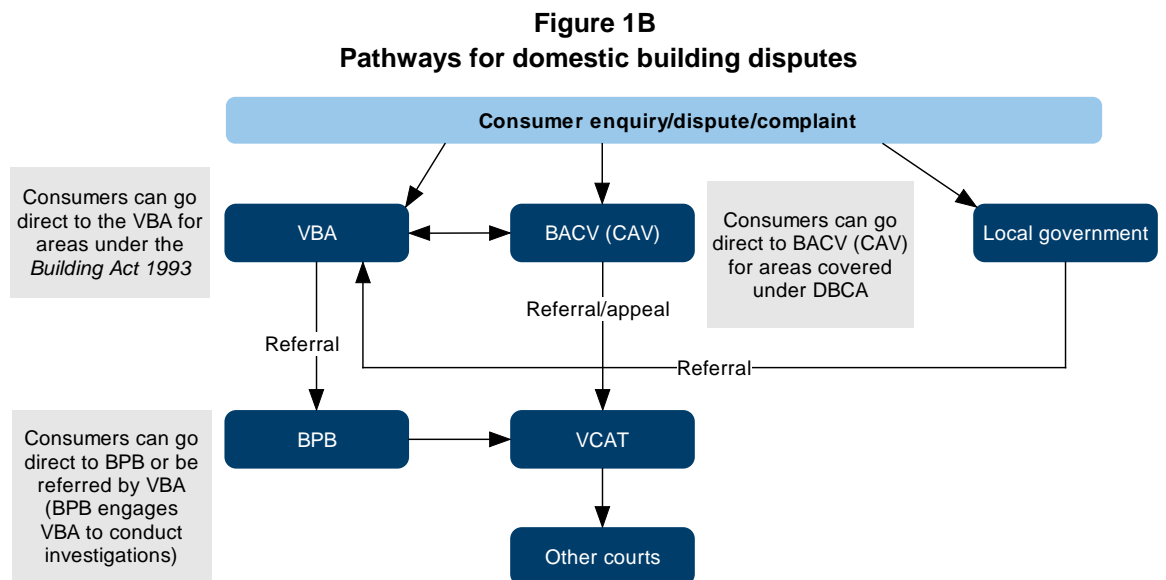


(a) The exceptions to this are the re-blocking or restumping of a home, or the demolition or removal of a home. These must be performed by a registered practitioner regardless of value.

Note: BACV is Building Advice and Conciliation Victoria, which is part of CAV.

Source: Victorian Auditor-General's Office.

Figure 1B shows the complex and multiple entry points and pathways for consumers wishing to have a concern or dispute with a building practitioner resolved under the current building consumer protection framework.



Source: Victorian Auditor-General's Office based on a presentation by the former Building Commission to the Legislative Council's Standing Committee on Finance and Public Administration's *Inquiry into Builders Warranty Insurance* in April 2010.

A key aim of the May 2013 proposed *Victorian Domestic Building Consumer Protection Reform Strategy* was to set up VBA as the one-stop-shop for registering practitioners, monitoring and overseeing the industry—including disciplinary activity—providing consumer information and preventing and resolving disputes. The reforms proposed that VBA would assume Building Advice and Conciliation Victoria's current conciliation functions and the functions of BPB which was to be abolished. These reforms included the establishment of VBA, however, they were not completed.

### 1.2.3 Previous reviews of the framework

Since 2000 a number of reviews, inquiries and audits have identified weaknesses in both the design and implementation of the building consumer protection framework in the following areas:

- the robustness and integrity of the system and processes for registering building practitioners
- the adequacy of practitioner compliance monitoring
- a lack of cohesion and accountability in the operation of the framework
- the extent to which consumers understand and are protected by DBI
- a lack of focus on measuring the performance and effectiveness of regulatory and other activities.

### VAGO's performance audit of the building control system, *Building control in Victoria: Setting sound foundations, 2000*

This audit found:

- weaknesses in the then Building Control Commission's monitoring—including its identification of building control risks and targeting of monitoring and enforcement activities
- a need to improve the rigour and suitability of registration and renewal processes
- that the Building Control Commission lacked a framework to measure its effectiveness
- the BPB was constrained in fulfilling its legislative responsibility to monitor the conduct and ability of building practitioners to practise, due to a lack of resources.

### Victorian Competition and Efficiency Commission's inquiry into *Housing regulation in Victoria: building better outcomes, 2005*

The inquiry found:

- significant opportunity for improvement, particularly in establishing a more closely defined regulatory environment and improved performance reporting to enhance transparency and accountability
- a need for the then Building Commission to improve its performance reporting and a recommended that it publish the rationale behind its monitoring and enforcement strategy and performance indicators.

### Legislative Council Standing Committee on Finance and Public Administration *Inquiry into Builders Warranty Insurance, 2010*

The inquiry found:

- that government policy on builders warranty insurance had developed primarily in reaction to market conditions since 2002 with inadequate consultation with consumer interests and insufficient regard to the aim of the scheme—consumer protection
- it was too early to determine the impact of the government's reforms to builders warranty insurance in 2010—the reforms had not yet addressed consumer complaints about the 'last resort' nature of the scheme
- first and 'last resort' schemes both require consumers to try to resolve problems directly with builders in the first instance—if the consumer is unsuccessful, 'last resort' schemes only become involved in limited circumstances such as the death, insolvency or disappearance of the builder, whereas first resort schemes can assist unsuccessful consumers even when the builder is still trading
- administration of Victoria's builders warranty insurance scheme, and consumer protection in the building industry generally, was fragmented and poorly coordinated
- poor accountability and transparency measures, along with reports of enforcement inaction and poor handling of consumer complaints, were adding to concern about Victoria's builders warranty insurance scheme.

### VAGO's performance audit *Compliance with Building Permits*, December 2011

This audit found:

- the then Building Commission could not demonstrate that the building permit system was working effectively or that building surveyors were effectively discharging their role to uphold and enforce minimum building and safety standards
- results of testing a sample of building permits revealed a system marked by confusion and inadequate practice—including a lack of transparency and accountability for decisions made
- the absence of leadership, guidance and rigorous scrutiny from the commission meant councils adopted a largely reactive approach to enforcing the Act that offered little assurance of compliance within their municipalities
- there was little assurance that surveyors carried out their work competently, that the Act was being complied with, and the risk of injury or damage to any person was being minimised
- the BPB's assessment process for registering building surveyors was not well documented, nor supported by clear criteria and standards—gaps in guidance and documentation reduced accountability for decisions and did not provide assurance that assessments were soundly based.

### Ombudsman Victoria, *Own motion investigation into the governance and administration of the Victorian Building Commission*, December 2012

The Ombudsman found:

- concerns with the vulnerability, integrity and administration of the registration system for building practitioners overseen by the BPB with administrative support from the then Building Commission
- BPB's lack of rigour or proper oversight of the building practitioner registration system created risk and opportunities for maladministration and misconduct to occur—this included registration as a licensed builder being given to people who failed parts of the competency assessment, and others being registered without having to sit assessment tests
- particular concerns with the conduct of the former Registrar of BPB who failed to declare business interests in the industry and approved applications for people he knew
- significant questionable spending by commission executives on entertainment, hospitality and sponsoring industry bodies' events and awards
- recruitment practices involving both contractors and internal staff that were in breach of the then Building Commission's policies and government procurement guidelines.

### 1.2.4 *Victorian Domestic Building Consumer Protection Reform Strategy*

Following a public consultation process in 2012, the government responded to weaknesses in the current framework by releasing the *Victorian Domestic Building Consumer Protection Reform Strategy* in May 2013.

The strategy acknowledged that the current framework provides only modest levels of protection for consumers and has significant gaps and opportunities for improvement in relation to:

- practitioner registration, licensing and re-registration standards
- the need to extend the scope of regulation beyond individual practitioners to corporations and partnerships
- the regulator's disciplinary powers
- the absence of binding rectification orders where building works are assessed as defective
- oversight of building surveyors and the building permit system
- the range, depth and accessibility of consumer information including information on building practitioners' disciplinary history
- the extent of protection provided by DBI.

The aim of the strategy was to address these issues and reduce the number of building disputes, and, where they do arise, to help them be resolved quickly, fairly and cost efficiently. The strategy proposed significant changes to administrative arrangements for regulation and oversight of the building sector.

While extensive, the reform strategy did not fully address the key issues with the current domestic building consumer protection framework identified in previous reviews and submissions to the reform process, including the:

- effect of having non-mandatory conciliation on the capacity for early resolution of building disputes
- conflicts of interest for private building surveyors between performing their statutory roles and their business interests.

Implementation of the reform strategy commenced in 2013 with stage 1 involving the establishment of VBA on 1 July 2013. Since the December 2011 VAGO report, the former Building Commission and VBA have had five chief executive officers with the first stable leadership team being established by VBA in April 2014.

The most significant of the stage 2 reforms relied on the *Building Legislation Amendment Bill 2014* which sought to enable:

- the transfer and enhancement of functions and powers from BPB, BAB and CAV to VBA to create a one-stop-shop for the registration and oversight of building practitioners
- provision of additional consumer information
- additional mechanisms to resolve domestic building disputes, including giving VBA the power to issue binding rectification orders to parties where building work is assessed as defective or incomplete by a VBA inspector
- the extension of the triggers for access to domestic building insurance.

This Bill did not proceed through Parliament in 2014. The new government is yet to announce whether it will pursue or re-examine these reforms.

## 1.3 Audit objective and scope

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The audit objective was to assess whether key elements of the current domestic building consumer protection framework are effectively managed by relevant entities.

To do this we examined whether:

- VBA, BPB and CAV are performing existing functions and using powers effectively
- VMIA's provision of domestic building insurance is effectively and economically managed.

This audit included the following relevant departments, agencies and statutory boards:

- Victorian Building Authority
- Building Practitioners Board
- Building Appeals Board
- Consumer Affairs Victoria
- Department of Environment, Land, Water & Planning
- Victorian Managed Insurance Authority
- Essential Services Commission
- Department of Treasury and Finance.

The audit examined relevant organisational arrangements and priorities, and evidence on how current responsibilities are met, measured and reported on.

## 1.4 Audit method and cost

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The audit involved:

- desktop research and interviews with relevant departmental and agency staff, members of statutory boards, consumers and practitioners
- examination of relevant policy and procedure documents
- document and file reviews and analysis of sampled registrations, monitoring and enforcement activity, disciplinary reviews, consumer complaints, records of outcomes of disputes, etc.
- examination of any other relevant evidence held by departments, agencies and statutory boards
- examination of consumer correspondence.

The report includes quotes taken from correspondence received by the Auditor-General from domestic building consumers. These quotes are included for illustrative purposes only and individual cases were not investigated as part of the audit.

The audit was performed in accordance with the Australian Auditing and Assurance Standards. Pursuant to section 20(3) of the *Audit Act 1994*, unless otherwise indicated, any persons named in this report are not the subject of adverse comment or opinion.

The total cost of the audit was \$595 000.

## 1.5 Structure of the report

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The report is structured as follows:

- Part 2 examines the registration, monitoring and discipline of building practitioners where the effectiveness of these processes underpin the contractual protections and statutory checks by building surveyors designed to prevent disputes
  - Part 3 assesses CAV's role in preventing and resolving disputes by educating consumers about their rights and obligations, managing complaints and conciliating disputes, undertaking compliance and enforcement activities, and advising government on how best to achieve its policy goals
  - Part 4 examines the effectiveness and efficiency of the domestic building insurance scheme.
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# 2 Building practitioner registration, discipline and compliance monitoring

## At a glance

### Background

The Victorian Building Authority (VBA) monitors and prosecutes noncompliance with the *Building Act 1993*. Private and municipal building surveyors also play a key role in compliance. The Building Practitioner's Board (BPB) registers and disciplines practitioners. Consumer Affairs Victoria (CAV) educates building practitioners about their obligations under the *Domestic Building Contracts Act 1995* and enforces this Act.

### Conclusion

BPB's practitioner registration system does not ensure that the only practitioners who are registered are qualified, competent and of good character. There are significant deficiencies in VBA's oversight of building surveyors and in the coordination of compliance and practitioner performance monitoring across agencies. However, over the last year VBA has commenced action to address many of VAGO's 2011 audit recommendations and to establish an appropriate governance framework.

### Findings

- There is limited assurance that BPB performs its registration and disciplinary functions effectively.
- The role of building surveyors is undermined by a conflict of interest arising from surveyors typically relying on builders for recurrent work.
- BPB sanctions appear ineffective in deterring practitioner misconduct.
- VBA lacks an effective monitoring and evaluation framework for its activities.
- CAV provides practitioner information, advice and training, but lacks outcome focused performance measures to gauge the effectiveness of these programs.

### Recommendations

That the Department of Environment, Land, Water & Planning reviews the regulatory arrangements governing the engagement of building surveyors to ensure they support the independent and objective performance of their function to provide appropriate independent oversight of building and the building system.

## 2.1 Introduction

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Building practitioner information and education services, registration and discipline, compliance monitoring and enforcement all play a part in ensuring that building practitioners meet required standards and that consumers are protected. The Victorian Building Authority (VBA) and Consumer Affairs Victoria (CAV) share responsibility for monitoring and compliance in domestic construction. Local councils are responsible for the administration and enforcement of parts 3, 4, 5, 7 and 8 of the *Building Act 1993* (the Act) and the *Building Regulations 2006* (the Regulations) within their municipalities.

VBA is primarily responsible for monitoring compliance with the Act and the Regulations. This includes auditing the collection of building levy payments and the compliance of building permits issued by building surveyors.

Building surveyors—both private and municipal—play a critical role in implementing, enforcing and monitoring the building standards prescribed by the Act and the Regulations through conducting inspections and issuing building permits. CAV and VBA provide educational resources, guidance and support programs for practitioners—VBA in technical building matters and CAV in issues of a contractual and customer focused nature.

The Building Practitioners Board (BPB) is responsible for supervising and monitoring the conduct and ability to practise of registered building practitioners. It operates a discipline and sanction regime which aims to reinforce the incentives for practitioners to behave appropriately, discourages those practitioners who have been found guilty of misconduct from repeat offending, and suspends or cancels registration for those practitioners whose misconduct is particularly harmful.

In 2011 VAGO undertook an audit, *Compliance with Building Permits*, which focused on both building permits and the role and oversight of surveyors. We found that 96 per cent of permits examined were noncompliant and we made a series of recommendations aimed at strengthening the regulation of building surveyors.

## 2.2 Conclusion

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There has been little improvement in the registration and oversight of building surveyors, and the coordination of compliance and practitioner performance monitoring since VAGO's 2011 report. The administration and monitoring of the building levy system is still hindered by VBA's lack of powers to reassess and recoup underpaid levy and to require building surveyors to remit levy promptly.

BPB's practitioner registration and discipline systems do not ensure that the only practitioners who are registered are qualified, competent and of good character. Registration assessment practices are inconsistent and no objective standards are in place. Deficiencies in this system are compounded by the open-ended nature of building registrations under the Act and the lack of effective triggers or mechanisms to review practitioner competence. In addition, sanctions imposed in BPB's disciplinary processes appear ineffective in deterring practitioner misconduct.

The independence of compliance monitoring by surveyors is weakened by a long-recognised conflict of interest for private building surveyors which undermines confidence in the system. This conflict, combined with building surveyors' disproportionately high representation in BPB inquiries, registration suspensions and cancellations, and reoffending, is concerning given their critical role in assuring building standards. Similarly, VBA's risk-based monitoring and compliance activities, while promising, are newly established and lack an evaluation framework to assess their effectiveness. However, over the past year VBA has taken action to address many of VAGO's 2011 audit recommendations and establish an appropriate governance framework, including developing a memorandum of understanding (MOU) with BPB to define governance arrangements between the bodies.

## 2.3 Practitioner registration and education

The practitioner registration system assesses a range of relevant factors including competence, solvency, character and work history. We evaluated the adequacy of these assessment processes by spot sampling a randomly chosen selection of 23 building practitioner registration assessment records. For a description of the practitioner classes chosen and the number of practitioner records in each class reviewed see Figure 2A. These classes were chosen as the most relevant to domestic building and most likely to directly impact on consumer protection. A full description of practitioner categories and classes is available at Appendix A.

**Figure 2A**  
**Practitioner categories and classes**

Category and class	Description	Number of records reviewed
Domestic builder-unlimited (DB-U)	May personally carry out, manage or arrange for subcontractors to carry out all components of domestic work.	4
Domestic builder-manager (DB-M)	May manage or arrange for domestic builders registered in another class to carry out components of domestic building work specified in their Certificate or Registration which is generally quite specific—for example, work on retaining walls or work on garages and carports.	3
Domestic builder-limited (DB-L)	May carry out, manage or arrange to carry out only the components of domestic building work specified in their Certificate of Registration.	8

**Figure 2A**  
**Practitioner categories and classes – *continued***

Category and class	Description	Number of records reviewed
Building surveyor-unlimited (BS-U)	May conduct building surveying functions—ensure construction projects meet building regulations—for all buildings.	4
Building surveyor-limited (BS-L)	May conduct building surveying functions—ensure construction projects meet building regulations—for buildings up to three storeys high with a maximum floor area of 2 000 square metres.	3
Building inspector (BI-L)	Permitted to inspect certain classes and components of buildings and varieties and types of construction.	1

Source: Victorian Auditor-General's Office based on information from VBA.

We also examined BPB's supporting documentation for the registration system, relevant programs, activities and legislation.

We found:

- a lack of objective guidance and standards for assessing applications
- a poor standard of documentation of assessment decisions
- a lack of competency assurance for 'grandfathered' practitioners—whose existing registrations were transferred into the new system without assessment—and practitioners applying for mutual recognition of qualifications from other states or territories
- inadequate assessments of practitioners' financial and business skills.

The current practitioner registration system does not ensure that the only practitioners who are registered are qualified, competent and of good character. VAGO's 2011 audit found significant deficiencies with the registration system and records for surveyors. Our spot sampling of records for both building surveyors and domestic builders—who undergo a similar registration process—shows that these deficiencies remain.

### 2.3.1 Registration assessment and approval processes

Under the Act practitioner registration lasts until cancelled, subject to the payment of an annual renewal fee and an insurance premium. This amplifies the significance of initial registration assessments and the consequences of allowing unsuitable practitioners to gain registration. Despite this, the registration process effectively provides absolute discretion to individual assessors.

All practitioner registration applications are assessed by an individual assessor—either a VBA in-house assessor, a BPB member, or in the case of DB-U applications, by a contracted assessor, whose assessments are then reviewed by a BPB member or assessor.

VAGO's 2011 audit recommended that BPB 'develop criteria and guidelines for evaluating the competency of applicants to be registered as building surveyors and clearly document the basis of all decisions'. Objective criteria and standards would ensure consistency and objectivity in assessment. They would also provide transparency given that BPB members, and therefore assessors, are usually appointed from, and may be currently active within, the construction industry.

The need for objective criteria and standards is reinforced by our spot sampling of registration files which revealed significant inconsistencies between assessors and a poor standard of documentation of decisions. Several issues were identified:

- Assessors' recommendations and the outcomes of individual assessment stages are not recorded clearly—two of the files contained assessors' reports that have both 'approve registration' and 'do not approve registration' boxes checked.
- Required supporting documentation is not recorded accurately.
- Assessors' commentary and/or annotations are inconsistent and often ambiguous—for example, some registration records provide detail against all checklists and components, while others leave sections blank, several files indicate the insufficiency of supporting evidence, but appear to approve registration regardless.
- Assessors have an inconsistent understanding of assessment evidence requirements—for example, some assessments contain detailed narrative descriptions of the applicants working history, demeanour, and the initial conversations between the assessor and applicant, while others contain no explanatory notes.

Despite requiring applicants to provide extensive supporting documentation including example building contracts, health and safety plans, business and financial plans, site plans etc., there is no guidance in place to support qualitative assessment of this documentation beyond a checklist evidencing that it has, in fact, been provided. The registration files we examined showed inconsistent practices and in some cases limited evidence that the supporting documentation had been assessed at all.

BPB needs to determine what supporting documentation is critical to the assessment process and then develop specific criteria for assessing the adequacy of this documentation beyond relying on the individual discretion and knowledge of assessors.

BPB advised that its registration subcommittee began work to address VAGO's relevant 2011 recommendation in January 2012, however, little progress was made. During 2013, VBA assumed oversight of this work given that legislative reforms were expected to transfer these functions from BPB to VBA. While together VBA and BPB made some progress, BPB still lacks a current registration policy and comprehensive standards and/or guidance for assessing the knowledge, skills, and suitability of applicants for registration. Consequently, there is no assurance around the adequacy, consistency and objectivity of registration application assessments.

## The BPB's consideration of applications

While BPB officially approves all registration applications individually, in practice these decisions are made on large numbers of applications at each meeting on the basis of limited information. The Ombudsman's December 2012 report recommended that BPB should 'ensure the board receives detailed information, including the results of applicants for each stage of the assessment to inform its consideration of applicants for registration'. Prior to this recommendation, BPB members received only a list for approval, showing the number of applicants that had been assessed for registration in each practitioner category.

From December 2013, BPB papers included a table indicating the qualifications and years of experience of each applicant and the computer-based test results for some classes of practitioner. However, these documents are often provided to members the day prior to the relevant meeting. This does not allow BPB members sufficient time to examine and inquire about any issues of concern related to the applicant's suitability in accordance with the requirements of the Act.

While these changes may technically address the Ombudsman's recommendations, they are not sufficient to address VAGO's 2011 concerns that the registration assessment and approval process provides little assurance that decisions are soundly based. BPB provides only limited applicant information in part because it is impractical for BPB to consider at length the large number of registration applications that it receives. However, introducing benchmark standards for assessing and evaluating applications prior to seeking BPB approval, would practically address this issue and provide greater assurance that registration approvals were based on objective and critical assessments of practitioner competence and suitability. Advice provided by BPB indicates that as of February 2015 all BPB agenda items, including registration application recommendations, are circulated with at least five days for members to review.



## 2.3.2 Competence

### Qualifications

The Act does not include specific minimum standards for qualification and experience, which could act as a baseline for practitioner competency. Such minimum standards would improve the objectivity and robustness of the practitioner registration system. Under the Act, BPB has limited discretion in granting or refusing registration. It must register an applicant if it is satisfied that the applicant has:

- provided proof of suitable insurance coverage
- submitted a suitable and complete application
- provided any more information that BPB reasonably requires, and either:
  - holds an appropriate prescribed qualification, or
  - holds a qualification that BPB considers is, either alone or together with any further certificate, authority, experience or examination equivalent to a prescribed qualification
- is of good character
- complied with any other condition prescribed for registration in that category or class.

In December 2012, the Ombudsman recommended that BPB 'review the registration process for all categories of registration and develop minimum standards for qualifications and experience of applicants, and clearly identify the supporting documentation to be submitted with an application'.

Under the Act, one of BPB's three functions is to make recommendations to the Minister about the qualifications for registration. However, it took until November 2013 for BPB to provide advice to the Minister for Planning recommending that Schedule 7 of the Regulations be amended to allow for minimum qualifications to be prescribed. The Minister responded in late February 2014 indicating that he had referred the Chair's advice to the then Department of Transport, Planning and Local Infrastructure to consider as part of the review of the Regulations review process in 2016.

### 'Grandfathered' practitioners

In late 1996, when the current practitioner registration system was introduced, the government directed BPB to 'grandfather' existing building practitioners—to transfer them directly into the new registration system without assessment. There were 26 242 practitioners eligible to have their registrations transferred, of whom 12 382 subsequently registered with BPB.

The risks posed by the grandfathering of practitioners into the current registration system and their continued trading are unknown. This issue was first raised by VAGO 15 years ago, but no attempt has been made to assess the competence of these practitioners or address this risk. Our spot sample of registration files examined only one 'grandfathered' practitioner. The relevant file did not show any evidence that the practitioner had formal qualifications.



When we first raised the issue of grandfathered practitioners in our 2000 report *Building control in Victoria: Setting sound foundations* we recommended that the competence of practitioners in categories and classes assessed as high risk should be assessed on a progressive basis, observing:

The 20 600 existing building practitioners, registered under transitional arrangements between July 1994 and June 1997, have not been assessed for suitability in terms of qualifications, skills or experience. In my opinion, the decision to 'grandfather' in such a large number of practitioners was an expedient process for the Board to follow in the circumstances.'

While this issue is diminishing over time as grandfathered practitioners age and retire, there are currently 5 677 grandfathered practitioners registered with BPB, accounting for 5 694 registrations—practitioners may be simultaneously registered in multiple classes. BPB advised us in the course of this audit that it believes that grandfathered practitioners do not represent any greater risk than any other practitioners. It also noted that the current legislative framework does not allow for the competency of grandfathered practitioners to be reviewed. BPB considers that the major flaw in the current legislation is the ongoing nature of practitioner registration.

### Mutual recognition

Mutual recognition is enabled by Commonwealth legislation and involves registering applicants in Victoria if they can demonstrate that they hold an equivalent registration in another state or territory and do not have an adverse disciplinary history in that jurisdiction. While BPB is precluded from conducting competency assessments of mutual recognition applicants it does subject these applicants to a police check.

Analysis of BPB registration data indicates that the number of mutual recognition applications increased by around 130 per cent between 2012 and 2014. The practitioner classification with the highest increase in mutual recognition applications was DB-L which increased by 273 per cent from 97 applications in 2012 to 362 in 2014.

Analysis of registration data identified 20 cases where BPB rejected applications for Victorian building practitioner registration, typically due to insufficient qualifications and/or experience, but the practitioner subsequently obtained registration under mutual recognition provisions.

In March 2013, BPB's registration subcommittee meeting raised concerns about the significant increase in mutual recognition applications and resolved to write to the Minister to point out concerns about the mutual recognition loopholes. While BPB advised that it has recently raised its concerns about mutual recognition in a submission to the Productivity Commission on its review of mutual recognition schemes, it has not advised the Minister on this issue.



### 2.3.3 Solvency, business and financial management

Insolvency is a trigger for insurance claims under the domestic building insurance (DBI) scheme and the most common reason for DBI claims. Given the prevalence of this issue, BPB should be actively considering this risk when it assesses registration applications.

BPB's assessment of solvency and financial and business management skills of registration applicants is inadequate and implicitly relies on the Victorian Managed Insurance Authority (VMIA) conducting a thorough assessment when it decides to offer DBI. Registration assessors are appointed on the basis of technical building background and are unlikely to be suitably qualified to assess financial probity.

Spot sampling of financial information provided in registration files indicated that:

- plans provided by applicants were typically very basic and aspirational
- there was no requirement to provide evidence of current financial standing or credit history—either as a trader or individual
- there was little evidence of any detailed assessment by BPB of financial information provided by applicants.

BPB's reliance on VMIA's assessment is inappropriate given VMIA focuses on solvency and does not assess key issues including the capacity of practitioners to successfully plan and run a business.

To gain registration certain practitioners must provide evidence that they are covered by DBI or that they are eligible to be covered. VMIA provides advice to BPB when denying an application for DBI eligibility—for further discussion of this refer to Part 4.

### 2.3.4 Character

VAGO's 2011 report recommended that BPB 'systematically verify a sample of character declarations supplied by applicants for registration to gain reasonable assurance they are reliable'. This recommendation was addressed by amendments made in July 2013 to the Act which make it mandatory for registration applicants to authorise a police check with their applications.

BPB began using police checks as a screening mechanism on all building practitioner registration applicants from March 2014. Police checks that return anything other than minor offences are referred to a Probity Panel of three BPB members including the Chair.

To date no candidate has been refused registration on the basis of the outcome of their police check alone, and no convictions for very serious offending have been disclosed in police check results. Prior to the introduction of police checks, BPB members contacted a sample of applicant supplied character referees by phone.

## Registration period and compulsory professional development

Once registered, a building practitioner can continue to operate subject to the payment of an annual fee and insurance premium. VAGO's 2011 report noted that the ongoing nature of registrations means that 'a practitioner does not have to demonstrate they have maintained their capability to the level that they can discharge their duties', and that this was 'a gap in the regulatory framework'.

The report recommended that the then Department of Planning and Community Development (DPCD), in consultation with stakeholders, seek approval from the Minister to:

- introduce a system of compulsory continuing professional development for building surveyors
- amend the Act to make registration renewal contingent on building surveyors satisfying minimum compulsory continuing professional development requirements.

In response, the then DPCD sought legal advice which advised that amendments would be required to both the Act and the Regulations in order to mandate compulsory continuing professional development for registered building surveyors.

The May 2013 *Victorian Domestic Building Consumer Protection Reform Strategy* committed to improve re-registration standards by limiting the registration period to 'no more than five years, with renewal being required on expiration of the period'.

DPCD subsequently commissioned a cost-benefit analysis that found that there was a lack of compelling evidence that introducing mandatory continuing professional development would improve professional standards. In light of this, DPCD advised government to strengthen the legislative requirements by introducing five-year re-registration periods. This was designed to provide the regulator with the capacity to assess the practitioner's ongoing competence as part of the registration renewal process.

Amendments to enact this change were included in the *Building Legislation Amendment Bill 2014* (the Bill). However, as the Bill did not pass Parliament, there is still no requirement for practitioners to demonstrate their ongoing competency. Legislative change to introduce a finite registration period remains the most direct way to address this issue.

## CAV's practitioner information and education services

CAV provides a range of practitioner information and education services for building practitioners including:

- practitioner information sessions at registered training organisations
- presentations in partnership with VBA at trade shows
- email updates to practitioners on their obligations.

CAV's reporting on its practitioner information and education services is largely narrative—for example, descriptive reports of trade show appearances. It cannot measure the effectiveness of these programs because it lacks outcome-based performance evaluation measures.

### Better Business Initiative

CAV's Better Business Initiative (BBI), described in Figure 2B, is primarily a compliance tool aimed at practitioners who generate large volumes of complaints. While BBI has resulted in positive outcomes, it is a targeted program. CAV needs to ensure that its broader practitioner education and information programs are similarly effective.

**Figure 2B**  
**BBI**

The BBI supports participating businesses to adopt practices to assist them in improving compliance with the *Domestic Building Contracts Act 1995*.

CAV targets builders who undertake a large volume of building works and also have a large volume of complaints. It develops an action plan for each builder which outlines the number of meetings, skills and resources needed to assist the builder. Follow-up meetings are held with BBI participants to determine whether they have experienced any reduction in complaint volumes. BBI participants may be subject to compliance measures to reduce complaints. If the builder does not respond to such measures this may lead to enforcement action.

In 2013, there was a 24.2 per cent reduction in complaints about the builders that CAV had engaged under the BBI.

The BBI effectively assists CAV to reduce the volume of complaints from specific building practitioners, by educating practitioners to improve industry practice and consumer experience.

Source: Victorian Auditor-General's Office.

## 2.4 Monitoring compliance

### 2.4.1 The role of building surveyors

Building surveyors are responsible for making sure that buildings are safe and accessible. They issue building permits and manage the inspection process from foundations through to completion. In 1994, regulations were introduced to allow private building surveyors to issue building permits to increase competition. Prior to these reforms, all building permits were issued by municipal councils.

VAGO's 2011 report found that the former Building Commission (BC) could not demonstrate that building surveyors were effectively discharging their role to uphold and enforce minimum building and safety standards. It recommended that BC consult with stakeholders to:

- develop standard templates and procedures to require building surveyors to adequately document their assessment approach and the basis of their decisions
- require building surveyors to use these templates and procedures to demonstrate how they had considered and acquitted mandatory safety and technical requirements.

The Bill included a requirement for surveyors to complete a checklist of required documentation and certify that all documents required had been given to the local council. However, this is not sufficient to fully address VAGO's recommendations. VAGO's 2011 audit found that there was both a lack of required documentation and a lack of detail on documentation that was provided. It also identified a lack of information supporting surveyors' assessments, and evidence that building surveyors were 'inappropriately abdicating some of their technical assessments to third parties'.

VBA has indicated that it intends to address these recommendations by:

- identifying specific regulations that require relevant building surveyors to apply discretion, and developing templates for building surveyors to use where there is discretion
- developing documentation outlining the role of the relevant building surveyor and drafting a code of conduct for relevant building surveyors which will require consultation with industry
- delivering information and training seminars to building surveyors in collaboration with peak bodies and representative groups.

In order to ensure that these actions effectively address the issue, VBA needs to monitor surveyors' use of the templates to confirm that their use is resulting in appropriate documenting of assessment approaches and decisions. It is also important that VBA maintain ongoing engagement with building surveyor peak bodies in order to gain support for, and enable evaluation of, any code of conduct and training initiatives established.

## Potential conflict of interest

The current regulatory framework fails to manage a long-recognised conflict of interest for private building surveyors. This potential conflict of interest arises when a private building surveyor is engaged by the builder rather than the owner. This is typically the case. In these circumstances, the building surveyor can potentially be reliant on the builder for future engagements, which may limit the building surveyor's independence to challenge any building work not consistent with standards or permits.

This issue was also raised in submissions to the government's *Victorian Domestic Building Consumer Protection Framework Public Consultation Paper April 2012*. The submission of the Victorian Bar observed 'the current system of private building surveyors, combined with a weak regulatory system, provides an environment where collusion and conflict of interest between builders and building surveyors is prevalent'.

Correspondence to the Auditor-General from consumers who have experienced difficulties in building indicates that this remains an issue:

'The builder insisted on using his own surveyor, claiming that this would expedite the project as they have been working together for a very long time and he said the surveyor knew his work.'

The Bill was to introduce a requirement that, prior to accepting an appointment in relation to domestic building work, building surveyors would be required to provide consumers with information about their role. The Bill also proposed a requirement for surveyors to adhere to a code of conduct.

However, responses to the government's *Victorian Domestic Building Consumer Protection Framework Public Consultation Paper April 2012* from a range of stakeholders raised concerns about the likely effectiveness of these measures. The Victorian Bar, the Law Institute of Victoria and the Consumer Action Law Centre advocated more substantial changes to building surveyor regulation, suggesting either a model similar to that of Western Australia, where building permits are issued by authorities, usually local councils, or a model where jobs are centrally allocated to private building surveyors by VBA or a similar authority.

VAGO's 2011 recommendations for addressing fundamental weaknesses in how building surveyors are regulated have not been addressed. These weaknesses mean that surveyors' potential conflicts are not effectively controlled and consumers are at risk from the kind of practices that have seen one in 10 surveyors disciplined by BPB over the past five years.

The Department of Environment, Land, Water & Planning should review the effectiveness of the regulatory arrangements that govern the engagement of building surveyors. In the interim, VBA and CAV should review their consumer education initiatives to ensure that consumers are informed about the role and accountabilities of surveyors to the greatest extent practicable.

## 2.4.2 The role of the VBA

### Performance audit

While progress by the former BC was slow, the VBA has taken positive steps to develop a risk-based performance audit program.

VBA is responsible for monitoring compliance with and enforcing the Act and the Regulations. It has the power to appoint performance auditors to examine the work carried out by registered building practitioners. Performance audit is effectively the only form of proactive and direct monitoring of practitioner work in the building regulation framework, particularly with regards to surveyors.

VAGO's 2000 and 2011 reports both found that the former BC's performance audit program did not effectively target major risks or achieve adequate coverage and scrutiny of practitioners' work. Instead it focused on administrative issues and hence did not meet the Act's intent to ensure work does not pose a risk of injury or death.

VAGO's 2011 report also noted that BC did not have targets for auditing private building surveyors even though they issued over 85 per cent of all building permits. The report recommended that BC strengthen its performance audit program to ensure it meets its legislative remit to provide assurance that the work of registered practitioners has been competently carried out and does not pose a risk of injury or damage to any person.

In September 2012, BC commenced an audit of 1 000 building permits which VBA subsequently continued and expanded. VBA conducted a more in-depth audit of a subset of 450 of this 1 000, targeting those that posed a risk to human safety. These audits detected significant levels of noncompliance and VBA's Compliance and Performance Division used the findings from these audits to identify risks and select areas of priority for future audits of building permits, and of the building levy. The division's business plan for 2014–15 identifies demolition, draftspersons and building surveyors as the three priority areas for audit.

VBA communicated the results of these audits to its board in July 2014. It also issued an industry report to practitioners in September 2014 including a discussion of technical and general findings, recommendations for practitioners and consumers, and a list of actions, including VBA actions. The report's findings on building permit files at council offices echoed those of VAGO's 2011 report, including:

- poorly prepared building permit forms with prescribed fields not completed appropriately and errors present
- property information and planning information lacking
- documentation on the building work—specifications, methodology, engineer computations, energy reports—and energy efficiency documentation lacking
- reports and consents absent from files.



A key recommendation to building surveyors was that they ‘must not approve building permit applications where documentation provided by the owner/owner’s agent is not sufficient to demonstrate compliance with legislation’. To assist practitioners to achieve compliance VBA issued individual audit reports in February 2015 to 212 practitioners.

Since mid-2014, VBA has been implementing a framework to guide a more systematic approach to the selection and conduct of performance audits. VBA’s June 2014 *Performance Audit Policy* provides a broad framework for VBA’s audit activity, including standards and expectations for audits. While this is a positive development, VBA needs to establish detailed guidance on how its employees should apply this audit framework to ensure rigour, objectivity and consistency in the process.

There are some key performance indicators listed in the Compliance and Enforcement Divisional Plan for measuring how well VBA targets and performs this audit activity, however, these are limited to timeliness and efficiency measures. The business case and project plans for each audit define tangible targets—for example, number of audits per class of practitioner, or target per cent uptake of recommendations by audited practitioners—against objectives such as increasing practitioner competency and compliance with the Act and the Regulations. However, VBA needs to develop more detailed outcome-based targets and standards to measure whether the audit program is achieving these objectives.

VBA is currently developing a monitoring and evaluation framework. In the interim, its reporting on the performance audit program consists of a monthly divisional report on operations to VBA’s board. Point in time information is also available through an ongoing compliance dashboard.



Advice to VBA's board in July 2014 stated that VBA had 'delivered on VAGO's Recommendations' by virtue of having undertaken the audit of 1 000 building permits and 'associated activities'. While these actions begin to address VAGO's recommendation, the recommendation requires an *ongoing* audit program to be established. The current year is the first of the new audit program and while VBA's corporate and divisional plans indicate that the program is intended to be ongoing, more time will be needed to ensure that the program operates effectively.

Individual actions identified in VBA's industry report, such as issuing guidance to building surveyors need to be finalised. It will also be important for VBA to provide assurance of the effectiveness of the audit program by meeting its commitment to having the audit framework independently reviewed regularly.

VBA has indicated that work to strengthen its audit program is ongoing. It is working to align VBA audit procedures with national standards where appropriate and to establish a practitioner intelligence unit to consolidate data from audits, investigations, levy collection, conciliation services, the customer service unit, and licensing and registration processes. This is intended to enhance decision-making for risk-based regulation. However, to make best use of these resources the potential for expanding enforcement options needs to be considered, particularly in regard to reassessing and recouping levy payable.

### 2.4.3 Building levy

VBA is funded by a levy on building permits and from fees charged to register building practitioners. The levy also funds other agencies, including Building Advice and Conciliation Victoria—discussed in Part 3. VBA is responsible for monitoring the system for collecting building permit levies, which raised \$24.5 million in 2013–14.

Levies are calculated based on the value of the works covered by the building permit and collected by the building surveyor, who then deposits the funds in VBA's Building Administration Fund each month.

VAGO's 2011 report found that BC relied entirely on the surveyor to accurately estimate the value of proposed building works. In the absence of authoritative guidance and systematic monitoring by BC there was no assurance that surveyors were accurately estimating the value of building works, and therefore that all levies due were being recovered. VAGO recommended that BC should develop guidance for surveyors, implement controls to prevent surveyors from using levies collected as their working capital and systematically audit surveyors' estimates of the value of building works.



VAGO's 2011 audit, like the BC's 2011 discussion paper before it, identified two key challenges in collecting the building levy:

- **Reliance on self-reporting**—payment of building permit levies to VBA depends entirely on self-reporting by building surveyors on the number of permits issued and the value of building works they account for.
- **A lack of adequate enforcement powers**—under current legislation, building surveyors who fail to meet their statutory obligations for reporting permits issued, prescribed building activity data and collected levies to VBA each month, or fail to remit all levies received are not committing offences.

### Guidance on determining the value of building works

For three years no action was taken by the then BC or VBA to address VAGO's recommendation to develop guidance for building surveyors on estimating building levy. This perpetuated the situation highlighted by VAGO in 2011 of there being 'no assurance that surveyors are accurately estimating the value of building works'.

There has been ongoing uncertainty about whether any advice issued by the then BC, now VBA, on determining the value of building works would be binding given ambiguities in the Act. VBA sought legal advice during August 2014 on defining the cost of building work under the Act from the Victorian Government Solicitors Office. The advice stated that although the Act is clear that the levy is payable as '0.064c in every dollar of the cost of building work', 'cost' is not defined in the Act, making its meaning 'somewhat ambiguous and uncertain'.

The Bill sought to clarify the method for calculating the amount of levy due. It did this by defining the cost of building works in terms of the contract price, and by giving VBA powers to reassess the costs of building works.

Since this audit commenced, VBA has reviewed and updated the *Reference Guide Building Permit Levy & Building Information*, which includes guidance for building surveyors on estimating the building levy. VBA has indicated that it intends to develop a new definition and methodology to determine the cost of work and to distribute appropriate guidance to surveyors by the end of July 2015. However, it still lacks the legislative authority to reassess the costs of building works in order to recover underpaid levies.

### Preventing surveyors from using levies as working capital

There was little evidence that BC had taken effective action to address the recommendation to prevent surveyors from using levy collected as working capital. Since this audit commenced, VBA has developed a draft practice note and building surveyor levy self-assessment checklist, which contain guidance on the appropriate use and reconciliation of building permit levy funds. These are currently under legal review. Failure to remit levies is not currently an offence under the Act, and without legislative change, compliance with such a practice note can only be monitored through the audit program, not enforced.

## Audit of building permit levy

In 2011, VAGO recommended that BC undertake systematic audits of surveyors' estimates of the value of building works to gain assurance that they are soundly based and that it is preventing financial losses arising from any incorrect valuations.

VBA and its predecessor, BC, have had a levy audit program in place in various forms since 1997. In 2013, VBA established an annual Levy Audit Work Program that targets surveyors based on historical risk posed by type—municipal, private or lodgement organisation, previous adverse audit findings, years of experience, and period elapsed since last audit. However, the program is largely focused on addressing levy leakage—surveyors failing to lodge permits and pay levy at all—not on the incorrect calculation of levy. In 2013–14, \$24 150 was recovered against 19 permits where an incorrect cost of work was reported. This accounted for only about 7.2 per cent of the total \$334 746 recovered by the Levy Audit Work Program in 2013–14, the remainder was recovered from 666 unreported permits.

The focus of the Levy Audit Work Program on levy leakage does not address VAGO's recommendation related to incorrect valuations. However, VBA notes that there is no legislative basis for recouping underpaid levy arising from incorrect valuations. Currently, practitioners may only be investigated and face possible disciplinary action relating to their competence. In contrast, since 2013, VBA has pursued three matters under section 205K of the Act, which provides for civil action against surveyors who fail to pay, and has recovered almost \$100 000.

In the absence of legislative change, VBA has strengthened its practitioner education and its communications to building surveyors in the following ways:

- Receipt confirmation emails are sent to building surveyors when they submit their monthly payment return. These emails contain messages to building surveyors about levy-related issues including:
  - upcoming levy payment return due dates
  - links to levy payment return forms on the VBA website
  - links to building permit activity data summaries—produced from submitted levy payment return data
  - upcoming seasonal events such as Christmas/New Year—many building surveyors close their offices during this period and VBA encourages building surveyors to lodge their levy payment return early whenever possible.
- Information sessions for registered building surveyors have been introduced for 2014–15 aimed at both newly registered building surveyors and those with greater experience.
- Media releases are issued regarding the Levy Audit Work Program, and to highlight particular examples of action against noncompliant building surveyors as a deterrent.

## 2.4.4 Targeting risk areas

VBA's risk-based inspection program 'field-based compliance' uses staff and community intelligence to target areas with a higher risk of noncompliance.

### Field-based compliance

As part of its monitoring and compliance system, VBA established field-based compliance programs from April 2014. These programs are time-limited, targeted investigations and inspections designed to address known noncompliance in the building industry.

Sites are chosen according to their likelihood of presenting a predefined risk, and examined to determine compliance in that area—findings can potentially result in prosecutions or referrals to the practitioner disciplinary system.

In 2013–14, the field-based compliance program focused on the construction of sheds. There were 164 inspections of construction sites of sheds constructed by owner-builders in the Bendigo area, and 143 inspections undertaken in the western suburbs of Melbourne focusing on sites where a registered domestic building manager was overseeing the work. However, the program has not been evaluated which means that its effectiveness in addressing risk is unknown.

The 2013–14 VBA annual report has only one measure associated with the field-based compliance program—number of inspections undertaken, a total of 307. This is an output measure which does not provide information on the effectiveness and efficiency of the program in meeting its objectives. However, VBA is developing a performance measurement and monitoring framework, which needs to contain relevant and appropriate performance measures in order to accurately assess performance.

## 2.4.5 Responsibility for monitoring

Under the Act, councils are responsible for administering and enforcing Parts 3, 4, 5, 7 and 8 and the Regulations in their municipal districts, including:

- issuing building permits and occupancy permits
- undertaking inspections where the council is appointed the relevant building surveyor
- protection of adjoining property
- enforcement of safety and building standards and the Regulations, for both municipal and private building surveyors.

Councils are required to appoint a municipal building surveyor responsible for administering and enforcing these parts of the Act. VBA is responsible for monitoring and enforcing compliance with the provisions of the Act and the Regulations relating to building and building practitioners.

VAGO's 2011 report noted that councils were not clear about whether their role to administer and enforce the Act within their municipalities extends to private building surveyors, and that there were significant opportunities for councils and BC to work together more effectively.

BC established a working group in August 2012 with members from the then DPCD, the Municipal Association of Victoria, the Victorian Municipal Building Surveyors Group and the Australian Institute of Building Surveyors to develop a strategy to address VAGO's recommendations. The strategy, *Towards a cooperative approach between the VBA and Local Government*, was intended to provide guidance to councils and was due for completion in May 2014. The strategy did not support councils' responsibility for administration and enforcement in relation to work undertaken by private building surveyors and considered that this should be undertaken by VBA.

However when the Bill was introduced it clarified that the role of councils is to administer and enforce relevant parts of the Act and the Regulations within its municipality even where a private building surveyor has been appointed.

As a result of this conflict, the strategy was not to be finalised until the respective enforcement roles of VBA and local councils were settled legislatively. The Bill did not pass, which means that VAGO's 2011 recommendations remain unaddressed.

An MOU has been drafted by VBA, the Municipal Association of Victoria and the Victorian Municipal Building Surveyors Group which will be finalised after consultation with council chief executive officers. VBA has also implemented a fast track process for municipal building surveyor referrals to VBA which forms part of the MOU.

It is clear that there has been ongoing uncertainty surrounding the role of councils in administering and enforcing the work undertaken by private building surveyors. However, VBA and the councils could have pursued an administrative solution. Such collaboration is clearly possible, even without legislative change, as is evidenced by the current MOU development. Timely establishment of communication and reporting protocols would have significantly enhanced system-wide monitoring, and assisted the development of audit activities.

## 2.4.6 Information sharing and agency coordination

Systematic information sharing between organisations would assist in identifying patterns of noncompliance and building practitioners that represent potential compliance risks.

CAV and VBA signed an MOU in 2008 acknowledging their joint role in domestic building, and providing for the joint arrangements for Building Advice and Conciliation Victoria, which is located at CAV. Under the MOU, there is an objective to 'enhance inter-agency information sharing and communication'.

Intelligence exchange between CAV, VBA and BPB is currently case specific and limited to on-site conciliations and section 43F referrals, which provide VBA with intelligence on builders. CAV has recently moved to establish a working group with VBA in order to address their relationship, including issues raised throughout the conduct of this audit. A more coordinated approach to practitioner intelligence has the potential to enable CAV to assist VBA in targeting its audit program and performing its practitioner monitoring functions more effectively, and also BPB in undertaking its practitioner disciplinary functions.

## 2.4.7 Reporting and evaluation of monitoring

VBA is responsible for providing assurance that the building control system is working effectively. Effective monitoring, evaluation and reporting on performance is required to enable VBA to perform this function.

VAGO's 2011 report found that BC had no effective performance monitoring framework, and could not evaluate the operation of the building permit system. In response, BC produced a framework in 2012, but this contained no targets, standards or arrangements for assessing system effectiveness. Although an implementation project for the framework was begun in 2013, it was ended to focus on the *Victorian Domestic Building Consumer Protection Reform Strategy*.

VBA remains without an effective monitoring and evaluation framework, although it has begun work on a new framework, by establishing a baseline dataset and reporting requirements. Once the framework is established, VBA should undertake regular reviews to ensure that it is providing meaningful data with which to assess the effectiveness of the organisations activities.

## 2.5 Addressing practitioner misconduct

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There is little evidence that the practitioner discipline system is operating effectively to protect consumers from poor practitioner performance, and current sanctions appear ineffective in deterring misconduct. The disproportionately high representation of building surveyors in BPB inquiries, registration suspensions and cancellations, and reoffending, is concerning given their critical role in assuring building standards.

Correspondence that we received indicates that consumers are dissatisfied with the sanctions applied by BPB:

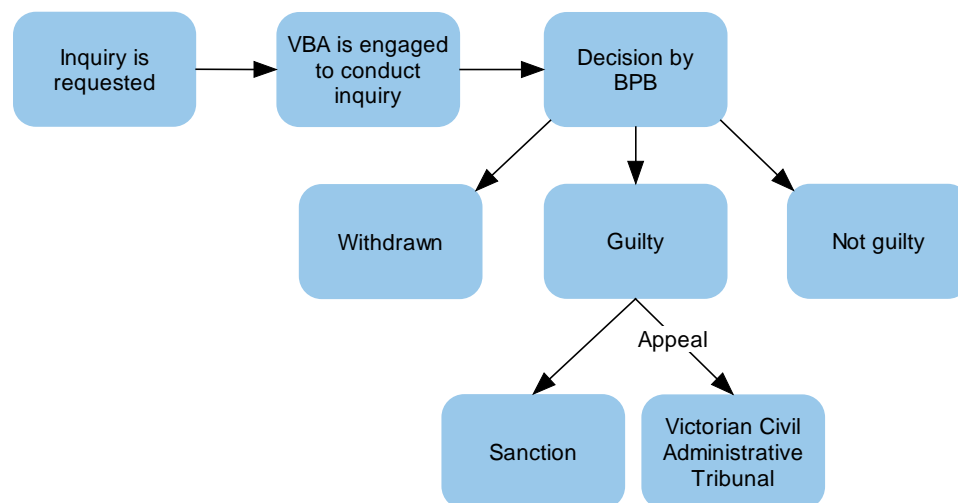
'In regards to our relevant building surveyor [...] he has appeared at least three times in front of the BPB in the past four years [...] Each time he has received a reprimand, fine and costs. He is still registered despite his consistency of noncompliance.'

### 2.5.1 Inquiries and sanctions

#### Process overview

BPB is responsible for disciplining building practitioners and may order an inquiry into the conduct or ability to practise of a registered building practitioner or a building practitioner who was registered or suspended for less than three years at the time of the conduct in question. BPB may initiate an inquiry itself or on the recommendation of CAV, VBA, the Victorian Civil Administrative Tribunal, an insurer, or at the request of any other person, including consumers. The disciplinary process is shown in Figure 2C.

**Figure 2C**  
**BPB disciplinary process overview**



Source: Victorian Auditor-General's Office.

Where BPB has decided to investigate, it appoints VBA to conduct investigations on its behalf in accordance with the Act.

BPB does not have any efficiency or timeliness standards in relation to its disciplinary functions, nor does it measure the time taken to conduct inquiries. In the absence of these measures, it is not possible to determine whether BPB performs this function efficiently.

However, correspondence from consumers suggests the process is lengthy, which underscores the importance of having effective measures related to the efficiency and timeliness of its inquiry and disciplinary functions and outcomes:

'While I am glad BPB has now decided to hold our Inquiry, I am very disappointed that it will be two years between my initial contact to BPB and the Inquiry possibly taking place.'

'We lodged our complaint about the builder with the BPB in early December 2008, but the inquiry was delayed and delayed and the BPB inquiry did not take place until May 2011.'

### Recording and reporting inquiry outcomes and sanctions

BPB's data recording and analysis of inquiry outcomes and sanctions does not allow for trends in risk and offending to be identified to inform training and compliance activities. Outcomes are recorded only as narrative paragraphs in the practitioner disciplinary register. Offences are not recorded in a consistent manner and are often bundled where breaches of the Act have occurred. Sanctions and offence information are not recorded in a database or using similarly functional software making comparison and aggregation difficult.

When a BPB inquiry finds against a practitioner, BPB reports the outcome on its Practitioner Disciplinary Register. VBA publishes this register on its website. The register lists practitioners who have been found guilty of misconduct by BPB, details of any penalties imposed and the suburb or town in which the conduct took place. The register enables consumers to check the record of practitioners before engaging their services. It is updated regularly as findings are made, though BPB and VBA do not promote its use or measure how often it is accessed.

Internal reporting consists of a monthly debrief on recent inquiry and conduct review outcomes and a report from the BPB hearings coordinator at BPB meetings. External reporting of aggregated data on BPB inquiries is limited to an appendix of the VBA annual report as shown in Figure 2D.

**Figure 2D**  
**BPB disciplinary activity 2013–14**

BPB performance	Number
Inquiries and conduct reviews	61
Inquiries completed	53
Conduct review meetings	8
Case proven	52
Dismissed	1
Registrations suspended	5
Registrations cancelled	0
Fines	38
Fines (\$ value)	\$173 383

Source: Victorian Auditor-General's Office based on the VBA Annual Report 2013–14.

BPB has recently sought to extract data to conduct quantitative analysis on its conduct inquiries. This data has been extracted from narrative entries in its disciplinary register and is therefore subject to the following limitations:

- the data set runs from January 2009 to December 2013 and cannot easily be broken down by financial or calendar year
- some information was not able to be extracted from source documents either because it was not available or because it was never recorded
- all percentages are approximations.

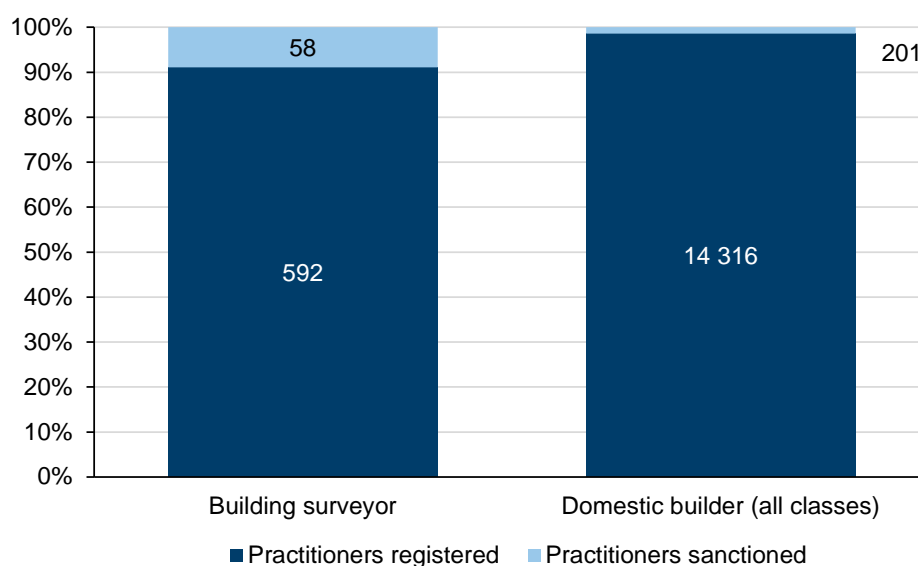
Despite these limitations, VAGO analysis of this available data is presented in the following two sections.

## Offences

Building surveyors are over-represented in BPB inquiries and findings of misconduct. This is concerning given their status within the building control system as 'gatekeepers' of safety and quality. Building surveyors can work on several sites simultaneously and because of the nature of their role have an influence in many more jobs than most builders. BPB inquiries may examine multiple offences at multiple sites—for example, in January 2013 a BS-U was found guilty of 17 offences in relation to five sites, while in 2010 another was found guilty of 25 offences relating to 11 sites.

Between January 2009 and December 2013, 58 building surveyors appeared before BPB with all found guilty of at least one offence. This represents nearly 10 per cent of registered building surveyors, with 16 of those 58 appearing more than once. Despite making up just 2.8 per cent of Victorian building practitioners, building surveyors represented approximately 16 per cent of BPB inquiries, and accounted for 36 per cent of allegations against all building practitioners during this period—with 86 per cent of these allegations against building surveyors proven—see Figure 2E. VAGO observed a similar trend in the 2000 audit where it found building surveyors accounted for one in every three complaints received.

**Figure 2E**  
**Proportion of surveyors and domestic builders sanctioned by BPB,**  
**January 2009 – December 2013**



Source: Victorian Auditor-General's Office based on information from BPB.



Most of the allegations brought before BPB for all building practitioner types between January 2009 and December 2013 resulted in a guilty ruling, noting that individual practitioners routinely face multiple allegations. Guilty rulings were made for 89 per cent of allegations against domestic builders-unlimited, 86 per cent of allegations against building surveyors, 91 per cent of allegations against domestic builder-managers and 81 per cent of allegations against building inspectors. The most common offence was that the practitioner failed to comply with the Act or the Regulations, followed by unprofessional conduct. A small percentage of allegations—1 per cent of allegations against building surveyors and 2 per cent for domestic builder-unlimited—found that the building practitioner was not a fit and proper person to practise as a building practitioner.

## Sanctions

The Act defines the decisions that can be made at a conduct inquiry. These range from finding a practitioner guilty of unprofessional conduct to finding they obtained registration or the required insurance by fraud or misrepresentation.

BPB may impose sanctions. Those most commonly imposed include:

- reprimanding the person
- requiring the person to complete a specified course of training
- suspending registration for not more than three years
- disqualifying the person from being registered for a period of up to three years.

In the most serious cases, BPB may cancel the practitioner's registration. In the past five years, 32 practitioners have had their registration cancelled.

From January 2009 to December 2013, the majority of BPB inquiries related to DB-U and building surveyors. On average during this period a registered building surveyor in Victoria was over five times more likely than any other class of practitioner to be suspended by BPB and almost seven times more likely to have their registration cancelled. While the over-representation of building surveyors in disciplinary hearings may be partly due to the fact that surveyors work concurrently on multiple jobs and complete more jobs in any given time period than builders, it is still concerning, given the critical role of surveyors in ensuring the safety and accessibility of buildings.

All building surveyors and domestic builders-unlimited found guilty by BPB received some form of sanction, the most common being a reprimand. However a reprimand was rarely applied as a sole sanction. The percentage of building practitioners subject to each sanction is shown in Figure 2F.

**Figure 2F**  
**Sanctions applied to practitioners found guilty by BPB**

Sanction	Domestic builder-unlimited	Building surveyor
Reprimand	59%	100%
Required to pay costs	94%	97%
Fined	65%	75%

Source: Victorian Auditor-General's Office based on information from BPB.

The range of costs imposed on both surveyors and DB-U ranged from less than \$1 000 to over \$80 000 with 45 per cent of surveyors' costs and 54 per cent of DB-Us' costs falling in the range of \$1 000 to \$5 000. Fines imposed on surveyors and DB-Us ranged from less than \$1 000 to almost \$15 000 with 45 per cent of surveyors' fines and 58 per cent of DB-Us' fines falling in the range of \$1 000 to \$5 000. BPB is limited in its capacity to impose fines by section 179(2) of the Act which sets a maximum fine of 100 penalty units—equal to \$14 761 until 30 June 2015.

Between 1 July 2009 and 23 July 2014, 22 building practitioners of all classes—mostly building surveyors and DB-Us—were found guilty by BPB on more than one occasion. An examination of sanctions imposed indicates that sanctions typically escalate with successive appearances. Five practitioners who received a combination of reprimands, fines and costs imposed in their first appearances, had their registrations suspended or cancelled at their next appearance. However, given the number of building practitioners, particularly building surveyors, who have appeared multiple times before BPB in this period, it is worth assessing the effectiveness of current sanctions in acting as a disincentive to engage in misconduct.

BPB has recently undertaken similar analysis of its disciplinary outcomes data. Recognising the limitations of the data identified above, and in preparation for assuming the functions of BPB, VBA has begun work to facilitate an improved data capture process within its Compliance and Performance Division.

## 2.5.2 Prosecutions

VBA's prosecutions focus on unregistered builders and builders operating without a valid permit. VBA seeks criminal prosecutions in the Magistrates' Court when the conduct of a building practitioner is serious in nature and/or where it considers the breach of the law was conscious and deliberate. It also seeks criminal prosecutions against individuals who perform building or works without being licensed or registered in Victoria. VBA's prosecution guidelines outline the factors VBA consider in deciding whether or not to prosecute. In addition, VBA is directed by the Director of Public Prosecution's prosecutorial discretion guidelines.

In 2013–14, VBA prosecuted 28 people in the Magistrates' Court:

- A person practising as a building surveyor while unregistered was fined \$10 000.
- A project manager was fined \$10 500 for entering into a major domestic building contract and carrying out the work without a permit, registration or insurance. The prosecution in this instance is a *Domestic Building Contracts Act 1995* prosecution under the authority of the Director CAV.
- A person who identified himself as a registered draftsman and registered engineer, despite not holding the relevant registrations, was fined \$4 500.
- A company director was ordered to complete 100 hours of volunteer work after being charged with carrying out work without a permit and without registration.

## Recommendations

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1. That the Department of Environment, Land, Water & Planning and the Building Practitioners Board, in consultation with the Victorian Building Authority, reviews the practitioner registration and discipline regimes, and advises government accordingly, so that:
    - only qualified, competent and suitable practitioners are allowed to trade
    - practitioners have necessary building, business and financial skills and experience, appropriate resources and character, and fully understand their responsibilities and obligations
    - monitoring provides assurance that practitioners maintain and update their skills over time and as building practices evolve
    - practitioners' suitability for registration can be reassessed at the expiration of a finite registration period
    - disciplinary systems and sanctions ensure that there is sufficient disincentive to engage in misconduct and that registered practitioners who do so can be excluded from trading
    - data from registration and discipline regimes is collected and analysed to inform system improvements.
  2. That the Department of Environment, Land, Water & Planning reviews the regulatory arrangements governing the engagement of building surveyors to ensure they support the independent and objective performance of their function to provide appropriate independent oversight of building and the building system.
  3. That the Victorian Building Authority reviews its monitoring and compliance framework, and takes action, including advising the Department of Environment, Land, Water & Planning where necessary, to:
    - identify poor practitioner performance and appropriately prosecute and/or refer for discipline
    - prioritise the monitoring and enforcement oversight of relevant building surveyors
    - clarify respective agency responsibilities for monitoring and compliance including expediting the establishment of a memorandum of understanding to clarify the roles of the Victorian Building Authority and councils for monitoring and enforcing compliance with the *Building Act 1993*
    - effectively administer the building permit levy including expediting the establishment of arrangements to allow the Victorian Building Authority to reassess and recoup underpaid levies, and require surveyors to remit levies promptly.
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# 3 Consumer education and dispute handling

## At a glance

### Background

Consumer Affairs Victoria (CAV) manages key parts of Victoria's consumer protection framework for domestic building. It provides education and information, undertakes conciliation, compliance activities such as the Better Business Initiative and enforcement action under the *Domestic Building Contracts Act 1995*. The Victorian Building Authority (VBA) receives complaints relating to the *Building Act 1993* and undertakes inspections of domestic building works, which support Victorian Civil and Administrative Tribunal hearings.

### Conclusion

CAV's building conciliation and dispute resolution functions provide limited consumer protection because CAV is unable to compel parties to undergo conciliation or enforce compliance with the negotiated outcomes. CAV and VBA do not adequately measure performance which means their effectiveness is not clear. CAV, VBA and the Building Practitioners Board do not effectively coordinate education and information to better assist consumers.

### Findings

- The effectiveness of CAV's conciliation service is limited by its inability to make participation mandatory and to issue binding rectification orders.
- CAV does not have relevant and appropriate performance measures and robust evaluation methods to determine the effectiveness of its activities.
- CAV has consistently briefed government on potential framework and legislative improvements.
- CAV and VBA could improve their information sharing, although steps have recently been taken to address this.

### Recommendation

That Consumer Affairs Victoria reviews its dispute resolution and conciliation activities and advises government on options to improve their effectiveness.

## 3.1 Introduction

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Consumers need to understand the domestic building system to make well-informed choices when choosing a practitioner, entering a building contract, and exercising their rights.

Consumer Affairs Victoria's (CAV) stated purpose is to help Victorians to be responsible and informed businesses and consumers. CAV's domestic building related functions are funded by consumers through the building levy, which it uses to fund a number of activities including:

- receiving and assessing complaints
- providing advice and conciliation services
- education and information programs for consumers and businesses
- compliance, enforcement and prosecution.

CAV also supports and provides advice to the Minister for Consumer Affairs in administering and reviewing the *Domestic Building Contracts Act 1995* (DBCA) which regulates domestic building work and provides for dispute resolution and domestic building insurance.

CAV has a role under the DBCA to receive complaints. While other bodies also accept building related complaints, CAV receives a much higher volume of complaints from consumers, which reflects its status as the state's consumer protection regulator.

Building Advice and Conciliation Victoria (BACV) conducts conciliations to resolve domestic building disputes. BACV is a division of CAV, jointly provided with the Victorian Building Authority (VBA) under a memorandum of understanding (MOU) between both organisations. It accepts complex or higher-value complaints for conciliation, provided there is a 'reasonable likelihood' of resolution, as required by the DBCA.

## 3.2 Conclusion

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CAV's building conciliation and dispute resolution function does not provide consumer protection because CAV is unable to compel parties to undergo conciliation or enforce compliance.

There is a lack of relevant and appropriate performance measures for both CAV and VBA's activities. Both VBA and CAV's functions are not well understood and are perceived as ineffective. Due to a lack of performance measurement, neither organisation fully understands the extent of this issue.

There is insufficient coordination and information sharing between CAV and VBA which means that despite the large volume of education and information provided, consumers may not always find the relevant information. CAV, VBA and the Building Practitioners Board (BPB) should more actively promote the disciplinary register and other tools that can assist in informing consumers and reducing consumer detriment.

Until recently, VBA had not addressed any of VAGO's 2011 audit recommendations. While VBA has recently introduced a new framework to handle complaints and to manage its investigations, it is too early to assess its effectiveness.

While CAV should improve its information, coordination and performance measurement, it has consistently provided advice to government and departmental heads about potential improvements to the consumer protection framework.

### 3.3 CAV's role

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As part of its role, CAV is responsible for advising the Minister for Consumer Affairs on the DBCA. The objectives of the DBCA are to:

- provide for the maintenance of proper standards in the carrying out of domestic building work in a way that is fair to both builders and building owners
- enable disputes involving domestic building work to be resolved as quickly, efficiently and cheaply as is possible having regard to the needs of fairness
- enable building owners to have access to insurance funds if building work under a major domestic building contract is incomplete or defective.

In practice, the DBCA limits CAV's ability to balance consumer and practitioner needs, and limits its capacity to achieve the legislative objectives of the DBCA.

Under the DBCA, CAV is unable to mandate conciliation or enforce any outcomes. CAV has consistently briefed the minister and departmental heads on the need for mandatory conciliation and the power to issue binding rectification orders. This suggests it is proactively advising government on potential improvements to the system. CAV has taken positive steps to address these limitations by including a focus on education, information and compliance activities such as the Better Business Initiative (BBI) that aim to reduce noncompliance before it occurs.

Section 43D of the DBCA gives CAV the power to institute proceedings on behalf of a building owner in a domestic building dispute. CAV uses this power to issue enforcement letters and instigate court proceedings at its discretion, although the rate at which it does this has declined significantly over the past five years. In 2014, CAV instigated court actions in one case where it alleged breaches of the DBCA and Australian Consumer Law (ACL). The number of court actions has declined from 13 in 2009–10, to 10 in 2010–11, seven in 2011–12, and four in 2012–13. According to CAV, this decline is the result of the proposed transitioning of dispute resolution and conciliation functions to VBA as per the former government's policy. As of 2015, CAV will retain these functions following the change of government.

Domestic building activities at CAV are funded by consumers through the building levy, which VBA collects as part of the building permit application process. CAV's Trust Fund Governance Committee provides advice and recommendations to the Director CAV, who is responsible for managing these funds in accordance with CAV's Trust Funds Investment Policy. These funds were valued at \$10.346 million at July 2014. According to the Trust Funds Investment Policy, the fund is to be used to carry out CAV's objectives.

## 3.4 Consumer education and understanding

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Some consumers are confused about the options for resolving their building construction issues, relevant processes and the role of relevant agencies. Addressing these misunderstandings is critical to reducing consumer detriment. Briefings by CAV to departmental heads and government support this finding.

Previous reviews, audits and correspondence from consumers received by the Auditor-General indicate that consumers are both surprised and disappointed by the limited powers of regulatory agencies. The *Victorian Domestic Building Consumer Protection Framework Public Consultation Paper April 2012* also noted that there was 'scope to improve consumer awareness of available information'. For example, BACV can assist in negotiating an outcome between a consumer and practitioner, but neither BACV nor VBA can compel a practitioner to rectify defective work. However, consumers are not always aware of this:

'The items on the report remained defective and the builder simply walked away—what are we supposed to do when the report states 'Neither the VBA nor the inspector can direct the builder to carry out the rectification work'.'

'Why have all these government departments and guidelines if consumer affairs and the VBA can't enforce what is written?'

Consumers appear confused about the role of some agencies in the framework. For example, the BPB inquiry and sanction functions are entirely disciplinary in nature. It has no power to provide restitution to consumers. Consumer correspondence to the Auditor-General suggests this is not well understood:

'The end result once the inspection report was submitted was that the builder responded not to us (as we were expecting) but to the BPB. Now this is the confusing part. The BPB does not pay for this home's mortgage or live here. We do!'

### 3.4.1 Agency roles

It is unclear whether CAV and VBA's education and information services are effective because there is insufficient coordination and cross-referencing of performance measures that measure consumer awareness of these services.

CAV, VBA and BPB provide consumer education and information mainly online through their respective websites:

- CAV provides education, advice and resources to assist consumers in planning and managing a building contract.
- VBA provides a range of technical resources for consumers, including fact sheets on specific problems such as termites.
- BPB maintains the disciplinary register, which currently has 387 building practitioners listed, and is accessible through VBA's website.



BPB's disciplinary register is difficult to locate on VBA's website, and it is not linked to CAV or VBA. Similarly, while VBA provides some suggestions to consumers about domestic building contracts on its 'contracts' webpage, it doesn't mention CAV's provision of a model contract for consumers and provides a link only to its homepage, not directly to CAV's contract assistance pages.

All agencies should make links to the register and model contract more prominent on their websites and as part of information and education tools to alert consumers to practitioners who have previously engaged in misconduct.



### 3.4.2 CAV's consumer education services

CAV focuses its consumer education services on preventing disputes by educating consumers on their rights and responsibilities. CAV's resources and services for consumers include:

- information designed to assist them in seeking quotes, choosing a builder and managing their contract
- checklists to guide them through entering a domestic building contract
- complaint forms
- social media communications and advertisements to inform them of CAV services should the need arise.

Since at least 2007, CAV has repeatedly briefed government that it believes that some industry contracts were biased in favour of industry with unfair contract terms, which breached the DBCA. As a result, CAV developed a model domestic building contract which it released in 2012.

All of these activities have the potential to reduce overall consumer detriment. However, CAV does not have performance measures for its consumer awareness or education and information services, which means the extent of their effectiveness is unclear. Despite this, its development of the model contract and associated checklists are positive steps, and its briefings on issues with industry contracts support its education activities.

## 3.5 Complaints and conciliation

The effectiveness of CAV's functions, and the extent of consumer protection they afford, is limited by CAV's inability to compel parties to participate in conciliation or enforce compliance with negotiated outcomes. This means that CAV cannot effectively protect consumers where both parties do not agree to conciliation. The remaining options for these consumers, such as Victorian Civil and Administrative Tribunal (VCAT), are expensive and may be out of reach. In addition, while CAV collects extensive data, it cannot demonstrate that it analyses or uses the bulk of this data to improve the efficiency or the effectiveness of its service, with the exception of BBI. This means it does not fully understand the impact or benefits derived from its conciliation service.

### 3.5.1 Accepting complaints

CAV's enquiries service is the first point of contact for consumers and building practitioners. CAV uses a triage approach to assessing complaints, and has detailed policies and procedures for complaints, Front Line Resolution (FLR) and conciliation, and has a BACV operating manual. CAV receives complaints and assesses them to determine suitability for conciliation, or whether a consumer should be referred to another body such as VBA or VCAT. CAV has a set of operating principles and a protocol with VBA for the referral of complaints under the MOU, which is detailed in Figure 3A.

**Figure 3A**  
**Operating principles and complaints handling**  
**under the MOU**

CAV	VBA
CAV is the first point of contact for all domestic building complaints	VBA accepts referrals from CAV relating to registration and technical matters
Solely technical matters will generally be referred by CAV to VBA	VBA has responsibility for solely technical matters
CAV will implement a triage approach to written complaints received	
In the process of resolving written complaints, CAV provides conciliation services	VBA provides technical inspection services
Builders can access the complaint resolution service	VBA supports BPB to hear cases in relation to building practitioners
The parties will explore opportunities to work together onsite where appropriate, CAV will provide conciliators	The parties will explore opportunities to work together onsite where appropriate, VBA will provide technical inspectors
CAV provides information and education services to consumers and building practitioners in relation to the DBCA	VBA provides information and education in relation to registration and training

Source: Victorian Auditor-General's Office.

Disputes that are not complex are dealt with by CAV using FLR—typically provided over the phone. All complaints are triaged by the Evaluation and Assessment Team of CAV's Information and Disputes Service Centre. Higher value or complex complaints are then referred to the Trader Compliance Services Branch to be assessed for suitability for conciliation by BACV.

CAV's Conciliation Policy includes a set of criteria that it uses to assess complaints to determine their suitability for conciliation, which in summary include:

- the complaint is within CAV's jurisdiction
- there appears to be a breach of contractual rights or consumer legislation
- CAV believes the complaint warrants involvement for consumer protection purposes and for the promotion of an informed and responsible marketplace
- the consumer has made a reasonable attempt to resolve the dispute with the trader
- the consumer has not breached the contract
- the complaint is reasonably likely to be settled
- VCAT or the courts have not already determined the matter and no case is pending.

Accepting a complaint is at CAV's discretion, and it may take into account any circumstances that suggest the dispute is unlikely to be settled, for example, if the builder is not able to be contacted. This approach is appropriate, given CAV's inability to compel parties to conciliate. However, there may be a gap between consumer expectations and CAV's approach.

CAV monitors the status of complaints undergoing FLR and those managed by BACV. It determines whether complaints should be referred to conciliation based on the level of financial or other individual consumer detriment, the frequency of the complaint amongst consumers and therefore the likelihood that establishing a resolution will assist other consumers, and the overall likelihood of resolution, which is a key legislative requirement. However, with the exception of the BBI, the lack of performance measures or evaluation associated with CAV's conciliation process means that its effectiveness is not known.

### 3.5.2 Conciliation process

Conciliation is a voluntary process, which means that in effect, there is no recourse to CAV if one party is unwilling or unable to participate. In these instances, CAV may advise a party to lodge a dispute at VCAT. However, seeking resolution of a building dispute through VCAT can be costly and time consuming:

'How are we to find the money to pay for an estimated 10-day hearing, which can cost \$10 000 per day? Show me an average person who has a spare \$100 000 in their back pocket to spend on fighting for something they've already paid for.'

CAV applies threshold criteria for undertaking conciliation and will do so only where there is a 'reasonable likelihood' of resolution, as required under the DBCA and in line with government policy. CAV's definition of resolution is 'where conciliation is commenced and an agreement between the parties is able to be reached... unless there is reason to believe the agreement may fall over or a follow up may be necessary'.

According to CAV, it will take on cases for conciliation where there is no breach of contractual rights, to assist in negotiating acceptable outcomes for consumers and building practitioners. This can include instances where there are customer management issues which lead to relationship breakdown. CAV should review this practice to determine whether it is the best approach to complaints where there is no breach of rights.

Conciliation may be undertaken by CAV even in the absence of a breach of consumer rights, and is therefore fundamentally about establishing a compromise between two parties in conflict, rather than the pursuit of consumer satisfaction or compensation.

Consumer correspondence received by the Auditor-General indicates that consumers may misunderstand CAV's role and its undertaking to provide conciliation, and see this as CAV supporting their claim. Consumers may be subsequently disappointed when conciliation does not result in an enforceable order to the builder to address their grievances:

'Most people assume new home builders are protected in the same way as new car buyers. Unfortunately, this is not so. Our experience of the building project revealed a deplorable code of builder conduct, home warranty insurance that can only be described as junk and massive failures by building, regulators and agencies to properly investigate consumer claims.'

'An urgent call was made to the first BACV conciliator [...] His advice was for me to 'get a lawyer and go to VCAT'. I then realised that all my efforts had been in vain.'

CAV produced a domestic building strategy in 2011 outlining its approach to domestic building compliance in a shared regulatory environment with the Building Commission (BC). Included in the program management approach was a target of 40 per cent of conciliations to be conducted onsite by BACV with representation from BC, now VBA.

In 2012, following a restructure and to meet government savings targets, the program management approach and its target were discarded. However, onsite conciliation has remained a focus of CAV, with 578 onsite conciliations undertaken in 2013–14. CAV focuses on onsite conciliation where a dispute is related to defective work, because it believes that this method achieves a higher rate of success. CAV concluded this as the result of a review of 350 BACV cases in 2010, but has not reviewed its decision since to ensure its effectiveness.

## CAV's system for determining the outcome of complaints

CAV uses a system of coding to assign outcomes to complaints, including where a complaint may be referred to another agency, where a complaint cannot proceed to conciliation because a building practitioner cannot be located or contacted, where conciliation cannot achieve a compromise, ineligible complaints, or where no action is required by CAV.

CAV assigns 'complaint resolved' not only to conciliations, but to matters in which CAV assisted in some way. However, complaints are sometimes listed as 'complaint resolved' without any follow up with the consumer to confirm that this is in fact the case, as Figure 3B highlights.

**Figure 3B**  
**Case study**

A consumer called and engaged a trader to build their home (which has been done) but is reluctant to deal with a mound of dirt left near the garage. The home is nearly finished and ready to be handed back to the consumer. The CAV officer contacted the trader to ask that he/she contact the consumer, which the trader agreed to. The complaint was then closed and the outcome code 'complaint resolved' was applied.

*Source:* Victorian Auditor-General's Office based on CAV FLR case notes.

While resolution of a complaint, at least in the case of conciliation, does not necessarily mean the consumer is satisfied with the outcome, it is difficult to see in the above case how CAV could consider resolution had occurred without following up the agreed actions. However, according to CAV, consumers will always inform it where a party has failed to comply with a resolved complaint and follow up by CAV officers is undertaken, although case notes provided do not always demonstrate this. In addition, CAV's inability to enforce any agreement made under conciliation means that it does not follow up on action. CAV assigns complaints as 'resolved' in instances where it considers that the outcome achieved by a conciliation, or through other means to which it may not have directly contributed, enables the parties to move forward without further escalation.

## Complaints monitoring and data collection

CAV is the main receiver of complaints from consumers about building-related issues. In 2013–14, it received 21 342 telephone enquiries compared to VBA's 2 014.

CAV collects extensive output data about the number of complaints it receives, but apart from its annual customer satisfaction survey, it does not currently collect any outcome-based data. CAV does not collect data on consumer or builder satisfaction levels or on the outcomes of closed building disputes. The annual satisfaction survey is of consumers of the Information and Disputes Service Centre and does not include BACV, and CAV does not survey builders. In 2014, 20 building consumers were surveyed, which does not provide meaningful information about overall consumer satisfaction in domestic building. In addition, CAV's system of outcome coding and FLR note taking does not provide the rigour needed to understand the reasons why complaints may or may not be resolved. This means that CAV's effectiveness in resolving complaints is unclear.

Figure 3C provides data on complaints at CAV from 2009–10 to 2013–14.

**Figure 3C**  
**CAV building activity 2009–2014**

Activity	2009–10	2010–11	2011–12	2012–13	2013–14
Total building calls answered	35 155	39 871	36 849	25 169	21 342
Complaints received in writing	2 325	2 889	3 823	3 244	2 285
Complaints received face to face	28	45	87	61	60
Complaints received via telephone	54	31	235	243	338
<b>Total complaints assessed</b>	<b>2 407</b>	<b>2 965</b>	<b>4 145</b>	<b>3 548</b>	<b>2 683</b>
Building disputes subject to conciliation	1 694	2 078	2 672	2 353	1 833
Percentage of building disputes that met CAV's criteria for conciliation	70%	70%	64%	66%	68%
FLR disputes finalised	0	2	337	314	523
BACV total disputes finalised	2 038	2 356	2 364	1 932	1 399
BACV total disputes subject to conciliation	1 584	1 877	1 825	1 459	1 141
Onsite conciliations undertaken	245	796	845	696	578

Source: Victorian Auditor-General's Office based on information from CAV.

There are a number of flaws in CAV's collection and reporting of information, including that it does not:

- collect information on the total number of consumers facing building difficulties
- seek to share and compare information about the proportion of overall complaints it receives compared to VBA and BPB.

CAV should consider adopting these practices, because collecting this information would assist it to understand the effectiveness and efficiency of its complaints handling and conciliation services, and allow it to better target its resources.

### 3.5.3 Complaints to the VBA

BC took no action to address VAGO's 2011 recommendations on complaints handling. VBA began to address these when it was established on 1 July 2013, but did not adequately do so until late 2014 when it introduced new complaints handling policies and procedures. The recent implementation of these means it is too early to determine their effectiveness.

#### Complaints handling processes

In 2013–14, VBA received 2 014 complaints about building practitioners—956 formal written complaints and a further 1 058 complaints on its building complaints telephone line.

Similar to CAV, VBA receives consumer complaints directly in cases where consumers are seeking a solution and also on behalf of BPB where consumers wish to request an inquiry.

In 2011 VAGO found that BC did not have appropriate arrangements to prioritise complaints or improve the complaints system. There were no quality assurance standards for handling complaints and no performance measures.

VAGO recommended that BC strengthen its complaints handling and investigation processes to:

- systematically prioritise and clearly document complaints according to the risk of noncompliance with safety and technical building standards
- investigate complaints with reference to clear standards of effectiveness and efficiency, and regularly review and monitor adherence to these requirements.

In November 2011, BC finalised its complaints management policy and its complaints assessment and procedures. These contained clear standards of efficiency with target time lines for most processes, but lacked standards for effectiveness, reporting time lines, and the requirement of the involvement of technically qualified staff. Despite the emphasis on internal review as a guiding principle in the Complaints Management Policy, there was no process for ensuring senior management was involved and no evidence that such a review ever occurred. Given these limitations, it is doubtful that the policies and procedures developed by BC could have addressed VAGO's recommendation.

VBA's revised complaints assessment and procedures policy and complaints management operational policy came into effect on 12 January 2015. These documents establish a clear triage process to prioritise complaints according primarily to the risk of noncompliance with safety and technical standards, and then in relation to a range of other factors including:

- the remaining time frame for potential consumer legal action
- whether the matter is a referral from a municipal building surveyor
- if the subject of the complaint has 'also had an unacceptable number of complaints and investigations and/or prior findings by the BPB'.

The assessment process incorporates both technical and customer service staff.

It is difficult to assess the effectiveness of the complaints management framework given that it has been in place for a short period of time. While the policy includes a requirement to keep clear, comprehensive and current file notes on each complaint and the progress of aspects of the process are tracked, for example, the delivery of technical inspection reports, a comprehensive performance reporting framework is still under development. It is important that VBA assesses the effectiveness of this policy once it is fully established.

### 3.5.4 Investigations and inspections

Both CAV and VBA lack comprehensive performance reporting frameworks for complaints management, investigations, and inspections. This means the effectiveness of these processes cannot be determined.



CAV and VBA are responsible for investigating complaints, and for providing onsite services to both consumers and building practitioners to assist in conciliation and to provide evidence to assist in achieving an outcome, or for future action through VCAT or BPB's practitioner disciplinary process.

An MOU between CAV and VBA sets out the arrangements to jointly operate BACV. BACV's service includes onsite conciliation, and inspections and investigations. CAV and VBA may work together in some instances by attending domestic building sites with both a conciliator, from BACV at CAV, and a building inspector, from VBA. The objectives of the MOU are to improve:

- coordination in complaint handling by VBA and CAV
- time lines for complaint resolution and referral
- inter-agency information sharing and communication
- information and communication to builders
- information and communication to consumers
- linkages between compliance and enforcement activities and disciplinary actions against registered builders.

Neither CAV nor VBA have ever sought to measure or assess the extent to which the objectives of the MOU are being met. As a result, it is not clear whether these arrangements are effective. While CAV and VBA have collaborated on some educational initiatives, information sharing could be improved, for example, in relation to building practitioners who are under investigation by VBA and the subject of a complaint to CAV at the same time. This could inform conciliation activities and reduce overall consumer detriment.

According to CAV, building complaints are a priority because of the high level of potential detriment to consumers. How a complaint is investigated depends on the value of the complaint and the likelihood of it being resolved— complaints over \$10 000 are always allocated to BACV, while complaints of a lesser monetary value are allocated to general conciliation. This includes FLR or general conciliation for cases between \$5 000 and \$10 000 that do not relate to defective work. Defective work cases over \$5 000 are allocated to BACV.

Where disputes cannot be resolved and the consumer is seeking redress, CAV recommends that the consumer apply to VCAT to have the matter resolved.

### The VBA

Until the establishment of VBA in 2013, there was no evidence that its predecessor organisation—BC—had addressed any of VAGO's 2011 audit recommendations.

VBA investigates complaints and conducts inspections producing inspection reports which can be used in conciliation processes, but also produced as evidence at VCAT hearings.

VAGO's 2011 audit was critical of BC's investigative and inspection processes finding that most were outsourced with no clear guidelines, documented standards or procedures to ensure investigations were effectively handled.



VAGO recommended that BC strengthen its complaints handling and investigation processes to:

- provide investigators with sufficient training to enable them to form appropriate judgments about technical building matters
- establish clear quality assurance standards and effective controls for technical reports sourced from its external panel to enable them to be competently prepared.

There is no evidence BC took any action to address these recommendations. Action was first taken in July 2013 when VBA issued expressions of interest for external consultants and reviewed and updated their skills requirement for external consultants acting on the technical panel used to supplement internal investigative and inspection resources.

VBA has made recent improvements, including updating its investigations policy and issuing a detailed Investigations Manual in October 2014. Investigations are now undertaken in-house by VBA investigators who have a Certificate IV in Government (Investigation) qualification. VBA investigators are responsible for gathering evidence for dispute resolution and preparing briefs of evidence for potential prosecutions.

VBA has established an enhanced training program for investigators to increase their technical skills including:

- a 1.5 day internal training session on recognising basic technical building faults
- a guest speaker program featuring investigators from other regulators sharing their skills and experience
- a nationally recognised cognitive interview training course.

VBA has advised that it is currently working to ensure its investigation processes comply with the Australian Government Investigation Standards where applicable.

Building inspectors are qualified to inspect building work and determine its compliance with the *Building Act 1993* and the *Building Regulations 2006*. VBA assigns a building inspector to conduct an inspection if detailed technical knowledge is required, and inspectors may then advise VBA's building investigators or assist by attending inspections.

VBA has an in-house team of building inspectors, whose inspection reports are reviewed by VBA building surveyors to ensure their quality and consistency. The current rate of required inspections exceeds VBA's capacity, which means it uses an external panel of contract inspectors. According to VBA, the inspection reports prepared by these contracted inspectors are reviewed by VBA building surveyors to ensure consistent standards apply throughout.

Individual inspectors are provided with feedback on their reports and this feedback, in addition to timeliness tracking, is recorded in a technical reports log. Reporting to the VBA board on the volume and progress of investigations and inspections is conducted through the regular compliance and performance division report on operations. At 31 October 2014, there were 247 current investigations into building practitioners being undertaken by VBA, a decrease of 13 on the previous month.

VBA's actions in response to VAGO's 2011 report to improve inspector training and ensure the standard of external technical reports are positive. However, these initiatives are all recently established and their effectiveness is not yet well understood. VBA should evaluate these programs to ensure they are achieving their objectives.

### 3.6 Is conciliation effective?

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CAV's performance measurement is inadequate. It provides information that is limited largely to the volume of its outputs, with the exception of the complaints reporting used for the BBI, which demonstrates a reduction in complaints for the builders that participate.

Monitoring and reporting are important in assisting CAV to identify trends and measure success, which in turn may enable it to provide more relevant and targeted services as a result.

CAV uses a range of strategic documents to set out its vision, objectives, and actions underpinning these, including its 2010–14 strategic directions document. While this document clearly outlines CAV's vision and priorities for the four-year period, it did not commit to evaluation. This means that CAV cannot be assured that it has achieved its objectives.

CAV recently developed its corporate plan 2015–18, which outlines its vision of 'a fair and competitive marketplace in Victoria', with updated goals including:

- businesses are compliant with consumer laws
- Victorians exercise their consumer rights
- a fair and safe rental market for Victorians
- a modern and effective consumer law framework
- a sustainable and innovative regulator.

The corporate plan does not specifically commit to evaluation, but does mention that CAV's strategy will be driven 'through a continually improving planning process that is integrated with evaluation'.

While CAV monitors its work through monthly, quarterly and half-yearly updates, these focus on output rather than outcome measures. This reporting does not include any robust evaluation of whether CAV is achieving its domestic building objectives. Reporting through CAV's annual report and Budget Paper 3 (BP3) measures does not enable an understanding of its effectiveness in supporting consumer protection for domestic building activity.

### 3.6.1 Internal reporting

CAV's reporting consists mainly of output reporting on the number of complaints, conciliations, and some limited reporting using outcome codes for the results of its conciliations process. CAV undertakes output reporting across several areas:

- monthly data on calls and enquiries
- key performance indicators, including referrals to VBA, profile of complaints finalised, time taken, and whether a complaint was subject to conciliation
- quarterly reporting on unregistered builders with major domestic building contracts and other enforcement issues
- quarterly reporting against the corporate plan, which focuses on project status updates and progress against output based BP3 measures.

This type of reporting means CAV has a good understanding of the volume and type of complaints it is dealing with. CAV has a relatively high rate of conciliations resolved, but it does not know the ultimate outcome of conciliations. In addition, reporting is not sufficient to determine the performance of CAV's domestic building activity. With the exception of BBI, CAV's performance measurement of its dispute handling and conciliation functions is inadequate and provides little insight into whether services are meeting community expectations and legislative or policy objectives.

### 3.6.2 External reporting

#### Budget Paper 3: Service Delivery

CAV reports its performance externally through its annual report, and through the Department of Justice & Regulation's BP3 measures. To assist it with external reporting, CAV undertakes monthly reporting on the volume of complaints it receives, including what proportion go to conciliation at BACV. CAV uses this information to track its progress against BP3 measures which cover the whole of CAV's operations, and are detailed in Figure 3D.

**Figure 3D**  
**CAV BP3 measures**

Type of performance measure	Performance measure
Quantity	<ul style="list-style-type: none"> <li>• Information and advice provided through telephone service</li> <li>• Information and advice provided through other services including written correspondence, face to face and dispute assistance</li> </ul>
Major outputs	<ul style="list-style-type: none"> <li>• Number of compliance activities, from compliance assistance through to court actions</li> <li>• Number of registration and licensing transactions</li> <li>• Number of Residential Tenancies Bonds Authority transactions</li> </ul>
Quality	<ul style="list-style-type: none"> <li>• Customer satisfaction with services provided</li> </ul>
Timeliness	<ul style="list-style-type: none"> <li>• Services provided within agreed time frames</li> </ul>

Source: Victorian Auditor-General's Office.

Figure 3D shows that the BP3 measures provide an understanding of the range of CAV's outputs, but not their effectiveness or efficiency:

- Quantity targets relating to enquiries received are outside of CAV's control.
- CAV's customer satisfaction quality measure is taken from an annual customer satisfaction survey for all of CAV's activities, and for 2013–14 only included 20 domestic building consumers which is not adequate to provide statistical representation.
- The timeliness measure does not measure the volume of services provided within a specific time frame, which means that it does not provide an understanding of the efficiency of service delivery.

BP3 measures do not provide sufficient information to give an understanding of CAV's performance overall, or in relation to domestic building consumer protection.

#### *CAV's annual report*

External reporting through the annual report does not provide sufficient detail nor report on appropriate measures to provide a sound understanding of CAV's performance in relation to the achievement of its objectives. In particular, CAV's 2013–14 annual report consists of a few pages of activity-related status updates and output-based reporting, for example:

- 'in 2013–14, we finalised 9 395 disputes through our Front Line Resolution service'—this is the entire FLR service, not limited to domestic building
- 'Building Advice and Conciliation Victoria also helps consumers and builders work together to solve disputes'.

These statements do not provide the information necessary to determine the effectiveness of CAV's activities or provide a context for consumer protection activity in domestic building.

### 3.7 Advice to government

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CAV has effectively carried out a core function of its role by providing robust advice to government in relation to consumer protection.

Since 2007, CAV has briefed government regularly on specific issues in consumer protection including:

- industry views and opposition to proposed schemes for domestic building dispute resolution
- consumer protection issues and the case for a dedicated consumer advocacy body
- model contracts and bias in industry body generated standard contracts
- the need to review the DBCA
- the inadequacy of domestic building insurance coverage
- proposals to implement the *Victorian Domestic Building Consumer Protection Reform Strategy*.

In 2007 advice to government, CAV stated the DBCA 'has not delivered contracts which fairly balance the rights of consumer and builders and accord with government policy as reflected in the DBCA'.

In 2009, CAV's proposal to amend the DBCA to address these issues, including introducing mandatory conciliation and rectification orders, was approved by government, but did not proceed. In addition, in 2010, CAV advised the Minister for Consumer Affairs to implement the proposal despite opposition from the Housing Industry Association and the Master Builders Association of Victoria.

In 2010, CAV provided advice to the Minister for Consumer Affairs that 'consumers lack of knowledge and poor bargaining position leads to an inability to negotiate changes to terms of standard industry contracts, or to properly monitor their building project'.

In a 2014 incoming government brief, CAV advised that it proposed and supports 'introducing mandatory conciliation prior to lodgement of a dispute at VCAT, providing an opportunity to resolve disputes in a non-confrontation setting'.

CAV has provided advice to government and departmental heads about potential improvements to the consumer protection framework across a range of issues that indicate that CAV is aware of the consumer consequences of the legislative limitations it faces and the extent to which these limitations impede its effectiveness.

## 3.8 When conciliation fails

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### 3.8.1 VCAT

CAV encourages consumers to apply to VCAT where they are unsatisfied with a conciliation outcome or where a complaint is not likely to be resolved through CAV. This occurs both at the beginning and end of the conciliation process:

'We have been let down on so many levels; by the trades who carried out noncompliant work that damaged our house; by the builder who failed in his responsibilities to oversee and correct the work of his trades; by the surveyor who failed in his responsibilities to identify and bring works into compliance via enforcement; by the organisation that refuses to carry out its duties as an industry regulator; by the fact that is builders warranty insurance; by the VCAT system that is highly unaffordable and ineffective for consumers.'

The audit did not examine VCAT's role in resolving domestic building complaints. However, correspondence to the Auditor-General from domestic building consumers who did go to VCAT, and those who decided not to, indicates that seeking resolution through the VCAT domestic building list is costly, risky and not considered a realistic option for many consumers who are often already suffering financial stress due to building costs:

'We considered VCAT, but decided against it [...] in the building area it is very expensive and you have to spend a lot of money without any real chance of getting back the expenses, aside from the money to rectify all the defects to the house [...] The VCAT system is not a solution.'

'After I obtained my first expert report, and had my first meeting with a lawyer, I was able to establish that to go to VCAT would cost me in the vicinity of \$50 000 plus, which I am afraid I didn't have at the time. All my savings were tied up in the extension and renovation and I had to maintain another house, as I could not return to mine until after the builder finished.'

## Recommendations

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4. That Consumer Affairs Victoria reviews its dispute resolution and conciliation activities and advises government on options to improve their effectiveness, so that they are:
    - easy to access
    - low cost, simple and timely
    - objective and outcome focused
    - supported by necessary powers to compel participation in conciliation and enforce compliance with negotiated outcomes
    - underpinned by relevant and appropriate performance measures and effective monitoring, reporting and evaluation to demonstrate effectiveness.
  5. That Consumer Affairs Victoria and the Victorian Building Authority review their consumer education and awareness activities to ensure consumers have access to straightforward and timely information and advice aimed at enabling consumers and builders to:
    - understand their rights and obligations under building contracts
    - understand the consumer protection framework and access required information to make informed decisions
    - be aware of the services available to assist with addressing consumer issues, and their limitations.
-

# 4 Domestic building insurance

## At a glance

### Background

Domestic building insurance (DBI) is mandatory for domestic building works over \$16 000. DBI is 'last resort' protection for the consumer because it only protects them when a builder fails to complete works to a satisfactory standard and the builder dies, disappears or becomes insolvent. The withdrawal of private insurers from the DBI market during 2009 and 2010 prompted government to direct the Victorian Managed Insurance Authority (VMIA) to provide DBI from the end of March 2010.

### Conclusion

DBI provides only limited protection for consumers, is significantly more costly for builders and consumers than it needs to be and is widely misunderstood. Government intervention in 2010 was effective in addressing risks associated with the withdrawal of insurers from the market, but did not improve the level of protection for consumers and added to the costs of providing the insurance.

### Findings

- There was no comprehensive implementation plan in place before the government intervened in the DBI market in 2010, despite the apparent risks.
- This led to a higher cost DBI delivery model being put in place that remains nearly five years later due to ongoing uncertainty about VMIA's future role in DBI.
- Consumers have ultimately borne the additional costs of this model, estimated at around \$21 million between July 2011 and July 2015, for little, if any, tangible benefit.
- VMIA generally manages DBI effectively but should gain greater assurance on their agent's performance.

### Recommendations

- That the Department of Treasury and Finance works with VMIA to review the adequacy and cost of the current DBI scheme and provide advice to government on options to lower premiums and/or enhance coverage for consumers.
- That VMIA obtains certainty about its ongoing role in DBI provision and implements the most efficient delivery model.
- That VMIA alters the DBI policy certificate to show the base premium amount.

## 4.1 Introduction

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Domestic building insurance (DBI) forms part of the domestic building consumer protection framework. The *Building Act 1993* (the Act) requires building practitioners to have DBI cover when undertaking domestic building works costing over \$16 000.

DBI is a 'last resort' consumer protection because it is only available when a builder fails to complete works to a satisfactory standard and has died, disappeared or become insolvent within six years of completion. DBI covers homeowners for:

- structural defects, for up to six years, and non-structural defects, for up to two years, from the time the home or renovation is completed
- non-completion of building work—this cover may be limited to 20 per cent of the original contract amount
- a maximum claim payment of \$300 000—this was \$200 000 up until July 2014.

DBI schemes and coverage levels in other jurisdictions vary but are almost all 'last resort' in nature. Only Queensland has a 'first resort' scheme where consumers can also make a claim if a builder fails to rectify defects identified in a rectification order from the building regulator.

In Victoria, between the commencement of the DBI scheme in 2002 and 30 June 2014, 5 598 DBI claims were lodged in relation to registered builders and 3 943 of these claims were accepted. The estimated cost of payments to claimants for claims on registered builders in this period was \$153.1 million. The average claim cost was around \$33 000, with by far the most common trigger for claims being insolvency.

In 2014, the number of DBI policies issued rose to over 60 000 with an average premium cost of around \$987. The average premium for DBI reached its lowest point in 2008 and has risen since as most private sector insurers withdrew from the market in 2009 and 2010. Since 2010, the average DBI premium for works undertaken by a registered builder has increased by around 55 per cent. Consumers often pay more than the premium, due to additional charges by brokers and builders.

The government directed the Victorian Managed Insurance Authority (VMIA) to provide DBI from the end of March 2010 following the withdrawal of private insurers from the DBI market. VMIA issues around 95 per cent of cover and is the only insurer of registered builders. The only private insurer offers DBI solely to owner-builders.

## 4.2 Conclusion

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DBI provides only limited protection for consumers, is significantly more costly for builders and consumers than it needs to be, and is widely misunderstood.

Government intervention in 2010 to direct VMIA to provide DBI addressed the risks to the building industry and economy associated with the withdrawal of insurers from the market, but did not improve the level of protection for consumers and added to the costs of providing the insurance.



The model for delivering DBI adopted by VMIA in 2010 was driven by the very short time frame available to implement government's direction. VMIA had to appoint an agent to undertake almost all activities except claims management. While this largely mitigated the risk of implementation failure, it maintained a broker driven delivery model and added further to the cost of DBI for builders and consumers.

VMIA has maintained this higher cost model for almost five years due to ongoing uncertainty about its future role in DBI. While VMIA's actions have been reasonable in the circumstances and it has progressively reduced the commission paid to its agent, this delivery model will have cost consumers an estimated additional \$21 million between July 2011 and July 2015 and needs to be addressed.

VMIA needs certainty on its future role in DBI to enable delivery costs to be effectively addressed. An alternative delivery model would enable consumers to benefit from lower premiums and/or better coverage. The Department of Treasury and Finance (DTF) and VMIA need to provide comprehensive advice to government on opportunities to improve the cost efficiency and consumer protection offered by DBI, or any replacement scheme.

## 4.3 Government intervention in the DBI market

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The government decision in March 2010 to intervene in the DBI market addressed a risk that consumers would be left without insurance coverage. However, this decision was not informed by timely or sufficiently comprehensive advice and announcement of the intervention without an implementation plan in place carried significant risks.

DTF had monitored the withdrawal of insurers from the DBI market during 2009 and was aware from November 2009 that the largest insurer would withdraw from July 2010. A better outcome could have been achieved if advice to government and a decision on the preferred intervention approach had been made earlier.

VMIA could not implement the government direction that it provides DBI from the end of March 2010. It did not have the necessary staff, processes and systems in place and it was concerned about its legal capacity to issue DBI policies in its own name. VMIA relied on cooperation from existing DBI insurers and had to appoint an existing insurer as its agent to ensure ongoing availability of DBI cover.

### 4.3.1 Managing risks in the DBI market

DTF has monitored the DBI market since the late 1990's due to a history of private insurers entering and leaving the market and the risks this created for the availability of what is mandatory insurance. In September 2008, DTF advised the Minister for Finance that there were seven insurers in the DBI market and while it considered the risk of insurers leaving the DBI market as low in the short term, it would be problematic if a major insurer left.

The Essential Services Commission (ESC) reported to government in March 2009 on the performance of Victoria's DBI scheme. The ESC found that DBI insurers had made reasonable profits by industry standards between 2005 and 2008, but the future profitability of the scheme was expected to decline due to increasing claims and the impact of a slowing economy on builder insolvency rates.

Subsequent ESC reports on the DBI scheme indicated that premium discounting between 2006 and 2009 coincided with an increase in claims, resulting in declining DBI profitability. This led to the exit of private insurers from the DBI market. In June 2009, there were five insurers operating in the Victorian DBI market. Two of these insurers, with an estimated combined market share of around 25 per cent, withdrew from the market during July 2009.

DTF advised government of the withdrawal of these insurers in August 2009 and indicated that while the three remaining insurers were willing to take on new builders, they were likely to tighten their eligibility criteria for DBI given the ongoing downturn in financial markets and economic conditions.

The government agreed to the further development of a contingency plan to support the existing market, including proposals to enhance consumer protection. DTF developed a contingency plan during the second half of 2009 and early 2010 in consultation with other relevant government departments and agencies, including VMIA.

The plan examined five options ranging from the introduction of a voluntary insurance model to a model under which government would underwrite and provide the insurance using agents, and manage claims internally. DTF preferred to maintain the 'last resort' nature of DBI and favoured options that minimised avoidable government involvement in the market given the risks associated with DBI.

In early November 2009, the NSW government announced that it was taking over the NSW DBI market from July 2010. DTF was concerned that NSW's decision would prompt remaining insurers to view the Victorian DBI market as commercially unviable and withdraw from it.

In November 2009, VMIA asked DTF to confirm there were no legislative barriers to prevent or impair VMIA's entry into the DBI market. DTF responded that its legal advice was that a Ministerial direction under the *Victorian Managed Insurance Authority Act 1996* (the VMIA Act) could be used for VMIA to be either the insurer of 'last resort', or the monopoly insurer with no need for immediate legislative change.

At the same time, VMIA advised DTF that it would not be capable of responding to a direction from government to provide DBI from either December 2009 or January 2010, and that any government announcement needed to allow sufficient time for this capability to be established.

DTF advised the Minister for Finance in late November 2009 that:

- the largest insurer in the DBI market would be withdrawing from July 2010
- a government monopoly insurer model could be implemented in the short term without any legislative change, but DTF favoured a staged intervention approach
- VMIA had advised that it would need several months to establish the necessary infrastructure to step into the DBI market and would need to rely on cooperation and assistance from private insurers for both personnel and systems
- the continued use of brokers to deliver DBI was an option under a statutory monopoly, but this was arguably unnecessary if there was only one provider in the market.

However, DTF did not provide advice to government on options to ensure the continued availability of DBI until March 2010. This was despite risks to market stability posed by the largest insurer's announced withdrawal, and the significant operational and potential legal issues involved in ensuring a timely and effective response.

### 4.3.2 Informing the government decision to intervene

In early February 2010, the largest insurer in the Victorian DBI market formally advised the government that it was withdrawing from the market and would cease providing DBI from 1 July 2010. This announcement meant there would be only two insurers left in the DBI market.

The government received advice on this development in March 2010 from:

- the Ministers for Finance and Planning who recommended that the government intervene to take over the DBI market from 1 July 2010
- DTF and the Department of Premier and Cabinet that did not support the intervention recommended by the ministers. Instead, both departments recommended a staged intervention model where the state would monitor DBI availability and pricing and consider intervening as an insurer of 'last resort' on a temporary basis if builders could not obtain insurance.

The advice to government from ministers and the departments was focused on addressing an immediate and pressing risk that builders would be unable to access mandatory DBI and therefore would not be able to undertake domestic building work. It outlined the events prompting the need to consider action, the available response options and some associated issues and risks.

The ministers recommended that the government direct VMIA to act as a statutory monopoly provider for DBI on the grounds that this model had the best chance of providing ongoing stability to the DBI market. The recommended model assumed that brokers would be retained and would deal with VMIA as the sole insurer.

The main reasons the departments opposed a statutory monopoly model were that:

- there was limited evidence of builders being unable to access DBI
- a statutory monopoly model would remove any scope for competition in the market place and would risk becoming less efficient and innovative
- the government would have difficulty exiting the market in the future
- the government may be exposed to legal action from remaining market participants seeking compensation for loss of business
- the risks involved in providing DBI meant the highest risk builders would be concentrated on VMIA's, and therefore the state's, balance sheet
- the state may be subject to criticism if VMIA ruled some builders as not eligible for insurance as a result of applying the same standards as commercial insurers
- there would be potential pressure on government to expand the scope of DBI, resulting in increased risk and costs.

The departments advised that the two insurers remaining in the DBI market had both indicated a willingness to continue to participate but may seek to leverage the situation to gain further support from the state. At the time, the government had a commitment to cover private insurers for losses above \$10 million from claims relating to individual builders.

The two departments recommended a staged intervention model on the grounds that this would provide an opportunity for new insurers to enter the market and enable government to monitor the market while reserving the option to take it over.

The government considered the advice and on 22 March 2010 decided that it would intervene to take over the DBI market and implement the statutory monopoly model.



The advice relied on by government when making this decision was not sufficiently comprehensive. The advice did not adequately highlight the legal, operational and timing issues, and risks associated with the options under consideration. Specifically, the advice did not:

- comprehensively address legal issues with VMIA's ability to provide DBI
- adequately reflect advice from VMIA that it would need several months to establish the capability to deliver DBI, and would need to rely on the cooperation and assistance of private insurers for both personnel and systems
- propose a strategy to mitigate the risk that remaining DBI insurers would withdraw at short notice following announcement of government intervention or make unreasonable demands to secure their continued participation in DBI
- comprehensively cost intervention options and models because all models and options presented assumed the ongoing use of brokers and did not include payments to an agent required by VMIA to facilitate delivery of the product.

### 4.3.3 VMIA's establishment of DBI arrangements

There was no comprehensive implementation plan in place before the government announced its intervention in the DBI market.

The Minister for Finance's announcement on 29 March 2010 indicated that the government would introduce a statutory monopoly for DBI provision, and that VMIA would provide DBI on a commercial basis from the end of March 2010 and work with private insurers to ensure their orderly exit from the market.

On 30 March 2010, the Minister for Finance used powers under the VMIA Act to direct VMIA to provide DBI from 31 March 2010—the next day. However, VMIA was not able to provide DBI from that date because it:

- was not a 'designated insurer' under the Act
- had not been given sufficient time to put in place the necessary resources, systems and processes to deliver DBI.

The VMIA Act requires the Minister to consult with VMIA before issuing a direction. VMIA advised that there was very limited consultation with it immediately before this direction. Adequate consultation with VMIA could have identified the legal and operational issues constraining its capacity to implement the government decision, before it was announced, and enabled a more strategic response to these issues and a smoother, less costly transition.

Because these issues were not adequately addressed before the government announcement, VMIA had no option but to make arrangements with an existing insurer to ensure the continued availability of DBI.

#### Initial contact with remaining domestic building insurance insurers

VMIA's inability to immediately step in and take over the DBI market meant the state's intervention approach carried a significant risk if the two remaining insurers decided to withdraw from the market at short notice.

This risk was mitigated by a history of DBI insurers providing reasonable notice of withdrawal and cooperating to facilitate the transition of clients to other insurers. However, the government decision was effectively closing the market and this could have precipitated a less cooperative approach from insurers.

The two remaining DBI insurers wrote to the government on 31 March 2010 advising that they were reconsidering their immediate and ongoing provision of DBI in Victoria, with one indicating that it would suspend DBI operations from 7 April 2010. Both insurers made it clear they knew that VMIA could not immediately step in and take over the entire DBI market.

The insurers offered to continue providing DBI if the government would underwrite all new DBI policies and pay them a commission on premiums of between 44 and 65 per cent. In effect, the insurers were proposing to transfer the risks associated with all new DBI policies to the state for a significant fee that would ultimately be passed on to DBI consumers or taxpayers.

This placed the state in a difficult position because VMIA was not operationally ready to immediately take over the market and had also identified a legal issue with its capacity to offer DBI.

### Legal issues with VMIA providing DBI

In November 2009, DTF advised VMIA that there were no legislative barriers to its entry into the DBI market and that a Ministerial direction could be used in the short term for VMIA to be either the insurer of 'last resort' or the statutory monopoly insurer.

VMIA obtained legal advice on implementing the Ministerial direction on 6 April 2010. This advice confirmed that while the direction gave VMIA authority to provide DBI, VMIA was not a designated insurer under the Act and that any builder relying on DBI provided by VMIA may be committing an offence under that Act. VMIA raised this issue with DTF on the day it received the advice and action was initiated immediately to amend the Act to identify VMIA as a designated insurer.

Advice to government on the proposed amendment indicated that VMIA was entering into a commercial arrangement with one of the existing private designated insurers as a temporary measure to remove the risk of legal challenge to its ability to provide DBI and that this would add considerably to DBI's cost. The government approved the amendment and legislation was passed through Parliament in mid-2010.

VMIA decided that it would not issue DBI policies in its own name until it was confirmed as a designated insurer under the Act. To cover the intervening period, VMIA reached agreement with the major remaining DBI insurer which involved reinsuring the liability for DBI policies issued by that insurer from 31 May 2010 until VMIA was confirmed as a designated insurer in mid-July 2010.



### Appointment of existing DBI insurer as VMIA's agent

VMIA's ability to negotiate a commercial arrangement with an existing insurer to implement the government decision was made more difficult because it was seeking to do so after the decision had been publicly announced and there were few insurers remaining in the DBI market:

- The first and largest insurer in the market would not negotiate given it had previously announced its intention to withdraw from the market.
- The second and smallest insurer in the market sought a commission of 65 per cent of DBI premiums and a further \$340 000 for services to be provided to VMIA.
- The third insurer sought a commission in the range of 44 to 48 per cent of premiums on the basis that it would pay broker commissions and meet its own operational costs from this commission.

VMIA obtained commercial advice that a commission between 35 and 40 per cent was reasonable and that anything above 50 per cent would be excessive. VMIA announced the appointment of the third insurer as its agent for DBI delivery on 13 May 2010.

The commencement date for the relationship with the agent was 7 May 2010. Under the agreement, the insurer offered DBI in its own name and at its own risk until 30 May 2010, and in its own name but totally underwritten by VMIA, between 31 May 2010 and 16 July 2010. From 17 July 2010 onwards, the insurer acted as VMIA's agent and issued DBI policies in VMIA's name.

The agent manages almost all aspects of DBI provision on VMIA's behalf, including managing the interface with brokers, assessing DBI applications against underwriting criteria and maintaining a system to record details of all DBI policies issued. VMIA directly manages claims and decisions to decline DBI cover.

The initial commission paid to the agent on DBI premiums collected in 2010–11 was 45 per cent. VMIA advised that this was towards the upper end of what was commercially reasonable at the time but reflected what was thought to be the short-term nature of the arrangement. VMIA subsequently negotiated lower commission rates and succeeded in making part of the agent's commission dependent on meeting agreed key performance indicators from July 2013.

The commission paid to the agent has declined since the establishment of the arrangement in mid-2010 as follows:

- 45 per cent from 31 May 2010 to 31 October 2010
- 42.5 per cent from 1 November 2010 until 30 June 2011
- 38 per cent from 1 July 2011 to 30 June 2013
- a maximum of 32.5 per cent from 1 July 2013, comprising base commission of 22.5 per cent with access to up to a further 10 per cent if all key performance indicators are met.

Payments to the agent between mid-2010 and 31 December 2014 totalled over \$80 million, including GST. Assuming a broker commission rate of 15 per cent of premiums collected, the agent paid broker commissions of around \$30 million from this amount.

VMIA achieved a reasonable outcome in difficult circumstances. By appointing an agent to provide DBI, VMIA accessed the agent's established systems and processes and largely mitigated the risk of failing to implement the government direction. However, VMIA was required to provide DBI on a break-even basis and the need to introduce another intermediary added to the costs to DBI consumers. These costs could have been at least partly avoided with earlier and more comprehensive advice, and a more strategic approach to the government's intervention.

In June 2010, DTF provided evidence to the Legislative Council's Standing Committee on Finance and Public Administration's *Inquiry into Builders Warranty Insurance* that the arrangements established for DBI had been designed to ensure that it would be available at 'the least cost that it should be available for'. This advice to the committee appears to have been inconsistent with DTF's knowledge at the time that VMIA's use of an agent would add to the costs of DBI.

## 4.4 DBI delivery model and costs

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Consumers ultimately pay for DBI, as the premium and any related costs are passed on by builders. The amount consumers pay partly depends on how many intermediaries are involved in the delivery model.

The DBI delivery model established by VMIA in mid-2010 retained brokers and added to delivery costs because the agent was an additional intermediary. While this model was intended to be temporary, it has been retained for nearly five years as government has considered reforms to the framework for domestic building consumer protection.

We estimate that this DBI delivery model will have cost an additional \$21 million between July 2011 and July 2015 compared to a model where VMIA might insource DBI delivery and dispense with brokers and an agent. These costs have been passed on to consumers through higher DBI premiums for little, if any, tangible benefit. An alternative lower cost DBI delivery model, such as VMIA directly providing DBI without brokers or agents, could have delivered the same benefits to builders and consumers, including improved stability and claim handling times.

Appointment of the agent was largely unavoidable. However, the need to retain brokers beyond an initial transition period was questionable because DBI is a mandatory product with standard cover and there was to be only one provider of insurance. In a typical competitive insurance market with a variety of insurers and products on offer brokers have a role acting for their clients by providing advice and sourcing lower cost, or better cover.



This audit has established that the two largest DBI brokers are associated with the two major building industry associations, the Master Builders Association of Victoria and the Housing Industry Association. The Legislative Council's Standing Committee on Finance and Public Administration's October 2010 report on its *Inquiry into Builders Warranty Insurance* recommended that government and VMIA review the role of insurance brokers under Victoria's new DBI arrangements. The government did not formally respond to the committee's recommendations. In early 2011, around 50 per cent of brokerage commissions were being paid to these two entities.

The cost of DBI to consumers can also include fees imposed by brokers and/or builders over and above the premium charged by VMIA. These fees are not transparently disclosed to consumers or subject to scrutiny by VMIA or the ESC.

VMIA has provided advice to DTF and the Minister for Finance on a number of occasions since late 2010 on the additional costs of the DBI delivery model and the capacity to eliminate commissions by eliminating brokers and the agent. However, the interim model has been retained due to ongoing uncertainty about VMIA's future role in providing DBI.

This uncertainty has constrained VMIA from investing in the internal capability needed to deliver DBI without an agent and/or brokers. While this was understandable, it is a lost opportunity to generate savings and pass the benefits on to consumers in the form of lower premiums and/or enhanced cover.

DTF advised that changes in government and the consequent changes in policy direction have meant that reform efforts have prioritised redesign of the domestic building consumer protection framework ahead of making arrangements for the delivery of DBI more efficient and cost effective.

DTF advised that it and VMIA are currently examining ways to reduce the costs of DBI. However, VMIA requires certainty about its continued involvement in the provision of DBI to enable it to more cost-effectively deliver DBI.

#### 4.4.1 Analysis and advice on the DBI delivery model

VMIA advised its board in October 2010 that the interim DBI delivery model involved high distribution costs and was significantly more expensive than if VMIA eliminated agents and brokers and dealt directly with builders. VMIA's modelling showed the total cost of maintaining the interim arrangement for 2011–12 was around \$11 million higher than a model with no agent or brokers.

The board was advised that the optimal pricing and distribution model for DBI involved a single agency dealing direct with builders to eliminate or substantially reduce commissions and loadings. VMIA identified that this model would deliver improved outcomes for consumers through lower premiums and/or increased access to cover.

VMIA advised DTF in December 2010 that one of the risks of delaying the statutory monopoly for DBI provision was that commission and transaction costs paid by consumers and builders, which could be reduced or eliminated under a statutory monopoly, would continue to be incurred.

The optimum DBI delivery model identified by VMIA was not implemented as there was a change in government in late 2010 and a decision was made by the new government not to implement the statutory monopoly model while broader reforms to the domestic building consumer protection framework were considered.

DTF advice to the Minister for Finance in March 2011 on deferral of the statutory monopoly model and VMIA's decision to increase DBI premiums from 1 July 2011 did not provide information on the additional costs associated with the interim arrangement for DBI delivery, or the relative costs of alternative DBI delivery models.

### Advice on DBI delivery costs in 2012

In March 2012 the Minister for Finance requested advice on options that could reduce DBI agent fees within the current model but not undermine the broader reform possibilities under consideration at the time.

DTF advised that given ongoing consideration of reforms, temporarily retaining current arrangements with VMIA using a single agent but seeking to negotiate a lower commission when rolling over the agreement with the agent was the best option. DTF preferred this approach due to the uncertainty, complexity, cost and risks of alternative options and because it had no financial impact on the state and was unlikely to draw criticism from building industry associations.

The DTF advice indicated that a DBI delivery model where VMIA offered DBI direct to builders, with no agent or broker involvement would:

- remove the 38 per cent commission currently paid and streamline DBI oversight
- involve once-off start-up costs of around \$4.6 million and an increase in VMIA's ongoing annual costs estimated at \$8.8 million
- translate into a decrease of 17 per cent for the average premium, based on the net savings under this model and recouping the start-up costs over two years.

DTF also advised the minister that in addition to the DBI premium, the cost of insurance for consumers is inflated by additional costs, such as extra fees charged by brokers direct to builders to arrange coverage, plus builders' own insurance surcharges—often around 10 per cent. DTF advised that these charges can inflate a DBI premium of \$850 into an end cost to the consumer of around \$1 200.

These additional fees imposed by brokers and/or builders are not subject to scrutiny by VMIA or the ESC and are not transparently disclosed to consumers. The ESC monitors the DBI market and reviews the validity of VMIA's premiums but its work does not extend to providing information on the full costs of DBI to builders and consumers. No agency monitors the total costs of the insurance scheme.

### Advice on DBI delivery costs in 2013

In February 2013, VMIA again highlighted the potential to significantly reduce the costs of the DBI scheme by removing agents and brokers, in advice provided to DTF and the Minister for Finance. After considering this issue, VMIA opted to retain the existing DBI delivery model given the ongoing uncertainty around proposed reforms.

In May 2013, the ESC raised VMIA's pricing of DBI with the Minister for Finance. The ESC noted that while VMIA's arrangement with the agent was reasonable in the circumstances, there was scope for savings under other delivery models.

In May 2013, the government released the *Domestic Building Consumer Protection Reform Strategy* which committed to broadening the triggers for accessing DBI beyond the existing narrow triggers and which stated that the insurance would continue to be provided by an open market, with VMIA remaining in the market to avoid supply problems.

In June 2013, DTF responded to a request from the Minister for Finance for advice on the advantages and disadvantages of terminating the agency arrangement for DBI delivery and having VMIA bring DBI operations in-house. DTF's advice clearly acknowledged that eliminating intermediaries would significantly reduce the costs of DBI and provide VMIA with more control over its delivery. Despite this, DTF recommended that the status quo be maintained until 1 July 2015 to provide sufficient time for VMIA to implement the new DBI arrangements outlined in the government's reform strategy. While this advice was appropriate in the circumstances, it meant retention of the higher-cost delivery model.

In July and September 2013, DTF provided advice to government on a proposal to replace the DBI scheme component of the previously announced reform strategy with a domestic building consumer protection fund to be administered by the Victorian Building Authority (VBA). DTF's advice indicated that an advantage of this proposal was that it would avoid the broker and agent costs under the current scheme.

In April 2014, the government announced the new approach to DBI delivery. This involved introducing a domestic building consumer protection fund to be managed by VBA. This fund was to replace DBI which was to be phased out by 30 June 2015. This reform was not progressed in 2014.

#### 4.4.2 Possible savings under different delivery models

VMIA could have delivered DBI for less than the costs incurred under the delivery model established in 2010.

In October 2010, VMIA estimated that the total cost of the interim DBI delivery model in 2011–12 was likely to be around \$11 million higher than a model with no agents or brokers, based on premium income of \$40 million. However, this estimate did not include an allowance for the significant start-up costs that would have been incurred for VMIA to deliver DBI totally in-house.

Figure 4A shows the estimated costs for the two DBI delivery models between 1 July 2011 and 30 June 2015. The first is the current model, involving brokers and an agent assisting VMIA. The second model does not involve any intermediaries and assumes VMIA deals directly with builders. This was identified as the optimum delivery model by VMIA in late 2010.

**Figure 4A**  
**DBI delivery costs and potential savings (\$ millions)**

Distribution model	2011–12	2012–13	2013–14	2014–15	Total
<b>Current model</b>					
Payments to intermediaries	16.3	17.4	16.7	19.6	70.0
VMIA expenses	2.0	2.0	3.1	3.5	10.6
<b>Delivery costs (before claims)</b>	<b>18.3</b>	<b>19.4</b>	<b>19.8</b>	<b>23.1</b>	<b>80.6</b>
<b>Model without intermediaries</b>					
Payments to intermediaries	–	–	–	–	–
VMIA start-up costs	13.2	N/A	N/A	N/A	13.2
VMIA annual operating costs	11.0	11.3	11.6	11.9	45.8
<b>Delivery costs (before claims)</b>	<b>24.2</b>	<b>11.3</b>	<b>11.6</b>	<b>11.9</b>	<b>59.0</b>
<b>Savings with no intermediaries</b>	<b>–5.9</b>	<b>8.1</b>	<b>8.2</b>	<b>11.2</b>	<b>21.6</b>

Source: Victorian Auditor-General's Office based on information from VMIA.

Implementation of the lower cost model from 1 July 2011 would have resulted in an estimated saving of around \$21 million to 30 June 2015. The savings foregone by not adopting a lower cost delivery model could have benefited consumers through lower DBI premiums or enhanced cover. The current DBI delivery model will be in place until at least the end of 2015.

## 4.5 VMIA's management of DBI

VMIA is managing its responsibilities for providing DBI robustly. It has:

- established adequate DBI governance, management and staffing arrangements
- recognised DBI in strategic planning and priority setting for the organisation
- put in place management information and performance measurement systems
- successfully reduced the commission payable to its agent and linked part of this commission to performance
- significantly reduced the average time taken to manage DBI claims to completion
- communicated with stakeholders—including DTF, the ESC, Consumer Affairs Victoria, VBA and the Building Practitioners Board.

While VMIA's processes for the day-to-day management of the DBI agency arrangement are robust, it could improve the indicators used to measure the agent's performance and could improve the level of assurance obtained on the adequacy of the agent's systems and performance.

### 4.5.1 Implementation actions

The government direction in March 2010 put VMIA in a position where it had to maintain DBI cover for more than 15 000 builders who had been assessed and accepted by private insurers, as well as assessing new applications for DBI cover.

VMIA moved to establish the governance, management and staffing arrangements required to implement the government decision. It:

- assigned responsibility for implementation to senior officers
- established a steering committee including representatives from DTF
- obtained legal, actuarial and other relevant advice to inform its actions
- negotiated an agreement with an existing DBI insurer to quickly access established systems and processes
- obtained communications advice and developed a stakeholder engagement plan
- communicated with stakeholders including insurers, industry bodies and brokers and developed a website to provide information to builders and consumers
- engaged or reassigned staff to deliver DBI
- investigated and established appropriate ICT systems and capability.

The government provided VMIA with start-up funding of \$3.6 million and a capital contribution of \$13.9 million to support its implementation of the direction to provide DBI. This funding contribution was set out in an agreement between DTF and VMIA in mid-2011. The start-up funding was fully repaid by the end of 2013. The capital contribution is only repayable if VMIA's DBI arrangements are wound up.

#### Initial assessment of builders

A builder cannot be registered as a building practitioner under the Act without showing proof of eligibility for insurance. The insurer typically sets a turnover limit when granting eligibility for insurance which limits how much a builder can trade.

The government direction presented a range of challenges because VMIA needed to obtain the relevant information and records of all builders eligible for DBI cover at the time of the direction and was exposed to risks for those builders it had not assessed.

Of the initial 15 000 builders, VMIA's agent had around 4 480 active builders on its DBI policy book at the end of May 2010. Records relating to the remaining builders were transferred from other insurers to the agent during 2010.

Recognising these issues, VMIA initiated:

- integrity checks on data transferred from private insurers on builders—this identified inaccuracies in records for around 10 per cent of builders
- a financial and solvency assessment on all builders
- an actuarial review of the DBI market to assess risk and premium adequacy
- a program of builder underwriting reviews by its agent to ensure that builders were accurately risk rated and classified for premium purposes.

### Assessment of premium adequacy

When VMIA entered the DBI market in mid-2010 the average premium was around \$636. Average DBI premiums have risen since the withdrawal of most private sector insurers in 2009. The average premium for a registered builder has increased by around 55 per cent since 2010.

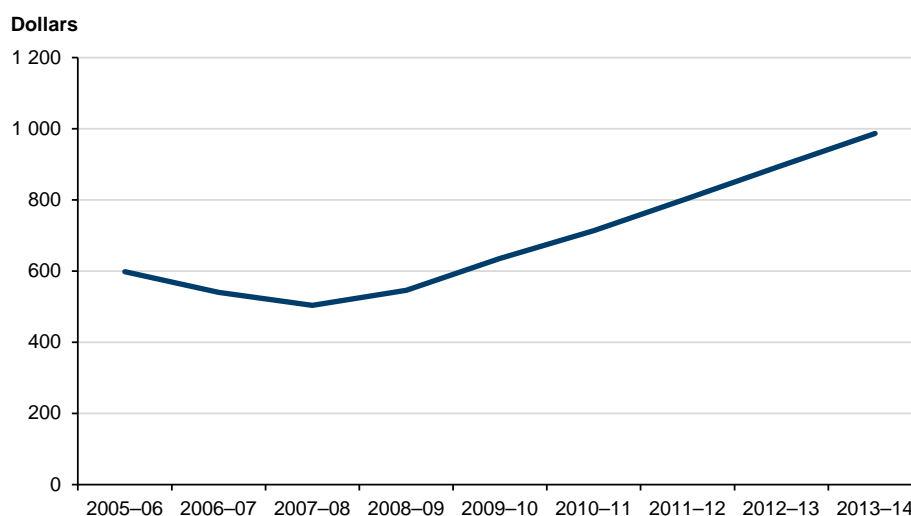
The most recent ESC report on the performance of DBI indicates that average premiums reached their lowest point in 2008 due to strong competition between insurers. The ESC noted that a lack of information about DBI claim costs could have driven premiums below cost-reflective levels at that time.

VMIA initially adopted the premium rates used by its agent and was instructed to keep premiums fixed for 12 months from June 2010. It was also directed to provide DBI on a break-even basis and has regularly assessed the adequacy of premiums to meet the long-term costs of the scheme.

VMIA's initial actuarial advice in 2010 indicated that the DBI scheme was 15 to 20 per cent underpriced, meaning premiums were lower than required to meet expected future claims costs. This work also identified a practice where some high-volume builders were only paying around 50 per cent of the applicable premium under discount arrangements with insurers. VMIA addressed the inequities in premium levels in 2011 by eliminating premium discounts.

VMIA increased DBI premiums in July 2011 and July 2013 to match the costs of providing DBI, including the emerging and expected future DBI claims costs identified by actuarial assessments. Figure 4B shows average premiums for registered builders from 2005–06 to 2013–14. Higher than necessary DBI distribution costs have contributed to, but are not the predominant cause of, increased premiums since 2010.

**Figure 4B**  
**Average DBI premiums for registered builders**



Source: Victorian Auditor-General's Office based on information from the ESC.

The Minister for Finance instructed the ESC to review the adequacy and validity of VMIA's DBI premiums every two years. The initial review was finalised in May 2013 and found that VMIA's premiums were sufficient for it to break even on DBI business and were not excessive.

The most recent ESC review of VMIA's DBI premiums was released in April 2015 and concluded that the average premiums for 2012–13 and 2013–14 and VMIA's approach to DBI underwriting were reasonable. The review also concluded that VMIA's decision to increase the capital charge applied to the 2013–14 premiums means that capital to support the DBI portfolio will be collected faster than it was previously. This was prudent given the uncertainty surrounding the duration for which VMIA would be underwriting DBI and the 'long-tail' nature of the product—where the full cost of claims is not known for several years after the policy is issued.

### Consideration of alternative delivery models

VMIA's mandate from government in 2010 was to implement a statutory monopoly for DBI. This changed in early 2011 under a new government which decided not to close the DBI market while broader consumer protection reforms were considered.

Recognising the high cost of the operating arrangement established in 2010, VMIA has periodically examined a range of different delivery models. This analysis has identified that other delivery models would have benefits including lower operating costs. However, VMIA has determined not to implement an alternative model given the ongoing uncertainty about its ongoing role in the DBI market.

## 4.5.2 Management of DBI agent

VMIA negotiated an agreement with an existing DBI insurer in mid-2010 to enable it to implement the government direction to provide DBI.

The agent manages almost all aspects of the provision of DBI on VMIA's behalf including the interface with brokers, assessing applications for DBI against underwriting criteria and periodically reviewing the financial strength of builders. The agent maintains an IT system which records details of all DBI policies issued. The VMIA manages claims and decisions to decline DBI cover directly.

VMIA has been generally effective in managing the agent appointed to support delivery of its DBI responsibilities. It has established:

- access and reporting requirements and arrangements
- monitoring and review mechanisms and processes
- payment approval mechanisms.

Opportunities for improvement include broadening the indicators used to measure its agent's performance and improving the level of assurance obtained on the adequacy of its systems and performance.



## Agreements with DBI agent

VMIA's relationship with the agent commenced in May 2010 and it entered into an initial Heads of Agreement in June 2010. A more detailed service-level agreement was subsequently established to specify operational details including service response times and reporting and quality assurance requirements.

The initial agreements did not include any performance indicators to measure how effectively and efficiently the agent performed its obligations. As a result, its remuneration was not linked to its performance. The initial agreement expired on 30 June 2013. A new agreement was negotiated and commenced on 1 July 2013.

In negotiating the new agreement VMIA was successful in reducing the commission payable to the agent from 38 per cent to a maximum of 32.5 per cent per month. Under the new agreement the base commission was reduced to 22.5 per cent and the agent is entitled to additional commission of up to 10 per cent, depending on its performance against a set of indicators.

These performance indicators relate to the completeness and timeliness of the agents performance of its responsibilities and reporting on these to VMIA. The indicators could be improved by introducing some dealing with the quality of performance in key areas such as assessing the financial strength of applicants for DBI eligibility, given that insolvency is by far the most common trigger for DBI claims.

VMIA's decision not to invite tenders for the agent role in the lead up to the expiry of the initial agreement was reasonable given the uncertainty around the reform process.

## Adequacy of assurance obtained on agent performance

VMIA demonstrated active and robust engagement and oversight of the agent. Regular monitoring activity includes:

- weekly analysis of data sourced direct from the agent's DBI system on eligibilities, insurance certificates and policies and amendments
- examination of the results of reviews undertaken by the agent on the performance of brokers and the status of builders against the underwriting criteria
- weekly meetings with the agent to discuss performance and address issues arising from VMIA's review and analysis of the agent's data and other information.

This regular monitoring enables VMIA to maintain a strong position in directing the agent on delivery of its obligations under the agreement.

The agent is also required to provide an annual attestation that it has established and maintained adequate controls over the ICT and other systems used to discharge its obligations to VMIA. This attestation is required to be complemented by an audit on whether relevant controls have operated as intended. The agent's attestations and audits have consistently confirmed adequate controls.



VMIA agreed to allow the agent to use its internal auditors to undertake these annual audits. This was initially agreed because the agent had insufficient time to appoint an external auditor. The internal auditor provides a detailed schedule on controls addressed and work performed but does not provide an audit opinion.

VMIA could enhance the level of assurance gained on the agent's performance by seeking its agreement to appoint an external auditor to perform and provide an opinion on this work. VMIA could also exercise its other rights under the agreement to directly review the agent's performance.

### 4.5.3 Assessment of applications for DBI

VMIA's mandate is to provide DBI on commercial terms. It assesses applications from builders for DBI cover eligibility using underwriting criteria which examine the level of risk posed by the applicant in terms of future claims.

VMIA's underwriting activity has significant implications for builders because DBI is mandatory for building projects above the threshold and builders have to demonstrate eligibility for DBI when seeking registration with the Building Practitioners Board.

Inability to obtain DBI effectively means a builder cannot operate in Victoria if undertaking works valued over \$16 000. VMIA was the only insurer offering DBI to registered builders in Victoria from 1 January 2014.

In 2010 VMIA was directed to provide cover to all builders who held eligibility for DBI with existing insurers. This was done and VMIA progressively undertook financial and solvency assessments on builders transferred from other insurers. VMIA initially adopted the underwriting criteria used by its agent and has subsequently reviewed and changed the criteria in consultation with the agent. The agent undertakes underwriting assessments against the criteria and VMIA monitors how the criteria are applied.

The underwriting criteria are focused on financial strength and risk because the vast majority of DBI claims are triggered by builder insolvency. As part of the underwriting process builders are assigned risk ratings which impact on the premiums they pay. VMIA also assigns an annual turnover limit on builders which puts an upper limit on the value of contracts the builder can enter into, in order to limit VMIA's exposure to claims if a builder becomes insolvent.

VMIA may also impose security and/or indemnity conditions on builder DBI eligibilities. The percentage of builders with conditions attached fell from over 30 per cent prior to VMIA's involvement to around 6 per cent in the September 2010 quarter.

#### Declined applications

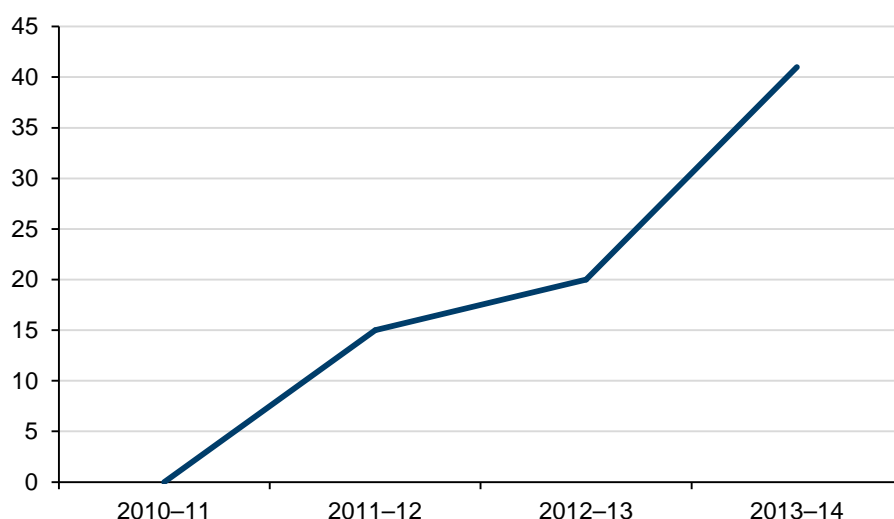
A decision by VMIA to decline eligibility for DBI to a builder has significant implications for the builder's capacity to be registered and trade. VMIA has established a robust process for declining access to DBI.

The Ministerial direction to VMIA in March 2010 provided for builders issued with an eligibility certificate in the previous 15 months to be provided with automatic cover by VMIA for at least 12 months. VMIA did not decline an application for DBI insurance until December 2011, around 19 months after it stepped into the DBI market.

While not declining an application for DBI in the 19-month period to December 2011, VMIA did withdraw cover from some builders with pre-existing eligibility for DBI coverage between 1 June 2011 and 30 November 2011 as a result of financial assessments of these builders.

Figure 4C shows the number of applications declined for the financial years 2010–11 to 2013–14. There was a steady increase in these numbers between 2010–11 and 2013–14.

**Figure 4C**  
**Declined applications, 2010–11 to 2013–14**



Source: Victorian Auditor-General's Office based on information from VMIA.

The most common reasons for VMIA declining a builder's eligibility for DBI are an adverse assessment of their financial position or the existence of an adverse corporate or disciplinary history.

There is no reliable data available on the number of applications declined prior to VMIA stepping into the DBI market in mid-2010. However, it was likely to have been lower than present given the capacity at that time of builders to approach a number of insurers to gain cover. Insurers did not share information on rejected applications for DBI and the ESC did not collect this information.

VMIA's internal auditor reviewed the design and operation of the processes in place around declining DBI applications in 2012–13 and found a strong control environment. We reviewed a sample of decisions where an application was declined and found that the process is consistently applied.

#### 4.5.4 Claims management

VMIA undertakes claims management directly and has established a process and supporting procedures to guide this activity. It has significantly reduced the average time taken to manage a claim through to completion compared to other insurers.

The claims management process involves establishing whether the builder has died, disappeared or become insolvent and, if so, assessing whether the claimed defects or non-completion meet the time limits and exist. Where a claim is accepted the insurer obtains quotes to inform the claim payment. For non-completion of building work, the cover may be limited to 20 per cent of the original contract amount and the maximum payment for all claims is \$300 000.

DBI is known as 'long-tail' insurance because the full cost of claims is not known for several years after the policy is issued. This is different to most consumer insurance products where the policy is renewed on an annual basis and the insurer will know its full claims liability with a high degree of certainty shortly after the anniversary date.

The long-tail nature of DBI cover means it is difficult to assess whether there have been changes in insurance claims history and management since VMIA's involvement from 2010. However, the available information suggests the following:

- The **timeliness of claims management** has improved since VMIA's involvement—the average time between receiving a notification and a claim being finalised across all insurers since the DBI scheme began in 2002 was 345 days at June 2014. This was a significant improvement since 2012 when the average claim handling time was 545 days. VMIA's timeliness is better than the average across all insurers, with an average claims handling time of 129 days for 2013–14.
- **Builder insolvency** continues to be by far the most significant reason for DBI claims—with this being the trigger for around 94 per cent of successful claims.
- While **DBI claims are relatively infrequent**, there are signs that the number of claims is increasing—5 598 claims in relation to registered builders have been lodged and 3 943, or around 70 per cent, of these have been accepted since the DBI scheme commenced in 2002.
- The most **common reasons for denying claims** are that the insurer does not accept that the reported fault is a defect or that the builder is insolvent.

There are opportunities to further improve the timeliness of claims handling and the level of consumer understanding of DBI claim triggers.

#### Claims data

The ESC has examined and publicly reported on the pricing and performance of DBI since 2009 under terms of reference from the Minister for Finance. The ESC collects quarterly data from relevant insurers and relies on these insurers providing accurate information because the data is not audited. While a number of insurers no longer offer DBI cover, they are responsible for managing claims on policies they have issued.

Figure 4D shows information from ESC reports on DBI policies, premiums and claims between 2002 and 2014. The ESC data assigns the number of claims and their costs to the year in which the DBI policy was issued. This enables an assessment of the insurers' loss on policies issued each year but the long-tail nature of the DBI scheme means that it is difficult to gain a complete understanding of this until at least six years after the policy issue date. This is why claims costs in Figure 4D for recent years are much lower than earlier years.

**Figure 4D**  
**DBI premium and claims 2002–14**

Year	Number of DBI policies	Premium <sup>(a)</sup> (\$'000)	Number of claims <sup>(b)</sup>	Net claims costs <sup>(c)</sup> (\$'000)	Excess of premiums over claims costs (\$'000)
2002	17 731	10 661	160	4 839	5 822
2003	40 305	27 521	402	12 043	15 478
2004	34 720	27 536	359	17 742	9 794
2005	46 975	31 986	549	18 661	13 325
2006	53 142	32 119	575	19 284	12 835
2007	54 690	30 574	772	20 320	10 254
2008	53 113	27 650	606	22 573	5 077
2009	61 555	34 251	519	25 332	8 919
2010	65 101	41 881	640	23 511	18 370
2011	61 355	44 330	562	15 316	29 014
2012	57 703	46 678	320	9 572	37 106
2013	61 219	54 925	129	3 472	51 453
2014 Jan-June	32 449	32 000	5	19	31 981

(a) This only shows premium charges. Additional fees or charges imposed by brokers and/or builders are not included. From mid-2010 onwards the premium charged by VMIA includes the commission payable to its agent from which the agent pays brokers.

(b) These claim numbers are for registered builders only. There have been a total of 377 claims in relation to owner-builders since 2002.

(c) Net claims costs include amounts paid to successful claimants and other costs associated with managing claims.

*Note:* This data covers both registered builders and owner-builders. The ESC assigns number of claims and net claims costs to the year the DBI policy was issued.

*Source:* Victorian Auditor-General's Office based on information from the ESC.

The expected cost of payments to claimants in relation to claims on registered builders between 2002 and 30 June 2014 was \$153.1 million at 30 June 2014, with the average cost per claim of around \$33 000.

Figure 4D shows a significant excess of premium income over claims costs. However, the long-tail nature of DBI explains this:

- **For the years up to 2006** the insurers' overall profit or loss on DBI can be determined with reasonable certainty because the period for lodging a claim can be assumed to have past for the vast majority of policies. The data shows that in the years 2002 to 2006 inclusive, insurers collected \$57.2 million more in premiums than was paid out in claims. This amount would have been used to pay expenses including underwriting costs, broker commissions and claims handling costs.
- **For 2007 and beyond**, the significant excess of premium income over claims costs will be reduced over time as claims are made and processed.

## 4.6 The case for broader DBI reforms

Since 2008, successive governments and stakeholders alike have widely accepted the need for broader review and reform of the level of consumer protection provided by DBI. Despite this, the insurance remains essentially unchanged while there continues to be consumer misunderstanding of the product and a lack of transparency about its costs.

DTF and VMIA need to provide comprehensive advice to government on options to improve the adequacy and cost-efficiency of the DBI scheme.

### Progress on DBI improvements and reforms

Government intervention in the DBI market in 2010 enabled insurance to continue to be available but did not improve consumer protection because it did not change the limited, 'last resort', triggers for making a claim. Government intervention simply changed the underwriter, or bearer of risk, for DBI from the private sector to the state.

The Minister for Finance announced in March 2010 that while consumer protection under DBI would not be immediately enhanced, the government would discuss potential improvements to the level of protection offered to consumers with VMIA. Work commenced in early 2011 on developing reform options for the broader domestic building consumer protection framework, including DBI.

Potential improvements to DBI and details of consideration and action on them include:

- **Expanding the triggers for making a claim**—the DBI scheme has been 'last resort' since 2002. The triggers for making a claim are limited to the death, disappearance or insolvency of the builder. Expanded triggers proposed by the previous government were not progressed.
- **Increasing the threshold for mandatory DBI and the maximum available payout**—from 1 July 2014, the threshold for mandatory DBI was increased from \$12 000 to \$16 000 and the maximum cover from \$200 000 to \$300 000.
- **Replace DBI with a consumer protection fund**—the previous government's proposed reforms included a proposal to replace DBI with a domestic building consumer protection fund to be administered by VBA. This reform was not progressed.

- **Improve consumer information and advice on the nature of DBI**—VMIA identified a lack of consumer understanding of the DBI product early on in its involvement and has introduced a range of information materials to enhance consumer knowledge. This information is useful and readily accessible from VMIA's website for DBI.
- **Introduce a DBI policy database**—this could act as a one-stop shop for home owners wanting information on their policy and the scheme in general. This database was initially suggested by the ESC in March 2009. The government approved implementation of a DBI policy database in August 2009. The database has not been established despite almost six years passing. VMIA advised that it is planning on implementing a DBI policy database during 2015.

### Transparency of DBI costs to consumers

The cost of DBI to consumers can also include fees over and above the premium charged by VMIA. These additional fees may be imposed by brokers and/or builders but are not subject to scrutiny by VMIA or the ESC and are not transparently disclosed to consumers.

The ESC monitors the DBI market and reviews the validity of VMIA's premiums, but its work does not extend to providing information on the full costs of DBI to builders and consumers. No agency monitors the total costs of the insurance scheme.

DTF advice indicates that the final cost includes additional broker and other fees, which can range from 30 to 50 per cent on top of VMIA's base DBI premium. VMIA publishes its premium rates, but the actual premium charged is not currently disclosed on the DBI insurance certificate and is not usually separately disclosed in building contracts. This means that consumers have no way of identifying the extent of additional charges by brokers and/or builders.

This issue could be addressed without the need for legislative change.

### Improvements requiring consideration

Opportunities to improve the delivery of, and consumer protection offered by, DBI or any replacement scheme should be considered as part of deliberations on future reforms and should address the following issues:

- the most cost-efficient delivery model for DBI or any replacement scheme
- expanding the triggers for making a claim beyond the current 'last resort' triggers
- further improving consumer understanding of the nature and limitations of DBI, or any replacement scheme
- providing consumers with more transparent information on the DBI premium cost for their building project.

DTF, with support from VMIA, needs to develop comprehensive advice including robust option analysis and costings to support government deliberations on these issues.

## Recommendations

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That the Department of Treasury and Finance:

6. works with the Victorian Managed Insurance Authority to review the adequacy and cost of the current domestic building insurance scheme and provide advice to government on options to lower premiums and/or enhance coverage for consumers.

That the Victorian Managed Insurance Authority:

7. obtains certainty about its ongoing role in domestic building insurance provision and implements the most efficient delivery model
  8. alters the domestic building insurance policy certificate to show the base premium amount
  9. enhances the performance indicators and level of assurance gained on its agent's performance.
-





## Appendix A.

# Building practitioner registrations 2013–14

**Figure A1**  
**Categories and numbers of building practitioners**

Category	Class description	No. registered
Domestic builder	<p><b>Domestic builder-unlimited (DB-U)</b> May personally carry out, manage or arrange for sub-contractors to carry out all components of domestic work.</p> <p><b>Domestic builder-limited (DB-L)</b> May carry out, manage or arrange to carry out only the components of domestic building work specified in their Certificate of Registration.</p> <p><b>Domestic builder-manager (DB-M)</b> May manage or arrange for domestic builders registered in another class to carry out components of domestic building work specified in their Certificate or Registration.</p>	14 398
Building surveyor	<p><b>Building surveyor-unlimited and limited (BS-U/L)</b> May conduct building surveying functions—ensure construction projects meet building regulations—for either all buildings (U) or buildings up to three storeys in height with a maximum floor area of 2 000 square metres (L).</p>	603
Quantity surveyor	<p><b>Quantity surveyor (QS)</b> Is permitted to estimate and manage the cost of construction projects.</p>	134
Building inspector	<p><b>Building inspector-unlimited and limited (BI-U/L)</b> Is permitted to inspect all classes (U) or certain classes (L) and components of buildings and varieties and types of construction.</p>	633
Engineer	<p><b>Engineer</b> Encompasses four sub-classes: electrical, mechanical, civil and fire safety.</p>	2 246
Temporary structure	<p><b>Erector or supervisor of temporary structures (V1 and V2):</b></p> <ul style="list-style-type: none"> <li>Class 1—adequate knowledge and experience to erect, maintain and dismantle stages, seating stands or equipment platforms and towers.</li> <li>Class 2—adequate knowledge and experience to erect, dismantle, or supervise the erection or dismantling of tents, marquees and prefabricated buildings over 100 square metres in floor area.</li> </ul>	107

**Figure A1**  
**Categories and numbers of building practitioners – continued**

Category	Class description	No. registered
Demolition	<b>Builder-demolisher (BD)</b> —three sub-classes: <ul style="list-style-type: none"> <li>Builder—demolisher (low rise buildings) BD-L—has adequate knowledge and experience to demolish (excluding special buildings) and strip unoccupied buildings with a maximum of two storeys.</li> <li>Builder—demolisher (medium rise buildings) BD-M—has adequate knowledge and experience to demolish—excluding special buildings—and strip buildings with a maximum of five storeys.</li> <li>Builder—demolisher (unlimited) BD-U—has adequate knowledge and experience to demolish and strip any building including ‘Special Buildings’ (as defined in the regulations).</li> </ul>	302
Commercial builder	<b>Commercial builder-unlimited and limited (U/L)</b> May perform, manage and/or arrange any commercial building work (U) or only the components of building work specified on their certificate of registration (L).	4 540
Draftpersons	<b>Draftsperson Building Design (Architectural) (DP-AD)</b> May design and develop architectural working drawings for the construction of commercial, industrial and residential buildings. <b>Draftsperson Building Design (Interior) (DP-ID)</b> May design and develop working drawings for the interior fit-out of commercial, industrial and residential buildings. <b>Draftsperson Building Design (Services) (DP-SD)</b> May design and develop working drawings for services design, including water, sewerage, hydraulics, lighting and fire protection systems.	2 360
<b>Total individual building practitioners</b> —practitioners can hold multiple types of registration.		<b>21 186</b>

Source: Victorian Auditor-General's Office based on the VBA Annual Report 2013–14.

## Appendix B.

# *Audit Act 1994* section 16— submissions and comments

### Introduction

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In accordance with section 16(3) of the *Audit Act 1994*, a copy of this report was provided to the Victorian Building Authority, Building Practitioners Board, Department of Justice & Regulation (Consumer Affairs Victoria), Victorian Managed Insurance Authority, Department of Environment, Land, Water & Planning, Department of Treasury and Finance, and the Essential Services Commission.

The submissions and comments provided are not subject to audit nor the evidentiary standards required to reach an audit conclusion. Responsibility for the accuracy, fairness and balance of those comments rests solely with the agency head.

Responses were received as follows:

Department of Environment, Land, Water & Planning .....	90
Victorian Building Authority.....	93
Building Practitioners Board.....	96
Department of Justice & Regulation (Consumer Affairs Victoria) .....	97
Department of Treasury and Finance.....	100
Victorian Managed Insurance Authority.....	102

**RESPONSE provided by the Secretary, Department of Environment, Land, Water & Planning**



Department of Environment,  
Land, Water & Planning

Ref: BSEC15000083R

1 Spring Street  
Melbourne Vic 3000 Australia

25 MAY 2015

Mr John Doyle  
Auditor-General  
Victorian Auditor-General's Office  
Level 24  
35 Collins Street  
MELBOURNE VIC 3000



Dear Mr Doyle

**VAGO PERFORMANCE AUDIT: VICTORIA'S CONSUMER PROTECTION FRAMEWORK FOR BUILDING CONSTRUCTION**

Thank you for the opportunity to respond to the proposed report on *Victoria's consumer protection framework for building construction*.

The Department of Environment, Land, Water and Planning (DELWP) welcomes the report's acknowledgement of the actions taken by the department to respond to the 2011 recommendations. DELWP agrees that the most direct way to address the issue of maintenance of competence by building practitioners and continuing professional development is to introduce time-limited registration.

I am also pleased that the proposed report acknowledges the work undertaken by the Victorian Building Authority (VBA) and the Building Practitioners Board (BPB) to commence implementation of the recommendations from the 2011 audit report.

The Victorian Government is committed to increasing protection from home building malpractice. The Minister for Planning has already asked the department to consult with industry stakeholders and consumer advocacy groups to identify improvements to the building regulatory system including the domestic building consumer protection framework.

I am pleased to confirm that DELWP accepts the findings of the report and more specifically accepts those recommendations directed to the department. An action plan to implement the recommendations is enclosed.

**Privacy Statement**

Any personal information about you or a third party in your correspondence will be protected under the provisions of the Privacy and Data Protection Act 2014. It will only be used or disclosed to appropriate Ministerial, Statutory Authority, or departmental staff in regard to the purpose for which it was provided, unless required or authorised by law. Enquiries about access to information about you held by the Department should be directed to the Privacy Coordinator, Department of Environment, Land, Water and Planning, PO Box 500, East Melbourne, Victoria 8002



**RESPONSE provided by the Secretary, Department of Environment, Land, Water & Planning – continued**

The department will work collaboratively with the VBA and the BPB in the implementation of the recommendations directed to the department and will provide advice as required to the VBA on the implementation of their recommendations.

The timing to implement the action plan has been considered carefully to account for the need to engage fully with stakeholders and formulate a range of policy options for consideration by government.

Yours sincerely



**Adam Fennessy**  
Secretary

Encl.

Any personal information about you or a third party in your correspondence will be protected under the provisions of the Privacy and Data Protection Act 2014. It will only be used or disclosed to appropriate Ministerial, Statutory Authority, or departmental staff in regard to the purpose for which it was provided, unless required or authorised by law. Enquiries about access to information about you held by the Department should be directed to the Privacy Coordinator, Department of Environment, Land, Water and Planning, PO Box 500, East Melbourne, Victoria 8002

**RESPONSE provided by the Secretary, Department of Environment, Land, Water & Planning – continued**

**Department of Environment, Land, Water and Planning**

**Action Plan**

**Victoria's Consumer Protection Framework for Building Construction**

DELWP accepts recommendation one and recommendation two and commits to the following actions:

Audit recommendation	DEWLP Action	Partner/s	Completion Date
1. Review of the building practitioner registration and discipline systems	<p>DELWP will:</p> <ul style="list-style-type: none"> <li>▪ lead the development of policy options for consideration by the Government that aim to improve domestic building consumer protection through strengthened regulation, practitioner registration requirements, discipline and dispute resolution; and</li> <li>▪ present advice based on the policy options to the Government.</li> <li>▪ work with the VBA and the BPB to identify the range of data on the registration and discipline regimes that would be required to inform advice to government on systems improvement.</li> </ul>	<p>Building Practitioners Board (BPB)</p> <p>Victorian Building Authority (VBA)</p>	December 2015
2. Review of the regulatory arrangements for the engagement of private building surveyors	<p>DELWP will:</p> <ul style="list-style-type: none"> <li>▪ lead the development of a range of policy options for consideration by Government that in so far as possible support building surveyors to better perform their statutory functions under the <i>Building Act 1993</i>; and</li> <li>▪ present advice based on the policy options to the Government.</li> </ul>	VBA	December 2015



**RESPONSE provided by the Chairman and Chief Commissioner, Victorian Building Authority**



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22 May 2015

Mr John Doyle  
Auditor-General  
Victorian Auditor-General's Office  
Level 24, 35 Collins Street  
MELBOURNE VIC 3000



Dear Mr Doyle

**Performance Audit Report *Victoria's consumer protection framework for building construction***

On behalf of the Victorian Building Authority (VBA), I welcome your report on *Victoria's consumer protection framework for building construction* and the enclosed recommendations.

VAGO identifies that many of the issues raised in the report are long-standing and inherited from the Victorian Building Authority's (VBA) predecessor organisation. The VBA notes your report's acknowledgment of the actions the VBA has undertaken since its establishment in July 2013 to implement your previous recommendations. In addition, the VBA has made significant efforts to transform the organisation and its culture in order to address the failings of the former Building Commission in its governance practices and in undertaking its core regulatory work.

Whilst you acknowledge the progress made by the VBA, your report also makes useful recommendations on actions the VBA can undertake to provide greater confidence to both consumers and building practitioners that the regulatory system is operating effectively. The VBA accepts the recommendations contained within the report and has already committed to taking steps to implement them. The VBA's response to each recommendation and the timeframe for their completion is attached.

The VBA will work closely with the Department of Environment, Land, Water and Planning, the Building Practitioners Board and Consumer Affairs Victoria as required in the implementation of the three recommendations that involve the VBA.

Finally, I would like to acknowledge the work of your audit team, their constructive engagement with the VBA and their understanding of the role of the VBA in a complex regulatory environment.

Yours sincerely

William R. Kuszniarczyk  
Chairman and Chief Commissioner  
Victorian Building Authority

**RESPONSE provided by the Chairman and Chief Commissioner, Victorian Building Authority – continued**

**Victorian Building Authority Actions and Implementation Timeframe**

<p><b>Recommendation 3</b>  <i>That the Victorian Building Authority reviews its monitoring and compliance framework, and takes action, including advising the Department of Environment, Land, Water and Planning where necessary, to:</i></p> <ul style="list-style-type: none"> <li>- <i>Identify poor practitioner performance and appropriately prosecute and/or refer for discipline</i></li> <li>- <i>prioritise the monitoring and enforcement oversight of relevant building surveyors</i></li> <li>- <i>clarify respective agency responsibilities for monitoring and compliance including expediting a memorandum of understanding to clarify the roles of the Victorian Building Authority and councils for monitoring and enforcing compliance with the Building Act 1993</i></li> <li>- <i>Effectively administer the building permit levy including expediting the establishment of arrangements to allow the Victorian Building Authority to reassess and recoup underpaid levies, and require surveyors to remit levies directly.</i></li> </ul>	<p>Agreed.</p> <p>The VBA will continue to enhance and evaluate the approaches that it recently introduced in relation to monitoring and identifying poor performance of practitioners, including building surveyors. In addition the VBA will build on the current field work compliance program and enhance its inspection activity of the work of building surveyors by <b>30 June 2016</b>.</p> <p>The VBA is continuing to work with the Municipal Association of Victoria and individual councils to finalise an MOU regarding administration and enforcement responsibilities under the legislation. The VBA and MAV agreed an MOU in May 2015 and are currently seeking individual council agreement. Completion of this recommendation is dependent on council agreement.</p> <p>On 27 April 2015 the VBA published guidance on its website on the appropriate use and reconciliation of building permit levy funds and a practitioner self-assessment checklist. The VBA is also considering a new definition and methodology to determine the cost of works which is scheduled to be finalised by <b>31 July 2015</b>.</p> <p>The VBA will continue its enhanced levy audit program. <b>Ongoing</b></p> <p>The VBA will advise DELWP in the development of policy options to allow the VBA to reassess and recoup underpaid levies by <b>31 December 2015</b></p>
<p><b>Recommendation 5</b>  <i>That Consumer Affairs Victoria and the Victorian Building Authority review their consumer education and awareness activities to ensure consumers have access to straightforward and timely information and advice aimed at enabling consumers and builders to:</i></p> <ul style="list-style-type: none"> <li>- <i>Understand their rights and obligations under building contracts</i></li> <li>- <i>Understand the consumer protection</i></li> </ul>	<p>Agreed.</p> <p>The VBA and CAV have already established a working party to review consumer education and awareness activities to ensure this recommendation is met. This review and an action plan to address improvements or gaps will be finalised by <b>31 December 2015</b>.</p>



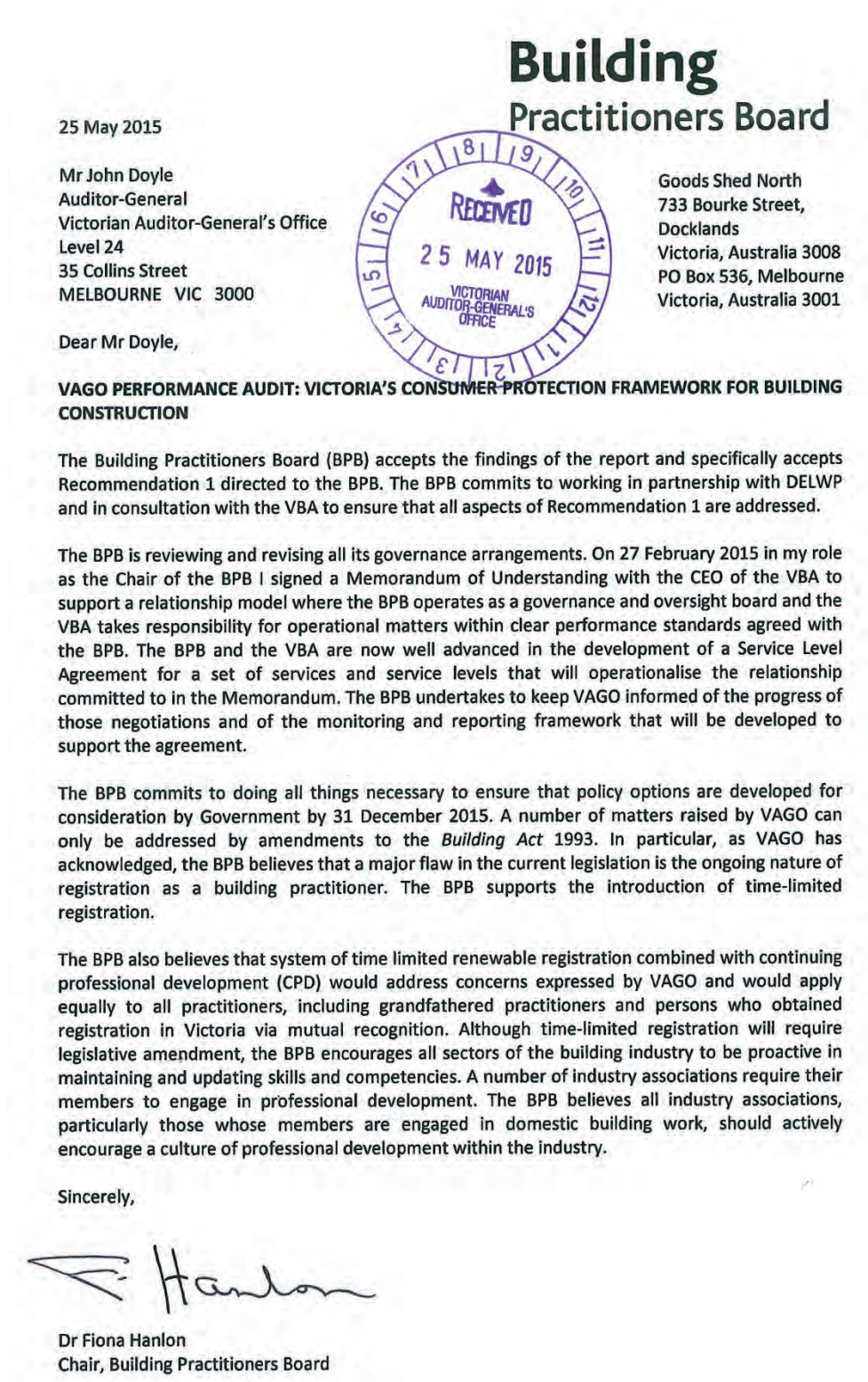


**RESPONSE provided by the Chairman and Chief Commissioner, Victorian Building Authority – continued**

<p>framework and access required information to make informed decisions</p> <ul style="list-style-type: none"> <li>- Be aware of the services available to assist with addressing consumer issues, and their limitations</li> </ul>	
<p><b>Recommendation 1</b>  <i>That the Department of Environment, Land, Water and Planning and the Building Practitioners' Board, in consultation with the Victorian Building Authority, reviews the practitioner registration and discipline regimes, and advises government accordingly, so that:</i></p> <ul style="list-style-type: none"> <li>- Only qualified, competent and suitable practitioners are allowed to trade</li> <li>- Practitioners have necessary building, business and financial skills and experience, appropriate resources and character, and fully understand their responsibilities and obligations</li> <li>- Monitoring provides assurance that practitioners maintain and update their skills over time and as building practices evolve</li> <li>- Practitioners' suitability for registration can be reassessed at the expiration of a finite registration period</li> <li>- Disciplinary systems and sanctions ensure that there is sufficient disincentive to engage in misconduct and that registered practitioners who do so can be excluded from trading</li> <li>- Data from registration and discipline regimes is collected and analysed to inform system improvements.</li> </ul>	<p>Agreed</p> <p>The VBA will provide input to DELWP and the BPB in relation to the development of policy options for consideration by the Government to improve the registration and discipline regimes for building practitioners.</p>



**RESPONSE provided by the Chair, Building Practitioners Board**





**RESPONSE provided by the Secretary, Department of Justice & Regulation  
(Consumer Affairs Victoria)**



**Department of Justice & Regulation**

Secretary

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25 MAY 2015



Our ref: CD/15/211517

Mr John Doyle  
Auditor-General  
Victorian Auditor-General's Office  
Level 24, 35 Collins St  
MELBOURNE VIC 3000

Dear Mr Doyle

**Consumer Protection Framework of Building Construction - Proposed Report**

Thank you for your letter dated 11 May 2015 enclosing the proposed audit report *Consumer Protection Framework for Building Construction* and the invitation to provide a formal response.

The Department of Justice & Regulation (the department) recognises the need for an effectively managed domestic building consumer protection framework for the wider Victorian community.

The department welcomes the findings/recommendations detailed in the report and accepts both Recommendations 4 and 5. A proposed action plan for the implementation of these recommendations is provided at Attachment 1.

Completion of the actions addressing the recommendations will be monitored by the department's Audit Tracking Register, which is updated and attested to by Deputy Secretaries and reviewed by the departments Audit and Risk Management Committee, on a quarterly basis.

Thank you for the opportunity to comment on the report.

Yours sincerely

**Greg Wilson**  
Secretary

Encl. Proposed Action Plan – Consumer Protection Framework of Building Construction



**RESPONSE provided by the Secretary, Department of Justice & Regulation  
(Consumer Affairs Victoria) – continued**

**Attachment 1: Proposed Action Plan – Victoria's Consumer Protection Framework for Building Construction**

**Department of Justice & Regulation response to VAGO recommendations**

Recommendation	Proposed Action	Completion Date
<p><b>Recommendation 4</b></p> <p>That Consumer Affairs Victoria reviews its dispute resolution and conciliation activities and advises government on options to improve their effectiveness, so that they are:</p> <ul style="list-style-type: none"> <li>• easy to access</li> <li>• low cost, simple and timely</li> <li>• objective and outcome focused</li> <li>• supported by necessary powers to compel participation in conciliation and enforce compliance with negotiated outcomes</li> <li>• underpinned by relevant and appropriate performance measures and effective monitoring, reporting and evaluation to demonstrate effectiveness.</li> </ul>	Consumer Affairs Victoria will continue to advise the Victorian Government on measures to improve the delivery and effectiveness of the dispute resolution and conciliation service it provides for domestic building consumers and building practitioners. This will include measures to promote participation and compliance with conciliated outcomes.	30 June 2016
	Consumer Affairs Victoria will review the dispute resolution and conciliation service to improve access to this service and ensure it provides an effective, low cost, simple and timely dispute resolution system for domestic building disputes.	30 June 2016
	Consumer Affairs Victoria will also review its dispute resolution and conciliation activities to ensure that they are objective and outcome-focused.	
	Consumer Affairs Victoria will develop relevant and appropriate performance measures and effective monitoring, reporting and evaluation to demonstrate its effectiveness in relation to its building related dispute resolution and conciliation activities.	30 June 2016
<p><b>Recommendation 5</b></p> <p>That Consumer Affairs Victoria and the Victorian Building</p>	Consumer Affairs Victoria and the Victorian Building Authority have established a working party	31 December 2015

**RESPONSE provided by the Secretary, Department of Justice & Regulation  
(Consumer Affairs Victoria) – continued**

Recommendation	Proposed Action	Completion Date
<p>Authority review their consumer education and awareness activities to ensure consumers have access to straightforward and timely information and advice aimed at enabling consumers and builders to:</p> <ul style="list-style-type: none"> <li>• understand their rights and obligations under building contracts</li> <li>• understand the consumer protection framework and access required information to make informed decisions</li> <li>• be aware of the services available to assist with addressing consumer issues, and their limitations.</li> </ul>	<p>to foster collaborative working arrangements in the current domestic building consumer protection framework.</p> <p>The working party will develop an action plan to ensure consumers have access to straight forward and timely information and advice.</p>	



**RESPONSE provided by the Secretary, Department of Treasury and Finance**



**Department of Treasury and Finance**

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Mr John Doyle  
Auditor-General  
Level 24  
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MELBOURNE VIC 3000



25 May 2015

*John*

Dear Mr Doyle

**VAGO AUDIT - VICTORIA'S CONSUMER PROTECTION FRAMEWORK FOR DOMESTIC BUILDING CONSTRUCTION PROVISIONAL DRAFT**

Thank you for the opportunity to respond to the proposed report on *Victoria's Consumer Protection Framework for Domestic Building Construction*.

The Department of Treasury and Finance (DTF) supports the findings and recommendations of the audit which reflect the potential to achieve improvements to the regulatory framework for building, including better consumer protection.

DTF notes that the report identifies an additional cost arising from the decision to retain an interim distribution arrangement for domestic building insurance (DBI). It is important to acknowledge that the Victorian Managed Insurance Authority has kept premiums to a level consistent with premiums charged by the market in 2002 (adjusted for CPI) when the scheme commenced.

DTF supports your recommendation that it work with the Victorian Managed Insurance Authority (VMIA) to review the adequacy and cost of the current DBI scheme and provide advice to government on options to lower premiums and/or enhance coverage to consumers.

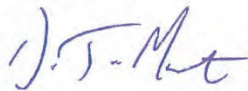
A review process is underway and initial advice on options to improve both the cost and cover of DBI has been provided to the Minister for Finance to help inform the Government's broader reform agenda in domestic building consumer protection.



**RESPONSE provided by the Secretary, Department of Treasury and Finance –  
continued**

The Government's approach to the continued provision of DBI will need to be settled before the VMIA's current mandate to provide DBI expires on 30 June 2016 and DTF will continue to work with the VMIA to identify opportunities to further improve DBI as part of this process.

Yours sincerely

A handwritten signature in blue ink, appearing to read 'D. Martine', is written over a faint, large watermark of the word 'VICTORIA'.

**David Martine  
Secretary**

**RESPONSE provided by the Chairman, Victorian Managed Insurance Authority**



22 May 2015

Mr John Doyle  
Auditor-General  
Victorian Auditor-General's Office  
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MELBOURNE VIC 3001



**FOR PUBLICATION**

Dear Mr Doyle

**PROPOSED VAGO PERFORMANCE AUDIT REPORT: VICTORIA'S CONSUMER PROTECTION FRAMEWORK FOR BUILDING CONSTRUCTION**

Thank you for the opportunity to comment on the proposed *Draft Performance Audit Report: Victoria's Consumer Protection Framework for Building Construction*.

The Victorian Managed Insurance Authority (VMIA) accepts the following recommendations relating to VMIA's role in supporting the community through the delivering domestic building insurance by no later than December this year. That the VMIA:

- Obtains certainty about its ongoing role in the provision of domestic building insurance and implements the most efficient delivery model.
- Alters the DBI policy certificate to show the base premium amount.
- Enhances the performance indicators and level of assurance gained on its agent's performance.

VMIA looks forward to continuing to work with the relevant departments and agencies to enhance the current domestic building consumer protection framework and deliver improved outcomes for the community.

On behalf of management I would like to compliment VAGO on the consultative approach taken through the conduct of this review which enabled VMIA to provide feedback prior to finalisation of the report.

I look forward to being able to report on progress against the recommendations.

Yours sincerely  
**John Peberdy**  
Chairman

[www.vmia.vic.gov.au](http://www.vmia.vic.gov.au)

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# Auditor-General's reports

## Reports tabled during 2014–15

Report title	Date tabled
Technical and Further Education Institutes: Results of the 2013 Audits (2014–15:1)	August 2014
Coordinating Public Transport (2014–15:2)	August 2014
Managing the Environmental Impacts of Transport (2014–15:3)	August 2014
Access to Legal Aid (2014–15:4)	August 2014
Managing Landfills (2014–15:5)	September 2014
Management and Oversight of the Caulfield Racecourse Reserve (2014–15:6)	September 2014
Effectiveness of Catchment Management Authorities (2014–15:7)	September 2014
Heatwave Management: Reducing the Risk to Public Health (2014–15:8)	October 2014
Emergency Response ICT Systems (2014–15:9)	October 2014
Public Sector Performance Measurement and Reporting (2014–15:10)	October 2014
Mental Health Strategies for the Justice System (2014–15:11)	October 2014
Information and Communications Technology Controls Report 2013–14 (2014–15:12)	October 2014
Auditor-General's Report on the Annual Financial Report of the State of Victoria, 2013–14 (2014–15:13)	October 2014
Additional School Costs for Families (2014–15:14)	February 2015
Responses to 2012–13 Performance Audit Recommendations (2014–15:15)	February 2015
Water Entities: Results of the 2013–14 Audits (2014–15:16)	February 2015
Portfolio Departments and Associated Entities: Results of the 2013–14 Audits (2014–15:17)	February 2015
Public Hospitals: Results of the 2013–14 Audits (2014–15:18)	February 2015
Efficiency and Effectiveness of Hospital Services: High-value Equipment (2014–15:19)	February 2015
Effectiveness of Support for Local Government (2014–15:20)	February 2015
Local Government: Results of the 2013–14 Audits (2014–15:21)	February 2015
Managing Regulator Performance (2014–15:22)	March 2015
Education Transitions (2014–15:23)	March 2015
Emergency Service Response Times (2014–15:24)	March 2015

Report title	Date tabled
Digital Dashboard: Status Review of ICT Projects and Initiatives (2014–15:25)	April 2015
Palliative Care (2014–15:26)	April 2015
Tendering of Metropolitan Bus Contracts (2014–15:27)	May 2015
Occupational Violence Against Healthcare Workers (2014–15:28)	May 2015
Early Intervention Services for Vulnerable Children and Families (2014–15:29)	May 2015
Universities: 2014 Audit Snapshot (2014–15:30)	May 2015
Technical and Further Education Institutes: 2014 Audit Snapshot (2014–15:31)	May 2015

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