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Building Policy
Ministry of Business, Innovation & Employment
PO Box 1472
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Emailed to: building@mbie.govt.nz

Dear Committee Members,

Insurance Council of New Zealand Submission on discussion paper: Building System Legislative Reform

Thank you for the opportunity to submit on the discussion paper on Building System Legislative Reform ('discussion paper'), which was released by the Ministry of Business, Innovation and Employment (MBIE) in April 2019.

ICNZ represents general insurers that insure about 95 percent of the New Zealand general insurance market, including about a trillion dollars' worth of New Zealand property and liabilities, and paid out approximately \$2.4 billion to consumers and businesses in 2018. ICNZ members provide insurance products ranging from those usually purchased by individuals (such as home and contents insurance, motor vehicle insurance and travel insurance) to those purchased by small businesses and larger organisations (such as product and public liability insurance, professional indemnity insurance, commercial property, and directors and officers insurance).

Please contact John Lucas (john@icnz.org.nz or 04 995 8006) if you have any questions on our submission or require further information.

Overarching comments

ICNZ strongly supports better regulation in the building space and welcomes the proposals outlined in the discussion paper. In particular:

- The proposed changes will provide better quality, more resilient buildings which will minimise the chance of defects arising in future.
- Clarifications to roles and responsibilities will allow for accountability by the appropriate parties should an element or elements of the build fail.
- The proposed changes will allow for greater protections and building outcomes for homeowners.

- The proposed changes would give insurers greater confidence in the building sector.

Against these positives, we again raise a concern ICNZ has raised a number of times before – that changes are required to building standards for commercial property to better integrate seismic resilience into the New Building Standard (NBS). This measure is essentially a life-risk measure, not a reflection of its ability to function after an earthquake, yet many people have been misled into upgrading their property in the belief it is strengthening resilience of the structure. While this is not part of the consultation process, it is a critical point that we encourage MBIE to address as part of this reform.

Part 2: Building products and methods

Proposal 1 -Widen the purpose of the Building Act to include the regulation of building products and building methods.

Do you agree with expanding the purpose of the Building Act to include the regulation of building products and methods and their use?

Yes No

Please tell us why or why not.

ICNZ supports the expansion of the purpose of the Building Act to include the regulation of building products and methods and their use. The current purposes of the legislation are to ensure that:

- People who use buildings can do so safely and without endangering their health
- Buildings have attributes that contribute appropriately to the health, physical independence, and well-being of the people who use them
- People who use a building can escape from the building if it is on fire
- Buildings are designed, constructed, and able to be used in ways that promote sustainable development.

Allowing for the regulation of building products and methods would be a logical extension. Insurers would support wider regulation of the building process as this will lead to the use of better products, better methods of construction, and more resilient buildings.

Consideration should also be given to further expansion of the purposes to includes buildings being designed and constructed to reflect the need for post-seismic event functionality and low cost remediation.

Proposal 3 - Set minimum standards for information about building products and require manufacturers and suppliers to supply that information.

2.5 Do you support the proposal to require manufacturers and suppliers to supply information about building products?

Yes

No

Please tell us why.

ICNZ supports the proposal to require manufacturers and suppliers to supply information about building products. However, we believe that the proposal could go further. ICNZ recommends that a 'Products Supplied Register' be developed and maintained for each building site to improve the traceability and accountability of the parties who supplied the products used.

A register such as this could include details of all products supplied to the site, confirmation that the products match the design specifications, and who the products were supplied by (meaning the New Zealand manufacturer or supplier). The register could be provided to the homeowner's GIP provider following practical completion so that they can track the suppliers of all products used in the build, in the event any aspect of it fails. The GIP provider would then have the option of holding the supplier of the defective product liable and seeking recovery.

As an example, consider ready mixed concrete. A Products Supplied Register could record the supplier, the batch number, the concrete specification as delivered such as aggregate size, MPa rating, slump specification and any admixtures. This would provide easy identification of the supplier should the concrete later crack for example, and would also help provide a cross-reference for other properties who have also used the same potentially-faulty product and the same supplier.

A Products Supplied Register would also provide a good check for specified product substitution. Product substitution is an area which commonly leads to building code and/or original specification non-compliance and would likely contribute to later building defect claims.

A Products Supplied Register would require appropriate oversight to be effective. To this end, registers could be required to be lodged with MBIE who could in turn carry out random audits to ensure that all details have been correctly recorded.

Proposal 4 - Clarify the responsibilities of manufacturers, suppliers, designers and builders for building products and building methods.

2.11 Do you support the proposals to clarify roles and responsibilities for manufacturers, suppliers, designers and builders?

Yes

No

Please tell us why.

ICNZ supports all measures that will clarify roles and responsibilities for manufacturers, suppliers, designers and builders for two main reasons. Firstly, as liability insurers, having greater clarity of an insured's specific role in a building project will help them to better price risk. Secondly, as property insurers, and potentially as builders warranty insurers, having clarity around roles and responsibilities will make it easier to pursue the appropriate party should part of the building fail.

Proposal 5 - Give MBIE the power to compel information to support an investigation.

2.13	Do you support the proposal to give MBIE the power to compel information to support investigations?
<input checked="" type="checkbox"/> Yes	<input type="checkbox"/> No
Please tell us why.	
ICNZ supports this proposal as it would help strengthen regulation and monitoring in the building sector, and likely improve outcomes for building owners.	

Potential impacts of the proposed changes

2.15	Do you think the impact of the proposed changes to the regulation of building products and building methods (proposals 1-5) would be positive or negative? What do you think the impact might be?										
<table style="width: 100%; text-align: center;"><tr><td>Strong negative impact</td><td>Negative impact</td><td>No impact</td><td>Positive impact</td><td>Strong positive impact</td></tr><tr><td><input type="checkbox"/></td><td><input type="checkbox"/></td><td><input type="checkbox"/></td><td><input checked="" type="checkbox"/></td><td><input type="checkbox"/></td></tr></table>		Strong negative impact	Negative impact	No impact	Positive impact	Strong positive impact	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input checked="" type="checkbox"/>	<input type="checkbox"/>
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Please tell us what the impact might be.											
The proposed changes will provide better quality, more resilient buildings which will minimise the chance of defects arising. The proposals will also allow for accountability by the appropriate parties should an element or elements of the build fail. This would particularly be the case if the Government adopts the Products Supplied Register, as suggested by ICNZ, and if improvements to seismic resilience standards were introduced.											
2.16	How do you think the proposed changes to the regulation of building products and building methods would change how you and your business/organisation operates?										
<table style="width: 100%; text-align: center;"><tr><td>Strong negative impact</td><td>Negative impact</td><td>No impact</td><td>Positive impact</td><td>Strong positive impact</td></tr><tr><td><input type="checkbox"/></td><td><input type="checkbox"/></td><td><input type="checkbox"/></td><td><input checked="" type="checkbox"/></td><td><input type="checkbox"/></td></tr></table>		Strong negative impact	Negative impact	No impact	Positive impact	Strong positive impact	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input checked="" type="checkbox"/>	<input type="checkbox"/>
Strong negative impact	Negative impact	No impact	Positive impact	Strong positive impact							
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Please tell us why.											
The proposed changes to the regulation of building products and building methods will help to give insurers greater confidence in the building sector. This may help to increase insurer risk appetite in this area and create greater interest in offering a builders warranty product.											
Further, if seismic building standards are improved, then property owners would be in a position to better retain and transfer risk to the insurance market at an affordable rate. It would also reduce the social and economic dislocation after seismic events.											

Final thoughts

2.28 If you have any other comments on the proposals for building products and methods, please tell us.

ICNZ supports all seven proposed changes to building product regulations. Without the changes to building product regulation, GIP providers will likely be exposed to greater risk of latent defects and systemic building system failures and this could determine whether or not they wish to enter the market and what price they would charge for their builders warranty products.

We note that while we do not have any specific comments on Proposal 7 in relation to MMCs, we support the establishment of such a regulatory framework. ICNZ supports innovation and methods which seek to reduce cost, provided they are subject to robust regulation and oversight by the appropriate parties.

Part 3.1: Occupational regulation of the Licensed Building Practitioner (LBP) scheme

Proposal 1 - Broaden the definition of restricted building work (RBW) to include more complex non-residential building work.

3.1.1 How effective do you think expanding the scope of RBW would be in managing risks to public safety in the building sector?

Not effective

Somewhat effective

Very effective

3.1.2 Do you agree with the proposed threshold for the definition of RBW?

Yes

No

Please tell us why.

ICNZ strongly supports the proposal to broaden the definition of RBW to include more complex non-residential building work.

There is no particular category of building which is exempt from risk and all buildings, whether residential, commercial, or mixed-use should be held to the same standards of safety and durability. ICNZ agrees with the discussion paper that owners and occupants of apartments in high-rise or multi-use buildings are equally vulnerable to the risks of something going wrong in the build process as owners of stand-alone dwellings. We further note the comment that one-third of commercial building inspections fail. These factors are concerning. We therefore consider the proposal to extend the RBW definition to be a logical one likely to result in improved building standards and increased levels of safety.

ICNZ is particularly pleased to see the inclusion in the definition of commercial buildings and larger than medium-sized residential properties. ICNZ has long held concerns around particular elements of these types of builds where non-LBPs are performing tasks vital to safety. We highlight two particular areas of concern below, which would benefit from the

increased regulation that would stem from broadening the definition of RBW. Please note that these are both issues which we have previously raised with Ministers.

- (1) The first example where RBW does not currently apply in commercial-type construction is passive fire protection. Non-compliance of passive fire protection in commercial buildings and high-rise apartments is common and very worrying. This non-compliance involves the failure to correctly fire stop service penetrations through fire rated walls, incorrect construction of fire rated walls and the installation of smoke extraction systems that do not work. This non-compliance places lives at risk, as well as risks to the building and businesses that may operate in that building. Passive fire protection installers are not currently licensed. ICNZ and the Association of Building Compliance ran a workshop on passive fire in August 2018. There was widespread interest in the workshop with over 150 fire protection industry specialists in attendance. Attendees agreed that to minimise the risks from poorly installed fire protection, there needs to be a specific licence class for passive fire protection installers.
- (2) The second example where RBW does not currently apply is the installation of non-structural elements for seismic loads that locate, retain and restrain ceilings, partitions and services in buildings. This work has generally not been done well and has contributed to extensive and unnecessary business disruption and insurance losses from the recent earthquake events affecting Canterbury and Wellington. This type of non-compliance has likely contributed to the high insurance costs and limited availability concerns currently being experienced in Wellington. The correct use of non-structural elements for seismic loads is also a life safety issue.

Proposal 2 - Higher competence requirements to increase confidence in the LBP scheme.

3.1.7

How effective do you think raising the competence standards for the LBP scheme would be in increasing confidence in the LBP scheme?

Not effective

Somewhat effective

Very effective

Please tell us why.

The proposals in this area are to:

- Raise the technical competence standard for LBPs to enter and remain in the LBP scheme.
- Introduce a tiered licencing system for LBPs to establish a progression pathway, including a specific licence for supervision.
- Simplify the licence class categories.
- Introduce behavioural competence requirements for LBPs.

ICNZ believes each of these elements will help to raise the skill level and competence of LBPs overall. Increased standards such as these will give insurers greater confidence in the type of person carrying out building work. This is important as insurer confidence will be reflected in premiums for liability insurance, and the decision of whether to enter the builders warranty market or not.

3.1.13 Do you think that the introduction of a fit and proper person test and a code of ethics for LBPs would help to ensure that building professionals are held accountable and improve the public’s confidence in the LBP scheme?

	Yes	No
Fit and proper person test	<input checked="" type="checkbox"/>	<input type="checkbox"/>
Code of the ethics for LBPs	<input checked="" type="checkbox"/>	<input type="checkbox"/>

Please tell us why.

Insurers are going to be heavily reliant on the competency and good conduct of all builders if they decide to make builders warranty products available in New Zealand in future. The proposal to introduce a fit and proper person test together with a code of ethics will only increase insurers’ confidence in the building profession as it will make the behavioural standards required of LBPs clear, and everyone will be held to the standard. Standards such as these will bring LBPs further in line with other professions insurers currently provide liability insurance for.

Without insurer confidence there is unlikely to be an expansion to the market which offers builders warranty products. This would likely mean that only a select group of LBPs will be able to offer GIPs as the few insurers offering products will be more selective in who they will offer cover to.

Final thoughts

3.1.16 If you have any other comments on the proposals for LBPs, please tell us?

This section of the discussion paper makes no mention of the known issues with “phoenix builders” where an LBP closes down their trading companies and then reforms under a new entity to avoid liability claims. This may happen on multiple occasions within a relatively short space of time.

ICNZ believes that the issue of “phoenix builders” is a major risk, particularly in terms of liability, which could be addressed by changes to the occupational regulation of LBPs. Stricter licensing requirements would go some way to reducing this problem. One option would be to follow the Queensland model and allow the regulator to suspend individual licences for non-payment of debt. Under the Queensland Home Warranty Scheme, a licensed contractor must pay all undisputed debts, or they risk loss of their licence. Licensed contractors who accumulate a certain number of demerit points within a three year period can be disqualified from holding a licence by the Queensland Building and Construction Commission for a period of three years¹.

¹ <https://www.qbcc.qld.gov.au/sites/default/files/Monies%20Owed%20Complaint%20Form.pdf>.

Part 3.2 Occupational regulation of Engineers

Final thoughts

3.2.17 If you have any other comments on the proposals for engineers, please tell us.

ICNZ supports the proposal for improved occupational regulation and licencing of engineers. We agree with the establishment of a new certification scheme but question whether it should be voluntary, as proposed. We also agree that there should be restrictions on medium-to-high complexity engineering work and restricted engineering work.

It is logical that engineers who undertake this type of work should be held to higher standards of technical skill given the size, type and use of the buildings involved, as well as the greater risks of getting it wrong. Engineers usually purchase Professional Indemnity liability insurance. This covers them (subject to the limits and exclusions or endorsements of their particular policy) for negligent damage caused to third parties in the course of their work. The proposed categories of restricted engineering work will likely give insurers greater confidence and may encourage greater acceptance of risk. Having improved information about certification and category of work an engineer may undertake will also help to price Professional Indemnity insurance more accurately.

ICNZ further supports the proposal for a robust process for the management of complaints and discipline, along with the proposed penalties for non-compliance. ICNZ believes that the proposal is appropriate for professionals such as engineers as the grounds for discipline and possible penalties appear similar to those for other comparable professions.

We note that the proposals may have an initial impact on the availability of engineers but believe that any impact will not be long lasting, with any reduction being filled as engineers upskill and meet certification requirements. We believe that any impacts on availability will in any case, be outweighed by the improvements to the work undertaken by engineers, and the improvements in life safety rating and resilience of buildings.

Part 3.3 Occupational regulation of Plumbers, Gasfitters and Drainlayers

Final thoughts

3.3.10 If you have any other comments on the proposals for plumbers, drainlayers and gasfitters, please tell us.

ICNZ supports the proposals to remove the current exemptions that allow unqualified persons to undertake sanitary plumbing, gas fitting and drain laying work. It appears that the exemptions are a hangover from the previous Act and may have been missed in moving to the Plumbers, Gasfitters, and Drainlayers Act 2006, rather than being bound in reason. As the discussion paper notes, it is also unfair that some tradespeople are exempted from regulatory requirements while others are bound by them.

Not only would this proposal create consistency in application of the law, it would lift the levels of competency for the work done and minimise the risk of failures occurring in future.

Part 4 Risk and liability

Proposal 1 - Require a guarantee and insurance product to be in place for all residential new builds and significant alterations. Homeowners would have the choice to actively opt out of having a guarantee and insurance product.

4.1 Do you support the proposal to require guarantee and insurance products for residential new builds and significant alterations?

Yes

No

Please tell us why.

ICNZ supports the proposal to require guarantee and insurance products to be offered for residential new builds and significant alterations. We agree with the comments made in the discussion paper that homeowners have a limited understanding of their risks and how to manage them. GIPs would help to protect homeowners against some of the risks to what is likely to be their greatest asset.

In an ideal world, having a GIP in place would be mandatory for everyone building a new home or undertaking alterations to an existing home. This would provide financial protection and certainty for all New Zealanders building or renovating their homes. Making it mandatory would have the advantage of building a sustainable premium pool quickly to meet claims. However, it is important that any mandatory requirement to provide builders warranty insurance products is balanced against supply, and at present, we are not confident that there is sufficient capacity to meet current demand, let alone the increased demand that would be created by a mandatory scheme.

Currently, builders warranty insurance in New Zealand is sold by just two providers that are backed by one syndicate at Lloyd's of London. It should not be assumed that Lloyd's will be able to provide further capacity in the future, or even to maintain the current level of capacity. Lloyd's capacity for this type of long tail business can vary from year to year and is influenced by claims performance, changes in the global financial markets, and regulatory requirements and legislative changes both here and in the United Kingdom. Issues around capacity are further complicated by the 10-year longstop period under the Building Act 2004. Certain case law around weathertight dwellings has seen the 10-year limitation period stretched even further and anticipating that the same position could be taken in relation to builders warranty insurance may affect future capacity. ICNZ recommends that serious consideration be given to the Lloyd's submission on this matter.

As in our response to question 4.10 below, we believe it would be best for the other changes proposed in the discussion paper to first be implemented, followed by a observation period of two years, before consideration is given to a GIP scheme, and whether that scheme should be mandatory. This will allow insurers, other than the one currently in the market, to make an informed decision based on the performance of the building sector, as to whether they will enter the builders warranty market.

4.2 Do you think homeowners should be able to actively opt out of having a guarantee and insurance product?

Yes

No

Please tell us why.

ICNZ echoes the comments already made in response to question 4.1 above, that ideally GIPs would be mandatory. However, we recognise that this requires a certain level of capacity which cannot be guaranteed at this time.

Allowing homeowners to opt out of having a GIP furthers the likelihood that the market will not be big enough to attract the other insurers that are needed to ensure a competitively priced market and adequate capacity. The present market lacks competition as two of the three providers are tied to specific building associations, which leaves one provider with a monopoly over the remainder of the GIP market. Insurers would have a limit on the amount of builders warranty business they could write as the builders warranty liability on any one insurer's books would have to match that insurer's capital position. With only one or two insurers providing builders warranty there will be limits on capacity to provide builders warranty products and this limit may not be enough to fill the needs of a voluntary market.

4.3 Should there be conditions on when homeowners are able to opt out? What should these conditions be?

Yes

No

Please tell us why and what the conditions should be.

There must be safeguards put in place to ensure a homeowner has been fully informed about what the offered GIP would provide, and what opting out would mean. The introduction of a GIP requirement, whether mandatory or opt out, must be accompanied by a concerted effort to inform homeowners about the risks presented by building or carrying out significant renovations, and the protections offered by a GIP. ICNZ believes that builders should be required to undertake training to ensure that they are able to fully inform a homeowner about a product. There should be routine checks carried out by MBIE with homeowners to ensure that they were aware of their rights and the builder correctly explained what the GIP would cover and the consequences of opting out. Homeowners should also be required to acknowledge in writing that they have been informed of and understand the risks of opting out of a GIP.

4.4 What types of buildings do you think should be required to have a guarantee and insurance product? (Please tick all that should apply.)

Standalone residential dwellings

Medium density housing (up to six storeys)

High density housing (over six storeys)

Mixed-used developments (i.e. where a part of the building is used as commercial premises, for example shops or offices.)

Please tell us why.

	<p>ICNZ notes that it may be problematic for high-rise apartment buildings to obtain GIPs, however smaller low-rise mixed-use residential/commercial buildings have builders warranty insurance offerings currently and this will likely continue.</p> <p>High-rise apartment buildings are likely to be a challenge for insurers to provide GIPs for due to the very high construction costs of these buildings and their complexity with construction. Insurers are not likely to have the necessary capacity to insure a high-rise apartment building for non-completion or defects. Insurers could also find it challenging to provide GIPs for a single unit in a high-rise apartment building that is being renovated due to the relationship and complexity with the existing building structure.</p> <p>The maximum claim value is normally the construction contract price including the value of any variations to the original contract. It should not be a problem for insurers to provide coverage for standalone residential homes exceeding several million dollars including small mixed-use residential/commercial buildings but excluding high-rise apartment buildings.</p> <p>ICNZ therefore believes that high-rise apartment buildings should not be included within any GIP scheme.</p> <p>Mixed-use developments should be required to have a GIP, provided that they are not high-rise buildings.</p>
<p>4.5</p>	<p>What threshold do you think the requirement for a guarantee and insurance product should be set at?</p> <p><input checked="" type="checkbox"/> Residential building work over \$30,000</p> <p><input type="checkbox"/> Residential building work over \$100,000</p> <p><input type="checkbox"/> Residential building work that would impact the structure or weathertightness of the building.</p> <p><input type="checkbox"/> Other (please tell us more in the comment box below)</p> <p>Please tell us why or any other comments.</p> <p>ICNZ prefers the lower threshold as it would mean that most alterations would require a GIP. Not only will this provide protection for a greater number of homeowners, but it will help to establish the premium pool which is used to pay builders warranty claims. If a viable premium pool is not established in a short period of time, meaning that there may not be enough premiums collected to pay claims, then this is likely to negatively impact on the sustainability of builders warranty insurance products being available for the New Zealand market.</p>
<p>4.6</p>	<p>Do you have any views on the minimum standards that should be set for a guarantee and insurance product?</p> <p>For example: the type of product, the types of events that are covered, the minimum level of cover, the period of cover, the nature of redress, the maximum claim value, dispute resolution processes, the ability to transfer to new owners.</p> <p>GIPs should cover non-completion, loss of deposits paid to the builder and structural defects including weathertightness failures for a period of ten years. This would be consistent with the cover currently being provided by the two insurance schemes in</p>

	<p>New Zealand. The insurers also offer additional cover for non-structural defects up to ten years rather than two and costs for alternative accommodation.</p> <p>A clear dispute resolution process will be important for GIP customers and insurers. We note that for customers insured through a Lloyd’s of London GIP they will have protection and information on the dispute resolution process via the Fair Insurance Code, which all Lloyd’s coverholders domiciled in New Zealand must comply with. The Code provides an automatic pathway to external dispute resolution (subject to a \$200,000 limit) if the dispute cannot be resolved internally within two months.</p> <p>ICNZ agrees with MBIE’s preference in the discussion paper that the homeowner should be the policyholder rather than the builder, as this will allow the GIP to be transferred to the next owner if the house is sold within the 10 year cover period. Having the homeowner and builder as joint insureds would not be an attractive option for insurers, as they would not be able to recover any money from the builder in the event the builder was responsible for a loss.</p>
<p>4.7</p>	<p>What financial and prudential requirements do you think should be placed on providers, to ensure there is a continuing supply of guarantee and insurance products?</p> <p>For example: reinsurance or other insurance backing, solvency, auditing requirements, security and prudential requirements.</p> <p>ICNZ notes that the Reserve Bank of New Zealand’s (RBNZ) review of the Insurance (Prudential Supervision) Act 2010 is due to recommence towards the end of this year. We believe that review would be a more appropriate forum to consider any necessary changes to financial and prudential requirements. We encourage MBIE to consult with the RBNZ, as any changes to financial and prudential requirements will need to be suitable to a whole-of-risk approach, rather than addressing one specific line of business.</p> <p>It is noteworthy that aspects of the current prudential regime include requirements for licensed insurers to hold sufficient solvency and/or reinsurance to meet a 1:1000 year seismic event. This is one of the world’s highest solvency requirements. The RBNZ can deem offshore insurers as carrying an equivalent level of solvency.</p>
<p>4.8</p>	<p>If residential new builds and significant alterations are required to have a guarantee and insurance product, what do you think the impacts will be?</p> <p>Requiring new builds and significant alterations to have GIPs will offer increased protection for the homeowner. Only builders of a certain standard will be able to offer GIPs which should help to ensure that the process is completed, and products of a high quality are used, minimising the risk of non-completion or future issues arising.</p> <p>Homeowners with GIPs may find that their houses are worth more if they decide to sell as evidence of a GIP on a LIM will be seen as a quality mark.</p> <p>These dwellings will also likely be seen as lower risk for insurers as they will likely be of higher quality than buildings without a GIP.</p>

MBIE proposes a two-year transition period.

4.10 How long do you think the transition period for guarantee and insurance products needs to be to ensure providers, builders and BCAs are prepared for the changes?

- Less than two years Two years More than two years

Please tell us why.

The introduction of the requirement for builders to offer GIPs should be delayed for two years after the proposed legislative reforms for occupational regulation, building products and methods, and offences, penalties and public notification changes are introduced and in full effect so that prospective new builders warranty insurers can observe changes to the residential construction sector before committing their capital. As some of the transition periods under the proposed changes in the discussion paper are six years, this would mean that the GIP scheme would not be implemented for at least another eight years.

When deciding to write a new type of business such as residential construction sector builders warranty, insurers will rely on historical claims information from the residential construction sector. This claims information will be used for modelling the new insurance product. Details such as average claims cost, claims frequency and claims cost recovery success all need to be understood so that coverage limits can be set, maximum portfolio loss expectancy can be factored for the purchase of reinsurance and importantly, the premiums that should be charged. This information and modelling is required so that the insurer can satisfy itself that the insurance product is going to be viable. The same information will be required by the RBNZ to make sure that the insurer will have enough capital to pay all claims.

Past and current poor performance of the residential construction sector has not been attractive for insurers to risk their capital by providing GIPs. Evidence of improved competency, accountability, and building standards will therefore be needed before more insurers look to offer builders warranty products.

Any information MBIE can provide insurers about the performance of the building sector once the proposed changes are implemented will help in their decision making as to whether they should offer builders warranty insurance. The success of these reforms will play a key role in future offerings.

It may be that after this period, depending on whether there has been a demonstrable improvement to building practice and performance due to these reforms, further consideration is given to whether GIPs should be mandatory.

Proposal 2 – Leave the liability settings for BCAs unchanged.

4.12 If the government decides to make all the other changes in this discussion paper, do you agree that that the liability settings for BCAs will not need to be changed?

- Yes No

Please tell us why.

Regardless of whether the government decides to make all the other changes in this discussion paper, ICNZ does not believe that liability settings for BCAs should be changed. If BCA liability is reduced this would likely reduce insurer appetite for offering builders warranty products.

Reducing BCA liability would likely increase the risk for builders warranty insurers as the BCA may relax their consenting and inspection checks. Less thorough inspections lead to an increased risk of latent building defects that would be picked up as claims on the builders warranty insurance during the ten years following completion of the build.

If a BCA carries out a negligent inspection or negligently issues a consent resulting in a builders warranty claim, then the insurers would want to exercise their normal rights to recover those losses from the negligent BCA. Limiting the BCA's liability setting in any way would prevent this and again, may reduce insurers' appetite to enter the market.

BCA consenting and inspections must be thorough, and the government should not take any steps to reduce the liability arising from these duties. The BCA building inspector needs to be able to monitor the builder's performance at every stage of the scheduled site inspections as the BCA has the statutory role of taking action against the builder who has failed to comply with the building code and the specific build plans and specifications for the particular build.

Builders warranty insurers will want to undertake their own various building site inspections during the construction phase to satisfy themselves that all building code requirements, best practice and specific design and construction considerations are all being met, even if the BCA is also undertaking inspections. We do not see this as an unnecessary duplication of roles between the BCA and the insurer. We believe it is necessary as it will create a better safety margin for identifying non-compliance and other problems before those parts of the construction are hidden and then manifest themselves later resulting in a future builders warranty claim.

It is important to note that if claims costs for builders warranty insurers increase, then premiums will likely have a corresponding increase.

As ICNZ does not support a limit on BCA liability, it also does not support a cap on BCA liability, be that at 20 per cent or some other amount.

4.16 What do you think would be the impacts of placing a cap on BCA liability?

A cap on BCA liability could lead to a homeowner bearing a higher proportion of the liability should something go wrong. While the proposed changes in all sections of this discussion paper are a good start, as outlined in response to question 3.1.16, the discussion paper does not fully address the issue of "phoenix builders". If steps are not taken to tighten LBP licensing, as ICNZ has suggested, and builders are still able to "phoenix" together with BCA liability being capped, the homeowner may not have any responsible parties to pursue for damage. This will mean that the homeowner is left to cover the cost of the majority of any damage which will likely drive insurance premiums higher.

Final thoughts

4.17 If you have any other comments on the proposals for risk and liability, please tell us.

ICNZ notes the wording in the discussion paper “require a guarantee and insurance product to be in place for all residential new builds and significant alterations”. While we recognise this likely means an ability to *offer* a GIP, we request confirmation that there is no suggestion of legislation to force insurers to offer a builders warranty product. While ICNZ sees that a mandatory GIP scheme would be ideal for developing a sustainable market quickly as this would create a more attractive market for a greater number of insurers to enter, there is no guarantee that will happen and we do not believe that governments should be mandating specific cover be offered.

Part 5 Building levy

Proposal 1 - Reduce the rate of the building levy from \$2.01 to \$1.50.

5.1 Do you agree that the levy rate should be reduced from \$2.01 to \$1.50?

Yes

No

Please tell us why.

The discussion paper states that the current building levy has generated a surplus of \$43 million. This would indicate that the current levy rate is not required to be maintained. ICNZ therefore supports a reduction to a level sufficient to cover the costs of the services MBIE provides. We note that reducing the levy rate is consistent with the objective of reducing a large and growing balance in the building levy memorandum account.

The changes proposed in the discussion paper are likely to result in increased costs for LBPs, engineers etc. In reality, this will mean increased costs for the homeowner. It would therefore be logical to decrease the building levy, if the current rate is not required, to balance some of the increased costs in other areas.

Proposal 2 - Standardise the threshold for the building levy at \$20,444 including GST (per \$1,000).

5.5 Do you have any comments on standardising the threshold at \$20,444?

ICNZ agrees that the threshold should be standardised to ensure consistent application of the levy throughout the country.

Part 6 Offences, penalties and public notification

Final thoughts

6.8 If you have any other comments on the proposals for offences, penalties and public notification, please tell us.

It would seem consistent with other legislation in New Zealand for there to be an increase in the maximum financial penalties under the Building Act, and for the maximum limits to be different for individuals and organisations. However, it is likely that an increase to the proposed limits will have an effect on the ability to obtain insurance, and the cost of that insurance.

ICNZ therefore queries whether MBIE is looking at restricting insurance for liability incurred under the Building Act. We note that insurance against fines is already unlawful under the Health and Safety at Work Act 2015, and limited under the Financial Markets Conduct Act 2013, while the Credit Contracts Legislation Amendment Bill, which is currently being considered, proposes to place similar restrictions on insurance.

We note Government commentary on the Health and Safety at Work Act which states that fines under that legislation cannot be insured against to ensure duty holders do what is reasonably practicable to keep workers and others safe. It reasons that duty holders may be less vigilant if they are able to insure themselves against the consequences². We question whether the same reasoning is likely to be extended to the Building Act, given it has similar safety interests in mind.

Overall feedback

Thinking about this consultation, do you have any comments or suggestions to help us improve future consultations?

3 Any other comments or final thoughts?

In completing the review of the building system, ICNZ encourages MBIE to think beyond life safety, and also think about building resilience post disaster. We believe that resilience is close to equal in importance. Following a disaster, houses will be needed, community buildings will be needed, and workplaces will be needed to get what will likely be a damaged local economy up and running as soon as possible. It is therefore important to set standards that will not only prevent loss of life but will result in more resilient buildings being built.

New Zealand is a seismically active country. Traditionally, New Zealand has risk-managed seismic risk by transferring it to local insurance companies that in turn transfer most of that risk to specialist international reinsurers. A building system that focusses not just on life safety, but building resilience is essential to the sustainability of earthquake insurance in New Zealand.

Creating resilient buildings will also require consideration of and addressing the examples raised in relation to question 3.1.2 around passive fire protection installation and the installation of non-structural elements for seismic loads.

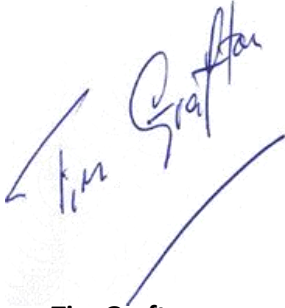
ICNZ would be happy to meet with MBIE to further discuss our particular concerns around these issues.

² <http://www.education.govt.nz/assets/Documents/Ministry/Initiatives/Health-and-safety/Tools/Health-and-Safety-at-Work-Act-2015-practical-guide.pdf>

Conclusion

Thank you again for the opportunity to submit on the discussion paper. If you have any questions, please contact our Insurance Manager on (04) 495 8006 or by emailing john@icnz.org.nz.

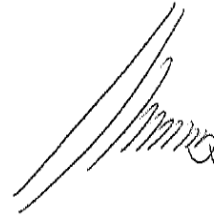
Yours sincerely,

Handwritten signature of Tim Grafton in blue ink, written in a cursive style.

Tim Grafton
Chief Executive

Handwritten signature of Jane Brown in blue ink, written in a cursive style.

Jane Brown
Legal Counsel

Handwritten signature of John Lucas in blue ink, written in a cursive style.

John Lucas
Insurance Manager