

New home warranties: homebuilding market study

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Homebuilding market study

Annexe J – New home warranties

Professor James Sommerville

September 2008

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1 EXECUTIVE SUMMARY

- 1.1 The purchase of a new home constitutes a significant undertaking in the lives of most homebuyers. The general anticipation is that the new home will bring them a period of enjoyment and happy use from the day they take possession until the day they leave. For the majority of these homebuyers this is the biggest single purchase they will make and is a process that will not be undertaken again for a significant number of years. Some homebuyers do undertake the purchase of a new home more than once and become well versed in the mechanics of the new home buying process and also the various impediments they have to overcome along the way.
- 1.2 Integral to the process of buying this new home is the interaction with the homebuilder and the homebuyer's partial immersion in some of the intricacies of the homebuilding process that is, understanding the need for, and using, the new home warranty.
- 1.3 The findings, from the research undertaken on the range and mechanics of new home warranties shows that in the international scene there is no clear picture as to how new home warranties should be structured or operated. The various countries considered, and discussed, show the breadth of approach being undertaken by each country and the divergence in approaches with regard to whether homebuilders should be registered and whether to legislate for home warranties, or not, as the case may be. The new home warranty system operating in the UK whilst perhaps not being seen as perfect, does have a number of features that provide the homebuyer with a fairly robust new home warranty system that is, it has a focal point in the National House Building Council ('NHBC'), and the other warranty providers (Building LifePlans, Local Authority Building Control, Premier and Zurich) offer well established products, the warranty providers are businesses which appear to be relatively stable, and, homebuyers, based on findings from research undertaken as part of this report, accept that a warranty adds to the overall process of buying a new home.

- 1.4 Analysis of literature, and data from the responses to the postal questionnaires sent out as part of this research, relating to the quality of new homes and the relationship with the new home warranty shows that there may be a gap between what the new homebuyer perceives as 'quality' and what the homebuilder sees as 'quality'. The warranty providers operating in the UK do not set quality standards, even though some do provide, and ask builders to adhere to, a set of technical standards.
- 1.5 Answers to a series of questions presented to focus groups, and sent out in a postal questionnaire as part of this research, show that there are a number of gaps in the homebuyer's knowledge of new home warranty provision for example, who actually provides the warranty, and how it operates. Many of the respondents were unfamiliar with the contents and coverage of their new home warranty, were confused as to who actually provided the cover under the warranty and yet, they valued the warranty being available since it provided some form of 'peace of mind'.
- 1.6 The new home warranty, generally, plays little part in the decision to move home, there are a number of other factors that are considered more important, and it may be that the provision of a new home warranty is seen as being something that happens almost without the homebuyer's intervention within the overall new home buying process.
- 1.7 All of the new homebuyers, who participated in this research, were aware of inspections having been carried out on their new homes by various bodies and their view was that these inspection regimes helped, in part, to instil quality in their new home. Standard of finish, standard of materials and good 'finishings' were strong indicators of 'quality' for the new homebuyers who responded to the postal questionnaire.
- 1.8 Even though new home warranty providers have devoted considerable effort to communicating with new homebuyers as to the warranty's scope and operation, there still exist gaps in the homebuyers' knowledge around the warranty. Many of the respondents stated that the warranty had not been explained to them prior to their occupation of the new home. When questioned as to who should provide the warranty there

was no strong support from the homebuyers for the current providers since the new homebuyers were of the view that the warranty was only an insurance policy. The Council of Mortgage Lenders play a significant role in the need for a new home warranty, since most new homes are required to have a warranty in place before mortgage funds will be released on the new home, and yet their part is poorly understood by the new homebuyers.

- 1.9 The new homebuyers who had raised a claim under the warranty saw bringing a claim against the homebuilder, under the auspices of the home warranty, as an experience that is less than conducive to the building of harmonious relationships.
- 1.10 Some 13 per cent of total homeowners who responded to the postal questionnaire had commissioned a snagging report, the remaining 87 per cent had not had a snagging inspection carried out.
- 1.11 This research throws some interesting light on the issue of warranties and the quality of new homes and is capable of much further expansion across the whole of the new homebuilding arena within the construction industry.

2 INTRODUCTION

- 2.1 Professor James Sommerville holds a Chair in Construction Management at Glasgow Caledonian University. He has extensive industrial experience in both the UK and Middle East construction markets, and serves, or has served, on a number of leading professional, industry and academic bodies including: Chair of The Chartered Institute of Building's Member Services & Support Board, and Grievance & Appeals Board, member of Council of The Chartered Institute of Building, member of the Council of The Royal Institution of Chartered Surveyors in Scotland, member of the Technical Standards Committee and Council of The National House Building Council, member of the board of AssetSkills (Scotland), a non-executive director of Inspector Home Ltd., External Examiner for a number of Universities and, is Referee for a range of leading industry and academic journals.
- 2.2 Having launched a market study on homebuilding on the 22nd of June 2007, The Office of Fair Trading (OFT) sought an analysis of a number of features of new home warranty provision, including International experiences, in the sector through commissioned research efforts¹. This research effort is guided by the parameters of the study set out at Section 8 Home building – reasons for a market study, June 2007, OFT934².
- 2.3 The author was charged with looking at a large number of separate questions surrounding warranty provision in the UK and internationally. Given the variety of issues examined, and the fact that several can be regarded as stand alone pieces of research in their own right, it has not been possible to present this research as one continuous narrative and, of necessity, a number of issues are discussed sequentially as stand alone issues.

¹ Following the receipt of a number of representations and meetings it was however decided at a relatively early stage of the study that the OFT's internal resources would be better employed focusing on issues other than new home warranties.

² www.offt.gov.uk/shared_offt/reports/comp_policy/oft934.pdf

2.4 As part of the research, it is noted that the OFT's study covers the extent to which consumers have power to drive competition, the level of consumer protection and redress and the extent and nature of competition in the home building industry.

2.5 Within this work the term homebuilder includes the term developer.

The data collection/research method

2.6 The data used in this research was collected through a mixed method approach executed during the months of November and December 2007 and January 2008.

2.7 The mixed method approach consisted of focus group meetings, postal and email questionnaires, semi-structured face-to-face interviews and semi-structured telephone interviews, which provided qualitative and quantitative data. The respondent groups comprised new-build homebuyers in a range of geographical regions throughout the UK, as shown in Figure 2.1.

2.8 The black dots on Figure 2.1 indicate those respondents who provided data on general issues surrounding new home warranties (204 respondents). The black crossed-circle represent respondents who had lodged a claim on their warranty (eight respondents who provided the detailed case reviews considered in annexe 1).

2.9 1600 questionnaires were sent to a stratified sample of new-build developments across the UK, and 204 responses were received back (a response rate of 13 per cent). Newbuild developments across central Scotland were targeted on the ground with a direct mail insertion through the letter box of each new home. The respondents from elsewhere in the UK were drawn from a database constructed from new homes that had had a snagging³ inspection carried out by Inspector Home Ltd. These

³ 'Snagging' is the process whereby a new home is inspected by someone, usually independent of the builder, who looks for, and records, defects in the new home. The list of defects is then passed to the homebuilder for rectification.

buyers of the new home who had commissioned the snagging inspection acted as conduits for the questionnaires and passed copies of the questionnaires to their neighbours. Hence the clusters in various areas.

Figure 2.1: Respondent clusters (each marker may include more than 1 respondent)



2.10 The fieldwork with regards to the questionnaires was executed during the months of November and December 2007 and January 2008. The field workers were drawn from directly employed, full-time, University research staff. The desk study and fieldwork for the international review was undertaken during the above periods and also March 2008.

2.11 There are a set of limitations that must be acknowledged within this research: the first is the actual number of newbuild developments underway which meant that only a sample of the total number of developments could be accessed in the time available, secondly, is the issue of a limited budget within which all research has to be undertaken, with more financial resources, so more people could have been used on a much broader range of newbuild developments throughout the country, thirdly, the timeframe within which the research has to be undertaken and reported upon meant that a cut-off point for the gathering of field data had to be rigidly adhered to, with more time to identify and contact new home owners, so a much broader sample of responses could have been gathered and their views processed.

New home warranties in the UK - what are they?

2.12 When a new home is purchased in the UK, the majority of homebuyers need monetary support from a financial institution in the form of a mortgage. In order to secure the mortgage, most lenders will ask for some form of warranty which covers the home against a set of perils for a specified period of time. This warranty is generally provided to the homebuyer by the homebuilder when the homebuyer takes possession of the new home. Most mortgage lenders insist upon having the protection afforded by this warranty in place before releasing the mortgage funds. Indeed, most lenders will not action the release of mortgage funds without the warranty being in place or the homebuilder being a member of a recognised warranty scheme. If a warranty is not in place then the homebuyer will need to source funds from a lender who is happy to offer the financing without the security of the warranty being in place. In the unusual situation where a homebuyer does not require the support of a lending institution then it is possible that this homebuyer could buy this new home without the need for a warranty. However, if this new home is then sold on within prescription (a 10 year) period the second buyer (or their lender) may ask for some form of guarantee to be put in place by the seller.

- 2.13 New home warranties are in effect insurance policies which provide cover against problems arising with specified parts of the new home and the resulting repairs to these specified parts for example, the foundations, the structural walls, the electrical wiring system. The warranty may also include some fixtures for example, a central heating system's boiler. General coverage offered by warranties is shown in Tables 2.1 and 2.2. From these tables it can readily be seen that there is a remarkable similarity between the National House Building Council ('NHBC') Buildmark warranty and the Zurich Building Guarantee. Other warranty providers do not make data relating to their coverage as freely available as NHBC or Zurich. Both NHBC and Zurich policies are similar and as such the consumer who, generally, has little knowledge of the homebuilding process is not in a position to make an informed decision as to whether these policies actually offer choice. The warranties are similar enough to be construed as being the same but provided by different organisations. In addition to the specific parts mentioned in the warranty, the warranty sets out to guarantee that certain features of the new home, such as the materials and workmanship, will meet minima laid down by the warranty issuing body.
- 2.14 These minima are usually described in a set of technical standards or a manual made available to the homebuilder by the warranty provider. The technical standards or manual sets out the relevant British Standards, makes reference to the relevant Building Regulations and Codes of Practice, and provides a mechanism for audit, undertaken by the warranty providers or their representatives, processes to identify whether the homebuilders are meeting these standards.
- 2.15 Currently, within the UK, there are five main players in the new home warranty market. They offer the following new home warranty products (in alphabetic order): Building LifePlans (BLP) Secure, Local Authority Building Control (LABC) New Home Warranty, National HouseBuilding

Council (NHBC) Buildmark, Premier Guarantee and, Zurich Building Guarantee⁴.

How do warranties operate?

2.16 In the year 2006 - 2007, there were an estimated 210,847 new home completions in the UK (based on data extracted from the Department for Communities and Local Government (DCLG)⁵ live tables on homebuilding). In terms of the number of new home warranties issued, the leading player is clearly NHBC with some 178,832 new home registered in the 2006 – 2007 financial year. Table 2.3 indicates the number of new NHBC registrations in the UK and the number of private home completions where they issued a warranty. Also shown in Table 2.3 is data from Department of Communities and Local Government ('DCLG') on private home starts and completions in the UK. In the previous years 2005, 2004, 2003, 2002, NHBC registrations were 188777, 184610, 178871, and 171519, respectively although the actual number of warranties issued may vary from this figure since some completions, and hence, warranty issuance, may roll-over from one year to the other. From the number of new homes completed each year, it is clear that the other warranty providers have the potential to have issued, on average, only a very small number of warranties per annum.

The part played by warranties in the quality of the new home

2.17 The other major warranty providers have been approached to provide data for this research but due to commercial sensitivity of some of the data, and the time constraints of the research, felt unable to provide hard data as to the number of warranties they issue and therefore no estimates relating to their data have been made.

⁴ www.blpinsurance.com www.labcnewhomewarranty.co.uk/
www.nhbcbuilder.co.uk/ www.premierguarantee.co.uk/
www.zurich.co.uk/buildingguarantee/home/intro.htm

⁵ www.communities.gov.uk/housing/housingresearch/housingstatistics/livatables/

- 2.18 In order that the home may have a warranty attached to it, the homebuilder is required to register with the warranty provider. The general process for such registration is as follows: details of the development site, when it is first proposed for development, are submitted to the warranty provider for their consideration. The information contained will at the very least locate the development, indicate the plot arrangement, and the home types to be located on each plot along with the technical details of the home types. Other data required by the specific warranty provider is provided by the homebuilder as required. The warranty provider will review the data provided and inform the homebuilder that they may proceed, or otherwise, with the development⁶. The homebuilder decides when to commence the actual building of the new home and informs the warranty provider that the actual plot, with the relevant home type on it, has commenced. The warranty provider will then initiate inspections of the building of the new home to ensure conformance to their standards. Building Control Inspectors will also visit the new home as it is being constructed but they, normally, do not play a role in the warranty mechanism. The warranty inspections take place at a range of stages of construction of the new home for example, when the substructure is complete, when the superstructure is erected, when the internal walls are ready for decoration, when the drainage system is installed, when the new home is ready to be handed over, and so on.
- 2.19 The registration process as discussed above entails the completion of a number of documents by the homebuilder which are aimed at assisting the warranty provider in establishing the level or risk attaching to the warranty, as and when it is issued. The documents are designed to extract as much detail as possible from the homebuilder that will inform the warranty provider as to the homebuilder's approach to risk, financial soundness, general operating procedures, and past record of claims. At the end of the registration process, the homebuilder then pays a premium for the issuance of the warranty. The premium charged is generally based on each builder's rating although BLP do use a wider reference based,

⁶ (note that this process is not Planning related, it is purely an early start on the risk assessment process)

where they take account of more financial data and risk management analyses, as a mechanism by which to arrive at an individual premium.

Table 2.1: Sample areas covered by NHBC Buildmark warranty

| Sample areas covered by NHBC Buildmark warranty | |
|--------------------------------------------------------|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Cover before completion | |
| What NHBC pay for | If builder does not start the home, the NHBC will repay the amount paid to the builder which you cannot recover. |
| What NHBC pay for | If the builder starts the home but does not complete, will repay the amount which you have paid the builder and cannot recover or pay the extra cost to complete the home to NHBC standards. |
| What NHBC pay for | The cost of work that the NHBC have instructed the builder to do, and which they fail to complete in accordance with NHBC Regulations. |
| What NHBC will not pay for | Anything not included in the original contract. |
| Builders Obligations the first two years after | |
| What the builder is liable for | Within a reasonable time, to put right any defect or damage which is notified to them within this period of cover. |
| What the builder is liable for | Any costs you incur for removal, storage and accommodation if you have to move out the home. |
| What the builder is not liable for | Wear and tear and deterioration caused by neglect. Dampness, condensation or shrinkage not caused by a defect. |
| What the builder is not liable for | Anything caused by alterations to your home and any cost that is greater than that need to carry out a workmanlike repair. |
| What NHBC will pay for | Any arbitration award or court judgement and the cost of work contained in the resolution service which is accepted by you and if the builder is insolvent, the cost of work which they would otherwise have been liable for. |
| What NHBC will not pay for | Anything for which you have held back a sum of money otherwise this will be deducted from the amounts due to be paid. |
| Cover in years 3-10 of the warranty | |
| What NHBC will | The full cost if it is more than £1000 for damage caused by a defect in the |

| | |
|----------------------------|----------------------------------------------------------------------------------------------------------------------------------------------------------------|
| pay for | following parts of a home mentioned above as part of the Buildmark 2000 policy. |
| What NHBC will pay for | The cost of rectifying a defect in a flue/chimney that poses an imminent danger to anyone living in the home. |
| What NHBC will pay for | Any costs you incur for removal, storage and accommodation if you have to move out the home. |
| What NHBC will not pay for | Claims relating but not limited to shrinkage, cosmetic damage, spalling (where the render falls off the walls), water entry to garages and sound transmission. |

Source: Adapted from NHBC, 2007a

Table 2.2: Sample areas covered by Zurich

| Sample areas covered by Zurich | |
|---------------------------------------------------------|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Cover before the new home is complete | |
| What Zurich pay for | If the developer fails to complete the construction of the new home, Zurich will pay the reasonable costs of completing the home to specification or pay the buyer the amount of any lost deposit. |
| What Zurich will not pay for | Any works that exceeds the original specifications and any claim made after the legal completion of the home by the first buyer. |
| What Zurich will not pay for | Any Claim where WE have not issued a valid Building Period Certificate. |
| What Zurich will not pay for | Any sum exceeding 10 per cent of the purchase price declared by the developer. |
| Obligations the first two years after completion | |
| What Zurich pay for | Reasonable cost of rectifying physical damage caused by the house builder's failure to comply with requirements. |
| What Zurich pay for | Professional fees in connection with the claim although the consent of the insurance provider has to be agreed. |
| What Zurich pay for | Reasonable cost of rectifying a failure in the building that poses a danger to health and safety. |
| What Zurich pay for | Cost of accommodation if the new home is not fit for habitation as a result of works need to be carried out. |
| What Zurich will | Anything excluded by endorsement on the insurance certificate and |

| | |
|--------------------------------------------|-----------------------------------------------------------------------------------------------------------------------------------------|
| not pay for | repairs that exceed the original specification. |
| What Zurich will not pay for | Claims for wear and tear, neglect, efflorescence, staining and scratching and any loss arising from any alterations of the new home. |
| Cover in years 3-10 of the warranty | |
| What Zurich will pay for | The reasonable cost of rectifying physical damage caused by failure to comply with the original requirements. |
| What Zurich will pay for | Rectifying a failure in the building due to non-compliance of the building regulations that poses a danger to health and safety. |
| What Zurich will pay for | Any costs you incur for removal, storage and accommodation if you have to move out the home and professional fees if previously agreed. |
| What ZURICH will not pay for | Anything excluded by endorsement on the insurance certificate and repairs that exceed the original specification. |
| What ZURICH will not pay for | Claims for wear and tear, neglect, efflorescence, staining and scratching and any loss arising from any alterations of the new home. |

Source: Adapted from Zurich 2007

Table 2.3: Registrations and completions

| Registrations and completions | | | |
|--------------------------------------|------------------------------------------------|------------------------------------------------|-----------------------------------------------------|
| Year | NHBC UK registrations In financial years | UK private home starts from DCLG data | UK private home completions from DCLG data |
| 2002/3 | 171,519 | 177,803 | 183,880 |
| 2003/4 | 178,871 | 178,852 | 190,577 |
| 2004/5 | 184,610 | 193,358 | 206,564 |
| 2005/6 | 188,777 | 204,873 | 215,024 |
| 2006/7 | 178,832 | 210,847 | 218,543 |

Source: NHBC (direct email to author) and DCLG website

2.20 In general terms, the majority of warranties issued offer to 'cover' that is, insure, a range of specified parts of the new home as outlined in Tables 2.1 and 2.2. The majority of the warranty providers offer an extensive list of exclusions. The majority of the warranties emphasise that a home does not include ancillary items such as: fences, temporary structures, swimming pools, lifts, electronic or mechanical equipment (whether built in or not) except those items which are necessary to comply with general requirements of the Building Regulations for example, if air conditioning is supplied then it must comply with the general requirements of the Building Regulations. Table 2.4 illustrates common features of the main warranties.

Table 2.4: Features of new home warranties

| Features of new home warranties | | | | | |
|-----------------------------------------------------|-------------------------------------------------------------|------|------|---------|--------|
| Elements within policy document | Warranty provider (✓ represents the risk is covered) | | | | |
| Risk covered | BLP | LABC | NHBC | Premier | Zurich |
| Insolvency of homebuilder | ✓ | ✓ | ✓ | ✓ | ✓ |
| Fraud perpetrated by homebuilder | ✓ | ✓ | ✓ | ✓ | ✓ |
| Homebuilder's failure to start new home | ✓ | ✓ | ✓ | ✓ | ✓ |
| Homebuilder's failure to complete new home | ✓ | ✓ | ✓ | ✓ | ✓ |
| Defects (although no detailed definitions provided) | ✓ | ✓ | ✓ | ✓ | ✓ |
| Structure (generally load-bearing elements) | ✓ | ✓ | ✓ | ✓ | ✓ |
| Contaminated land | Extension | ✓ | ✓ | ✓ | ✓ |
| Period of cover | | | | | |

| | | | | | |
|-------------------------------------------------------------------------------|-------|---------------|----------|---------------|-----------------|
| 8 years | | Varies | √ | √ | √ |
| 10 years | √ | | possible | | |
| Excess on claim (in some cases specific clauses attach stated sums) | £2500 | £100/100 0 | £650 | £100/10 00 | £ varie s |
| No-blame basis (the homebuyer does not have to prove the cause of the defect) | √ | | | | |
| Instruction on how to notify/make a claim given | Yes | Yes | Yes | Yes | Yes |
| Those marked with an * are acceptable to the Council of Mortgage Lenders | * | | * | * | * |

2.21 The new home referred to in the warranty document, together with any of the included parts (a list of specific areas included within the warranty) are covered for problems arising during defined periods. In the first instance, normally for a period of two years, cover is actually provided by the homebuilder and during this time the homebuilder usually will attempt to make good the problem identified. At the end of this two year period a secondary time period commences, usually for eight years, within which the warranty provider then becomes liable and will attempt to make good the problem. Some warranty providers extend the warranty cover period from eight to ten years for example, BLP, whose policy is active from the date of handover of the new home. In practice what this means is that there are warranty providers who rely on the homebuilder covering the first two years after the date of handover of the total warranty period and others for example, BLP, who cover from the date of handover. Should the homebuilder fail that is, through insolvency or fraud, to commence or complete the building of the new home, the majority of the warranty providers will become active and move in to facilitate the completion of the new home and ensure that the homebuyer is able to move into the new home. If the homebuilder fails in the first two year period to make good an identified and notified problem then, there are mechanisms

described in the warranty providers' documentation whereby the homebuyer can revert to the warranty provider to seek rectification of the problem.

- 2.22 In order to have the warranty placed on the new home, the homebuilder will be required to satisfy the warranty provider that construction has been undertaken in accordance with the current Building Regulations operated by the local authority Building Control department or the Approved Inspector, and any general standards/guidelines laid down by the warranty provider.
- 2.23 Ensuring conformity with Building Regulations is normally achieved through the attainment of a Completion Certificate (a document issued by the local authority Building Control department or the Approved Inspector that signifies that the works shown on approved drawings and specification have been followed and completed to the satisfaction of that Completion Certificate issuer). Compliance with the warranty provider's own standards/guidelines is often monitored by the warranty provider's own dedicated inspection teams or specialists that they are able to call upon to carry out a range of inspections, at various stages of the build process.
- 2.24 If the build process has proceeded as planned, and the new home has also been inspected throughout the various inspections and the stages of the build process for example, sub-structure, super-structure, internals, services, etc., then the warranty is issued by the warranty provider to the homebuilder. The warranty is for the home and attaches to that building not the owner. Thus if the new home is sold within the warranty period, the warranty remains in force for the new homebuyer to call upon if and when necessary.
- 2.25 Whilst there are a number of warranty providers operating in the UK, only three provide what may be seen as direct links to a Building Control service, although, the actual extent of the Building Control service offered varies significantly between the providers.

2.26 In the UK, anyone can build a new home for sale. However, the majority of mortgage lenders (who are member of the Council of Mortgage Lenders)⁷ will require some form of warranty to be in place to underpin their lending on a new home mortgage and as such, the majority of homebuilders join a warranty scheme. The NHBC may be seen to be the new home standard setter and leading warranty and insurance provider from their position of coverage of the market and their length of existence. NHBC is as a non-profit distributing company (any profit made from operating is held within the business and used solely for the operation of the business), established over seventy years ago, providing home warranties and risk management services to the homebuilding industry. More than 80 per cent of new homes built in the UK each year are registered with the NHBC and have the 10-year warranty and insurance policy called 'Buildmark' attached to them (NHBC, 2008a).

The remit of NHBC

2.27 At its inception in 1936, NHBC's stated objective was to 'encourage and promote a high standard of design, workmanship and materials in house building in the United Kingdom.' This objective was to be achieved through establishing a register of qualified home-builders who built to a set of minimum standards. NHBC sets, monitors and maintains a series of construction technical standards⁸. NHBC registers homebuilders, inspects their work at key stages of the construction process, and seeks to reduce the number of defects in new homes⁹.

2.28 NHBC extended its role, in 1967, by offering consumer protection to homebuyers through the introduction of a 10-year warranty and insurance policy called the Buildmark. In 1985, NHBC's role was broadened further when the then Government authorised NHBC to carry out Building Control inspections in competition with local authorities.

⁷ www.cml.org.uk/cml/home

⁸ See sections R1 – R5 of NHBC Technical Standards, Part1, General Information, 2006 onwards.

⁹ NHBC, (2007) *Who we are and what we do*, www.nhbc.co.uk/Newscentre/Library/filedownload,16305,en.pdf

2.29 NHBC offer 'Buildmark' as a warranty and insurance policy which has two parts: for the first two years NHBC offers to underwrite the homebuilder's liability to repair any defects in the property. NHBC acts as 'mediator', investigating whether any defect is a breach of its Technical Standards and, if found to be so, instructs the homebuilder to carry out repairs. If the homebuilder fails to do so, then NHBC can intervene to ensure the work is carried out. The second part of 'Buildmark' consists of an insurance policy for years 3-10, which covers the main structure of the home. NHBC offer their products to self-builders and companies.

Technical standards, registration and inspection

2.30 NHBC's Technical Standards lie at the centre of the organisation's aim to raise the quality of new homes: they set, and repeatedly review, the standards to which new homes are built and provide advice and assistance to homebuilders. New homebuilder applicants are put through a technical and financial vetting system and if accepted on to the register, then they must comply with NHBC Rules and build to NHBC's Technical Standards.¹⁰

2.31 NHBC carries out inspection at key stages of construction of a new home for example, foundations, sub-structure, super-structure, services, etc. By inspecting every new home as it is being constructed, NHBC seeks to minimise the incidence of defects and manage risk for the homebuilder. NHBC also provides a range of services for the homebuilder, including technical information, training, health and safety, engineering and energy rating services.

Other UK warranty providers

2.32 Zurich Financial Group, through their Zurich Building Guarantee have a ten year latent defects warranty covering newly built homes for sale or rent by the private homebuilder or social housing sector. For the first two years the homebuilder is responsible for rectifying damage or major

¹⁰ NHBC, (2007) *Who we are and what we do*, Available: www.nhbc.co.uk/Newscentre/Library/filedownload,16305,en.pdf,

damage caused by defects that do not meet Zurich's published technical requirements. If they do not deal with them, Zurich will act for the policy holder and arrange for remedial action themselves. The remainder of the 10 years is insured by Zurich. Zurich's policy provides a range of options to widen the cover and the warranty can be extended at the end of the normal 10 year term, subject to claims experience and the payment of an additional premia, Zurich warranty cover can also be provided for self builders.

2.32 Premier Guarantee was established in 1996 and operates in the Republic of Ireland and the UK. It operates a 10 year warranty that provides structural defect cover for a, restricted, full cost of repairs to any one house. Other home warranty providers for example, Building Life Plan¹¹, Build Zone¹², and Local authority Building Control¹³, provide new home warranties but are able to capture a relatively small share of the market place.

¹¹ <http://blpinsurance.com/default.asp?id=28>

¹² www.build-zone.com/range_of_structural_warranty_products.aspx

¹³ www.labc.uk.com/site/scripts/documents_info.php?categoryID=204&documentID=15

3.1 WARRANTIES - AN INTERNATIONAL REVIEW

Review of home warranty schemes operating in other countries

- 3.2 This section of the report offers commentary and analysis on a range of international new home warranty schemes operated in (in alphabetic order): Australia, Canada, Japan, France and the USA. Discussion as to how they compare vis-à-vis the UK is provided and was achieved via a combination of a desk study, electronic mail communications and in-depth analysis of a range of program operators in the international market places. The desk top study took place during November and December 2007, and January through February of 2008: the in-depth analysis took place during March 2008¹⁴.
- 3.3 Data was derived from the analyses of either home warranty providers or new homebuilders in the other comparison countries. With the limitations of time and budget, the review of new home warranties in each of the countries has been curtailed to a representative review of new home warranties operating in specific states/provinces/territories of each country for example, whilst Canada has 10 provinces and three territories, only the home warranty program operating in two provinces will be considered and taken to be representative of that country. This view was taken by the author because of the lack of coherence across the country and also the fact that the geographical areas could be considered as 'atypical' in that they have warranties that have been operating for a reasonable period of time. Similarly, the USA has fifty states and one district, of which one representative state will be considered. This approach is considered to be robust in that in some countries there is no 'national' driver of warranty approach nor single warranty scheme.
- 3.4 Table 3.1 shows details of the web addresses of the various warranty providers reviewed along with associated bodies that act upon or influence the new home warranty provider. A number of these website

¹⁴ A number (two) of the in-depth analyses, in both Canada and The USA, involved graduates of Glasgow Caledonian University who are active employees of organisations operating in the private sector housing and construction markets, of these two countries.

locations have been used to provide general background materials on each of the countries.

Table 3.1: Warranty providers, and associated bodies, in the selected countries

| Warranty providers, and associated bodies, in the selected countries | | |
|-----------------------------------------------------------------------------|--------------------------------------------------------------------------|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Country | Warranty provider/Associate | URL |
| Australia | Housing Industry Association | http://hia.com.au/ |
| | Australian Statistics Bureau | www.abs.gov.au/ |
| | Home Indemnity Insurance | www.docep.wa.gov.au/ConsumerProtection/PDF/Factsheets/home_indemn_insur.pdf |
| | Builders' Registration Board of Western Australia | www.builders.wa.gov.au/default.aspx?MenuID = 13 |
| Canada | National Home Warranty | www.nationalhomewarranty.com/main_2.asp?content_id = 85&prov = bc |
| | Tarion | www.tarion.com/home/ |
| | Home Protection Office | www.hpo.bc.ca/Builders/Insurers.php |
| | Canada Mortgage and Housing Corporation (CMHC) | www.cmhc.ca |
| France | The Canadian Homebuilders' Association: | www.chba.ca/ |
| | L'Agence Qualité Construction | www.qualiteconstruction.com/webzine/default.asp?main = 38 |
| Japan | Organisme Professionnel de Qualification et de Certification du Bâtiment | www.olacia.fr/fr/menu/rubrique_4/article_1.html |
| | Home Owner Warranty | www.how.or.jp/ |
| | The Building Center of Japan | www.bcj.or.jp/en/03/01_03.html |
| | Japan Architectural Education and Information Center | www.jaeic.or.jp/index_e.htm |
| The United | Ministry of Land, Infrastructure, Transport and Tourism | www.mlit.go.jp/english/2006/2006_pamphlet/index.html |
| | Building Guidance Division, Housing Bureau | www.mlit.go.jp/toukeijouhou/chojou/stat-e.htm |
| The United | Laws justia | http://law.justia.com/virginia/codes/toc5500000/ |

| | | |
|-------------------|-------------------------------------------|------------------------------------------------------|
| States of America | National Association of Homebuilders | 55-70.1.html www.nahb.org/ |
| | Department of Housing & Urban Development | www.hud.gov/offices/hsg/sfh/mhs/prod03.cfm |
| | New Jersey | www.state.nj.us/dca/codes/newhome_warranty/nhw.shtml |
| | US Census Bureau | www.census.gov/const/www/newresconstindex.html |

International new home warranty schemes

Australia

- 3.5 Australia is comprised of six States and two Territories, each of which is autonomous, and as such, the underlying approach to new home warranties is subject to variation from State to State.
- 3.6 Australia has enjoyed an increase¹⁵ in consumer awareness about claims relating to goods and services and also, of consumer rights, over the last few years¹⁶. However, in spite of increased education and awareness initiatives and considerable consumer protection legislation, it is still common for many new homebuyers to enter into contracts by a simple shake of hands¹⁷.
- 3.7 In an attempt to address these issues, State Governments have introduced a variety of laws that squarely put the onus on the homebuilder to be fair, by regulating Home Building Contracts and providing for Home Indemnity Insurance schemes, along with the licensing of homebuilders. In terms of volume of new home starts compared with

¹⁵ Williams, PG, Consumer understanding and use of health claims for foods, *Nutrition Reviews*, 63(7), 2005, 256-264.

¹⁶ www.expertguides.com/default.asp?Page=9&GuideID=165&Ed=69,
www.lexmundi.com/lexmundi/NewsBot.asp?MODE=VIEW&ID=508&SnID=2,
www.cavill.com.au/pages.asp?area=12&page=162

¹⁷ www.consumer.gov.au/html/home_builder/html/2Parts1-6.html

the UK, during the year to Dec 2007, Australia recorded some 104,349 private new home starts (ABS, 2008) whereas the UK recorded some 210,847 new home starts.¹⁸

- 3.8 In Western Australia, where 17,208 new homes were commenced during the year to December 2007, then in the majority of cases of new homebuilding, the home indemnity insurance policy must cover the building work during the construction period and for a further period of six years from the date of practical completion. Practical Completion is the date from which the new home was capable of being used for its intended purpose.
- 3.9 Before being allowed to carry out new home construction work worth more than Aus\$20,000 for themselves or others, except as a subcontractor to another builder, new homebuilders must fulfil basic criteria. These include: contacting their insurer to arrange home indemnity insurance (HII) cover for the new home, providing a copy of the relevant insurance certificate to the relevant local government authority in order to obtain the necessary building permit or licence, and, giving the new homebuyer the insurance certificate prior to asking for any money or performing any work under the contract to build the new home (Home Building Contracts Amendment Bill, 2002). Note that in other areas of the country the threshold value varies for example, work carried out by homebuilders/contractors valued at over \$12,000 in New South Wales, South Australia, Victoria and, Tasmania.
- 3.10 The presumption inherent in new home construction is that it will be carried out by a licensed or registered builder. Many of the States/Territories have legislated to ensure that only those homebuilders who are licensed and/or registered with an appropriate body actually carry out the construction work and the registration body takes a positive role in ensuring homebuilders follow good practice. Table 3.2 shows the Australian pattern on licensing of homebuilders and the provision of home indemnity insurances.

¹⁸ See Table 2.3 for annual values.

Table 3.2: Licensing and registration of homebuilders and home indemnity provision

| Licensing and registration of homebuilders and home indemnity provision | | |
|--------------------------------------------------------------------------------|-------------------------|---------------------------------|
| State/Territory | Licensing (date) | Home Indemnity Insurer |
| Australian Capital Territory | Yes (1924) | Private 1988 |
| New South Wales | Yes (1971) | Government 1973-96 Private 1997 |
| Northern Territory | Pending | Under Consideration |
| Queensland | Yes (1971) | Government 1979 |
| South Australia | Yes (1968) | Private 1986 |
| Western Australia | Yes (1939) | Private 1997 |
| Victoria | Yes (1995) | Government 1974-95 Private 1995 |
| Tasmania | Yes (2004) | Private 1993 |

3.11 As an example of a registration body, The Builders' Registration Board of Western Australia has a number of statutory functions including, to:

- determine the training for homebuilders seeking registration
- maintaining a suitable and accessible register of homebuilders
- issue certificates showing that a particular homebuilder holds registration
- undertaking proceedings for alleged offences against the Builders' Registration Act 1939 and the Home Building Contracts Act 1991
- carrying out the provisions of clauses contained within the Builders' Registration Act 1939, and,
- carrying out general homebuilding information and associated educational activities.

- 3.12 The Builders' Registration Board's of Western Australia has a set of strategic objectives which include: maintaining the highest possible standards within the building industry (which is not specifically restricted to the local industry), ensuring that those undertaking building activities in Western Australia comply with the provisions of the Builders' Registration Act 1939 and the Home Building Contracts Act 1991, and also, resolving building disputes efficiently, cost effectively and according to the prevailing law.
- 3.13 In addition to the above areas of activity, the Builders' Registration Board is required to provide administrative support to a body known as the Building Disputes Tribunal. This support includes meeting the relevant expenditure necessary for the effective functioning of, and collecting of any fees directly payable to, the Building Disputes Tribunal itself.

Building disputes

- 3.14 As noted above, in addition to the process of licensing homebuilders, a number of the States/Territories, including Queensland, New South Wales, Victoria and Western Australia, have introduced a novel feature by including 'Building Disputes Tribunals'. These are perceived as being quasi judicial Tribunals with varying powers to issue 'Orders' but with a clear emphasis centred on being low cost, non legalistic, quick, and a forum to determine workmanship and some contractual disputes that arise in homebuilding. The decisions (Orders) that emanate from the Tribunals are legally binding on the various parties and failure by the homebuilder to comply may result in cancellation or suspension of the homebuilder's licence to operate (in effect the removal of the ability to work) and/or a fine or prosecution in the relevant Local Court.

Home Indemnity Insurance cover

- 3.15 At the outset, H.I.I. was intended to be applied to all new homebuilding undertaken throughout Australia. However, recent activities by the insurance providers have lead to a number of exemptions for example, multi unit developments exceeding three storeys. The various State/Territory Governments have decided on an individual basis what

exemption, if any, should be given. However, home indemnity insurance has some basic features which are available across Australia.

- 3.16 The general cover that the new homebuyer can expect from an H.I.I. policy is for an agreed amount to complete the house or remedy defects in the event that their homebuilder dies, disappears or becomes insolvent and cannot complete these statutory obligations. Additional features are available within many of the home indemnity policies offered as 'standard' by the various providers. A number of the insurance provider's offer to tailor the policy to suit specific conditions/ new homebuilders.

Building audits

- 3.17 Insurers and the various licensing authorities have, in recent years, taken a greater interest in the new homebuilders' performance and will avoid insuring or licensing them unless the new homebuilder has provided adequate business information (trading and financial) and a robust and practical business plan.
- 3.18 Premiums payable by the new homebuilder are set accordingly, with costs varying widely due to each homebuilder's turnover, previous record of claims, location of the business and the work being undertaken, construction methods to be adopted, etc. In accordance with other warranty schemes operating internationally, new homebuilders consider that the limitations, and business enquiries, imposed by some insurers are too restrictive to allow for the flexibility that is to be found in the current new home market place¹⁹.
- 3.19 The following table (Table 3.3) provides a State/Territory review and breakdown of some of the characteristics and requirements of available homebuilder's warranty insurance.

¹⁹ Review of licensing in the NSW home building industry, Issues Paper, NSW Government, 2006.

Table 3.3: Insurance requirements and general features

| Insurance requirements and general features | | | |
|----------------------------------------------------|--------------------------|----------------------------------------------------------------------------------------------------------------------------------------|---------------------------------------------------|
| Feature | | | |
| State/Territory | Aus\$ value as threshold | Period of cover | Information source |
| Australian Capital Territory | 12,000 | Six years from the handover for structural defects and two years for non-structural defects. | Building Electrical and Plumbing Control (BEPCON) |
| New South Wales | 12,000 | Two years for non-structural defects and six years for structural defects or a period of 12 months for incomplete work. | NSW Office of Fair Trading |
| Northern Territory | Pending | Pending | Pending |
| Queensland | 3,300 | Six months from handover until 6.5 years from date of completion. | Building Services Authority |
| Tasmania | 12,000 | Six years after completion of work. | Consumer Affairs and Fair Trading |
| Victoria | 12,000 | Usually three months from handover until six years from the date of completion for structural defects and two years for non-structural | Building Advice and Conciliation Victoria |
| South Australia | 12,000 | Within five years from date the building was completed. | Office of Consumer and Business Affairs |
| Western Australia | 12,000 | Six years from the day of practical completion. The minimum statutory period for maintenance is four months. | Department of Consumer and Employment |

3.20 What can be seen from Tables 3.2 and 3.3 is that the national Australian picture is not coherent and even those geographic areas who share physical boundaries have differences in approach. The terminology varies from area to area and the 'on the ground' support for the implementation and enforcement of legislation differs.

Comparing Australia with the UK

3.21 Comparing Australia to the UK there are a number of clear differences in approach to the issue of quality in new homes and warranty provision. In Australia the predominance is for home builders to be registered and only these registered builders may construct new homes. In the UK, the homebuilder may see registration as advisable, but they are not required to do so since there are other mechanisms by which to obtain warranty cover, other than through the recognised new home warranty providers. In Australia, new home warranty insurance is provided by a number of private organisations, with no single organisation appearing to act as the focus for this provision. The Registration Boards, where operating in an Australian state/territory, act to ensure good practice is followed by the homebuilder and that disputes are resolved swiftly, economically, and in a fair manner. The Australian warranty insurance providers also actively monitor the homebuilder's performance as a means to gauge the desirability, or otherwise, of the homebuilder's insurance application. The Australian home warranty insurance providers offer cover under the umbrella of an agreed amount of money to complete the house, or remedy defects, in the event that their homebuilder dies, disappears or becomes insolvent and cannot complete these statutory obligations: in the UK, the new home warranty is a more detailed document.

Canada

3.22 'New home warranty programs across Canada are a hodgepodge of provincial systems that offer Canadians inconsistent protection if something goes wrong with what is often the most expensive purchase of their lives', according to research conducted and released by the Consumers Council of Canada (Friedland *et al.*, 2007).

- 3.23 The picture on new home warranties in Canada is complex and not readily understood. Canada's Office of Consumer Affairs (OCA) sees the need to determine the broader national picture and arrive at consistent cover across Canada.
- 3.24 Homebuyers who attempt to resolve building defects must find their way through a number of areas: the complexities of the warranty and its associated regulations, and the underlying construction standards imposed by the various provincial building codes. Nationally, the picture on homebuyer protection is uneven since each provincial or regional warranty scheme, generally, acts independently of the other, although there are now schemes which attempt to cover much broader geographical areas.
- 3.25 New Home Warranty schemes operating across the various provinces in Canada are essentially creatures of their individual provincial chapter of the Canadian Home Builders' Association (CHBA). Most were established in the early-mid 1970's as marketing tools and still remain under the influence of their provincial branch of the CHBA. There is an entity within the CHBA called the National Home Warranty Council, however, it has no authority over the individual warranty schemes, though they meet several times a year to exchange information on topics of mutual interest or concerns to warranty scheme operators.
- 3.26 CHBA sees itself as the voice of the homebuilding industry in Canada. They are recognised for their technological know-how, and highly regarded for supporting an innovative spirit, upholding the quality of new homes, and a commitment to support the business success of members. They also support their members' ability to provide affordability and, choice for consumers.
- 3.27 CHBA works to support the view that all Canadians have the right to decent, safe and appropriate housing. To this end, it supports and encourages the professionalism of its members by providing members with opportunities to learn, grow (and take pride in achievements). Two of its member organisations are National Home Warranty (operating in British Columbia and neighbouring provinces), and Tarion (who operate

mainly in Ontario), discussion on each of these organisation's new home warranty schemes follows.

British Columbia – Overview of National Home Warranty

- 3.28 New home warranty schemes operating in British Columbia come under the regulation of the Homeowner Protection Office (HPO). HPO are responsible for establishing the framework for, and monitoring the provision of, mandatory third-party home warranty insurance within the province of British Columbia.
- 3.29 The Homeowner Protection Office (HPO) is a provincial Crown²⁰ corporation formed as a direct result of the recommendations within the Barrett Commission's²¹ report (1998) on the quality of condominium construction in British Columbia.
- 3.30 The report prompted the development of the Homeowner Protection Act which was passed on the 28th July, 1998, with its main purposes being the strengthening of consumer protection for homebuyers of new homes and improving the quality of residential construction in British Columbia. The Act specifically provided for the creation of the HPO which officially opened on 1st October, 1998.
- 3.31 The HPO is responsible for a number of areas including: homebuilder licensing and establishing the framework for and monitoring the provision of mandatory third-party home warranty insurance, administering a relief

²⁰ In Canada, a Crown Corporation is a wholly owned federal or provincial organisation that is structured like a private or independent enterprise. They are established to carry out regulatory, advisory, administrative, financial or other services or to provide goods and services to a range of end users. Crown corporations, on the whole, enjoy greater freedom from direct political control than, what may be seen as 'normal', government departments. Crown corporations are ultimately accountable for their affairs, through a Canadian minister, to the Canadian Parliament.

²¹ Barrett, D. *The Renewal of Trust in Residential Construction: Commission of Inquiry into the Quality of Condominium Construction in British Columbia*. June 1998.

grant for buyers of leaky homes, and, a research and education function designed to benefit the residential construction industry and consumers. Homebuilders operating within British Columbia must be licensed by the HPO and arrange for suitable home warranty insurance before they can obtain a building permit. A searchable database of Licensed Residential Builders and building envelope (the visible external structure) renovators is available to the public for searching, on the HPO website²².

Home Warranty Insurance

- 3.32 New homes constructed by a licensed new homebuilder are required to be covered by defect warranty insurance comprising two years on labour and materials (some limits apply), five years on the building envelope (including water penetration) and 10 years on the structure of the new home (collectively known as 2-5-10 year home warranty insurance).
- 3.33 Home warranty insurance may only be provided by insurance companies approved and regulated by the Financial Institutions Commission (FICom). The HPO maintains regular contact with these insurance companies and their agents/brokers, in order to communicate concerns, share information, work on streamlining and standardising processes, and generally ensure that home warranty insurance is a viable and effective system for homebuyers, homebuilders, and insurance companies alike²³.

National home warranty

- 3.34 National Home Warranty (National), a for profit organisation²⁴, operates under the watchful umbrella of the HPO and serves a broad swathe of western Canada (including, in alphabetic order, Alberta, British Columbia, Manitoba, and Saskatchewan) with a new home warranty scheme operating since 1990. Currently, National claim to have more than 3,500

²² www.hpo.bc.ca/Consumer/index.php

²³ As of 18 March 2008, there were four companies offering home warranty insurance in British Columbia: www.pacificwarranty.com/, www.lombard.ca/, www.nationalhomewarranty.com/, www.travelersguarantee.com/.

²⁴ nationalhomewarranty.com/main.asp?content_id=5&prov=main

registered homebuilders and provide new home warranty coverage for an estimated 27,000 homes and condominium units in western Canada, in 2006. The general features of this new home warranty scheme are as follows:

- One year's cover against defects in materials and labour.
- Two year's cover against defects in the major systems in the new home and the exterior cladding.
- Five year's warranty for any building envelope defects,
- A ten year warranty for any structural defects.
- If the new homeowner is required to move out of the new home while repairs are being made, then National will cover reasonable expenses to a maximum of daily figure.

3.35 These provisions within National's warranty scheme fit quite closely with others in Canada in that they follow the pattern of:

- Year one covers: most defects in materials, design and labour.
- Two year's cover for: any defect in materials and labour supplied for the electrical, plumbing, heating, ventilation and air conditioning delivery and distribution systems, along with any defect in materials and labour supplied for the exterior cladding, caulking, windows and doors that may lead to detachment or material damage to the new home, and also, any defect in materials and labour which renders the new home unfit to live in.
- Five years of cover for: defects in the building envelope of a new home including a defect which permits unintended water penetration such that it causes, or is likely to cause, material damage to the new home.
- 10 years of cover for: any defect in materials and labour that results in the failure of a load bearing part of the new home, also, any

defect that causes structural damage that materially and adversely affects the use of the new home for residential occupancy.

What National offer as part of their service

- 3.36 National's inspectors work with homebuilders aiming to identify and resolve problems before they are 'built into' the structure, conducting reviews of plans and specifications before a multi-family project (where more than one family live in the building for example, a block of flats) is actually registered with the warranty provider. This process allows National to assess the risk potential in the ground and site conditions, general design of the new home, building envelope, building materials and other project components that will go together to form the new home. The findings from the review of the proposal are shared with the industry professionals working on the particular new home. National's inspectors undertake a series of inspections throughout the building process to ensure the new home meets building code requirements as well as National's own standards.

Building disputes

- 3.37 There is provision within the regulations for third-party mediation of disputes between new homebuyers and the warranty providers. This process can be initiated at the sole option of the new homebuyer and the process is performed independently of the Homeowner Protection Office.

Ontario: Overview of Tarion Warranty Corporation

- 3.38 Tarion Warranty Corporation (formerly called the Ontario New Home Warranty Program) ('Tarion') was set up in 1976 as a private, not for profit corporation administering the Ontario New Home Warranties Plan Act. It must be noted that Tarion is not a government body, crown agent or public insurance body and it receives none of its funding from government sources. The funding it does receive is entirely from homebuilders who are registered, renewal fees and new home enrolment fees (Tarion, 2006).

3.39 Tarion provides for mandatory and universal coverage for all new homebuyers whether or not the homebuilder is registered or the home is enrolled with Tarion. For the sake of cohesion, the responsibility for new homebuilder licensing, registration, conciliation and financial compensation is passed to this single entity. The intent of the New Home Warranties Act was to create a consumer protection scheme designed to protect homebuyers from incompetent²⁵ or financially irresponsible vendors and homebuilders, and also to avoid expensive multi-party law suits.²⁶

3.40 Tarion is charged with registering new home sellers and homebuilders, enrolling new homes, investigating illegal homebuilding practices, resolving warranty disputes between homebuilders and new homebuyers, and promoting high standards of construction among new homebuilders. Also, Tarion works with the new homebuilders to help educate new homebuyers about their warranty rights. Under the New Home Warranties Act Tarion discharges three important roles:

- Regulator: Tarion registers homebuilders, imposes terms and conditions on registration, such as security requirements and limits on the number of homes that may be built, and is able to revoke registrations.
- Surety: Tarion maintains a robust guarantee fund with which to pay claims and/or arrange for necessary repairs when homebuilders fail to comply with warranty obligations under the Act, and,
- Conciliator/Adjudicator: Tarion acts as conciliator in disputes between new homebuilders and homebuyers, and determines the validity of claims made under the warranty.

3.41 Under the New Home Warranties Act the statutory warranties provided to the new homebuyer are, generally, as follows:

²⁵ www.bdale.com/warranty.htm

²⁶ www.allaroundthehouse.com/lib.vw.na30.htm

- One-year warranty: that for one-year from the date of possession, the home is free from defects in work and materials, fit to live in, and, constructed in accordance with the Ontario Building Code.
- Two-year warranties: that for two years from the date of possession the home is free from water penetration through the basement or foundations, free from defects in the building envelope, such as caulking, windows and doors, that result in water penetration, free from defects in work and materials in the electrical, plumbing and heating delivery and distribution systems, free from defects in work and materials which result in the detachment, displacement or physical deterioration of exterior cladding, and, free from violations of the Ontario Building Code's health and safety provisions.
- Seven-year warranty: that for seven years from the date of possession the home is free of major structural defects, which is defined as, any defect in work or materials that results in failure of a load-bearing part of the home's structure, or that materially and adversely affects its load bearing capacity, or, any defect in work or materials that materially and adversely affects the use of the home for the purpose for which it was intended.

Tarion as Conciliator/Adjudicator

- 3.42 Tarion acts as conciliator in disputes between new homebuilders and the homebuyers and determines the validity of warranty claims. When a claim is made by a homebuyer, the homebuilder is given a reasonable opportunity to make good defect: if the homebuilder does not address the problem, then Tarion conducts an inspection of the complaint to determine if it is justifiable. If the problem is upheld, the homebuilder is ordered by Tarion to address and make good the defect. If this work is not executed within a relatively short period of time, then Tarion will step in to resolve the problem directly.
- 3.43 In 2003, Tarion introduced the new Customer Service Standard, which provides for minimum after-sales warranty standards and repair timelines that Tarion requires from homebuilders. They, uniquely among warranty

providers, perhaps for the sake of clarity and ease of use, provide a ready-reckoner that all interested parties can scan in order to calculate the cost of the warranty for each new home.

Comparing Canada with the UK

- 3.44 The picture on home warranties across Canada can be described as mixed. There are Provinces which clearly are setting a path for others to follow but the national view is still piecemeal. Quality in the new home may be seen to be driven by the licensing of homebuilders and the mandatory requirement for a new home warranty. There is a range of for, and not-for, profit organisations who provide warranties. Canadian warranties follow a similar pattern to that found in the UK, in that the period of cover provided by the warranty changes for varying parts of the building for example, five year warranty for building envelope defects, and 10 years for structural defects. Canada differs from the UK in that disputes relating to the new home are dealt with by an independent body. CHBA and the National Home Warranty Council provide advice and technological support to the homebuilders but are not regulatory or registration bodies. In the UK the warranty providers set technical standards which the homebuilders must comply with. In Canada a ready reckoner is provided for all parties to scan and calculate the cost of the warranty for each new home. This practice is not followed in the UK.

France

- 3.45 Historically, (from the time of Napoleon), France has benefited from a code which enshrined the concept of liability for defects, and supported the remediation of defects in buildings. In essence, the code laid out that should the whole or part of a building fail to function as intended, because of a defect, then the architect or homebuilder would bear an absolute liability for 10 years, they could not be absolved of this liability for any reason. The Code was revised in 1967 and the liability period was shortened to two years except for structural defects.

- 3.46 The approach prevailing from 1967 onwards lacked a robust inspection regime and the building permit provided by the public authority only assessed conformity with planning rules, and did not include any technical validation of the design of the works. As such, even though consumer protection frameworks were well developed, they did not help decrease the incidence of defects nor improve the remediation of these defects²⁷. The intention of the 1967 changes did not bring about the protection expected, with the result that the homebuyers suffered from both the defects and the costs resulting from litigation to have the defects remedied.
- 3.47 As a solution to the problem, the Spinetta Law was introduced in 1978²⁸, aimed at reducing the occurrence of defects, prompting the homebuilder to carry out necessary repair works, and clarifying the responsibilities of each of the construction and design professionals involved in the new build. The Spinetta Law introduced significant changes to the building process, with the following being the key areas: identification and clarification of liabilities, introduction of a formalised inspection regime, and, restructuring of appropriate insurance indemnity schemes. This law has subsequently been amended by Order No. 2005-658 (June 2005) clarifying the meaning of certain words and the application of the compulsory insurance for example, the term 'building work' has been replaced with 'construction work'(construction being a broader term and seen to include work on the buildings themselves), and a list of excluded structures added for simplification. The amendments also brought sub-contractor's liability into line with those of the main contractor.

²⁷ See for example: Prais, S.J., Steedman, H. (1986) Vocational Training in France and Britain: the Building Trades, National Institute Economic Review, Vol. 116, No. 1, 45-55, Paterson A. C. (1984) Presidential address. The Structural Engineer, 62A, No.11, 335-342, Turner, G. (1995) Latent defects liability and 'build' proposals and insurance considerations for commercial, retail and industrial property Structural Survey, MCB University Press, Vol. 13 No. 4, pp. 13-15, and, Knocke J. (Ed.) (1993) Post-construction Liability and Insurance E & F N Spon, London.

²⁸ The law of 4 January 1978 (Loi Spinetta) on liability and insurance in construction introduced compulsory insurance against construction risks to cover repairs of damage 'within a ten-year period' to building work: the building works were not defined in terms of their nature i.e. whether for new homes or office or factories. Spinetta was reformed with Order No 2005-658 of 8 June 2005 published in the Official Journal on 9 June 2005.

Overview of the system under the Spinetta Law

- 3.48 The Spinetta Law provides that all parties engaging in construction work are held liable, for a period of 10 years, for damage to the structure of the building. In conjunction with this 10 year liability period, they are also liable for a period of two years for other construction works, materials and elements for example, the heating system, of the building. The law provides that both of the liability periods cannot be expunged²⁹ that is, the responsibility can not be passed to another or ended.
- 3.49 The warranty commences when the building is handed over: if after handing over the building a defect is found, then the homebuilder is liable for one year from completion of the works. The Spinetta Law is unclear as to the definition of what constitutes a warrantable defect or damage, with the final decision on such matters being left to the courts. The Spinetta Law also fails to clearly define what is meant by terms relating to damage, the application of the 10-year warranty for damage to 'solidity' of the building is limited to areas relating to 'critical' or 'major damage', but these are not defined. The evaluation of degree of damage that is, extent and cost implications, is once again left to the courts to decide upon.

Double Compulsory Insurance System

- 3.50 Both the client that is, the person commissioning the new building, and the design / construction team provide insurance cover for the works to the Architect or responsible person employed to oversee the new build, and thus the general construction costs in the French construction

²⁹ Booth, A. (2008) Architect RIBA DUAOB Inscrit au Tableau Regional de l'Ordre des Architectes de Basse-Normandie au titre d'Architecte (Diplome de l'University d'Architecture Oxford Brookes) No. general 49004 regional 731 11 Rue de la Ville, 50480 Brucheville <http://brittany.angloinfo.com/countries/france/build.asp>

industry are greater than the cost of similar works in the UK³⁰. 'This insurance is not cheap, costing several thousand euros for the construction of a new house or wholesale renovation of a dilapidated property'.³¹ All liabilities, except criminal responsibility, are deemed to be insurable and, generally, it is the insurance companies of the parties that is, the client, design or construction team, involved in the new build home who settle any disputes which arise. The Spinetta Law requires that all parties to the construction process have in place appropriate insurance before construction work actually begins, if an architect is employed, then it is their responsibility to ensure that the person commissioning the new build, the contractors, the subcontractors and the various suppliers all have adequate insurance in place. The client is required to insure against responsibilities for a period of 10 years and a policy known as Dommage Ouvrage (DO) is put in place to provide such cover, the DO being available on a project by project basis.

- 3.51 The Spinetta Law ensures that no monetary limit is attached to the value of claims made under this type of policy, so that the insurance will always be able to meet any claim made under the policy and be able to fund the cost of any works required to complete the project. Defective work is repaired immediately (under the insurance), in order that the claim may be settled between the insurance companies of the parties concerned.
- 3.52 The premium to be charged for policies operating under the double compulsory insurance system that is, both the person commissioning the building works and the team doing the design and construction, provide insurances, and the premia for these policies is governed by a Central Premium Rate Committee which makes the final decision regarding insurance premia to be charged.

Inspection of works

- 3.53 The new home inspector is perceived by the homebuyer, the homebuilder and the design team, as being independent, and checks the construction

³⁰ www.totalfrance.com/france/fiches.php?fiche_id=40

³¹ www.french-property.com/guides/france/building/new-build/defect-guarantee/

works not only from the design stage but through the construction stage as well. There are technical standards to be followed, but these are not mandatory, simply recommended, although inspections are based on these standards.³² There is a fee for these inspections with the inspection fee being borne by the homebuyer: the inspection company is then held liable for defects etc., for a 10 year period, the same as the homebuilder.

Quality Control in new homebuilding

- 3.54 As a result of fluctuations in insurance cost, L'Agence Qualité Construction (AQC) was established in 1982 with the aim of preventing defects as well as improving the quality of homebuilding. AQC is composed of some 41 bodies representing government, homebuilding professionals, homebuilders' associations and representatives of other relevant organisations. The principle activities of AQC include undertaking relevant statistical analyses and disseminating findings. It also provides information on incidents and events of building defects and claims, both recent and historic.
- 3.55 New home warranties in France are seen as a general insurance matter, and as such there are a significant number of organisations who offer the range of insurances required.

Comparing France with the UK

- 3.56 Unlike the UK, France has legislation which prohibits those involved in providing the new home from escaping responsibility for defects and requires insurance for the new home. France also has clarified responsibilities within the legislation, which is a feature not seen in the UK. Insurance cover is provided by all parties (including sub-contractors) involved in building the new home in France, whereas in the UK only the principal homebuilder offers a warranty. Under the French approach there is no monetary limit to a claim, whereas the UK approach is to set limits within the warranty. There are technical standards to be followed in

³² Smith, D (2007) Presentation to IBCI Building Control conference, County Clare, March, www.i-b-c-i.ie/docs/conferences/2007/Smith.pdf

France (not provided by the warranty companies) but these are only recommended: the UK warranty providers see their technical standards as mandatory. Defective work is addressed quickly within France and the eventual costs settled amongst the insurance providers: the UK approach is to apportion blame and wrangle over the costs. France, unlike the UK, has a dedicated quality agency that seeks to reduce defects in new homes and ensure that new homes are well built. Much of the resolution of claims within France and the definition of what constitutes a defect, are left to the courts to decide.

Japan

- 3.57 The Building Standard Law of Japan (BSL) received its first major revision for over 30 years in 1998 (the revision of the BSL came into effect in May 1999), with subsequent amendments in 2004 and 2007. The changes consisted of: specification of interim and final building inspections, and, transformation of the BSL from a specification-based building code to a performance-based building code. This change sought to move the BSL from a series of prescribed, or acceptable, solutions, to a series of more open and subjective objectives and requirements.
- 3.58 The BSL requires that all homes undergo interim and final inspections during construction. The interim inspection must be completed before a building is eligible to receive its final inspection. To provide guidance to inspection organisations, a qualification system and standards have been established within the revised BSL.
- 3.59 The second revision, in 2004, saw the BSL move from being a specification-based standard to a performance-based standard. In addition to revising the BSL, the Housing Quality Assurance Law, 2000³³ was enacted to provide homebuyers with specific mechanisms to resolve disputes with building contractors. Subsequently, HQAL and Japan Housing Performance Indication Standards (2004) moved the process further towards ensuring homebuyers could be assured of high standard

³³ http://211.133.243.132/en/03/01_03.html

new homes. These standards being achieved through a 10-year warranty on defects on principal structures, a Housing Performance Indication System which looked at nine performance areas, and also included the establishment of housing dispute resolution bodies.

3.60 The objectives of the HQAL were to: improve the quality and performance of homes, provide homebuyers with a mechanism for resolving disputes with their builders, establish a set of 'Housing Performance Indication Standards' against which specific homes could be compared (that is, benchmarks).

3.61 The HQAL came into force in 2000 and ostensibly was designed to protect the consumer. The Act incorporated two important functions: one was the introduction of an enforcement mechanism, on the homebuilder or seller, of newly constructed homes, for a 10-year defects liability period, the other was the establishment of a Housing Performance Indication System and the setting up of a Housing Dispute Resolution System for homes falling within the remit of the system. The 10-year liability system and Performance Indication System was based on the around the system in France. There are, however, significant differences between the French and the Japanese systems: first, the 10-year liability period in Japan can not be passed on to successive homeowners. Secondly, the French requirement for homebuilders, sellers, designers or anyone else who may be liable for defects to have insurance cover is not enacted. It applies only to homebuilders or sellers who build or sell the new home and covers defects of structural performance and waterproofing elements for example, the roof. The new home builder can not contract out of their liability: the liability for other miscellaneous defects is defined in the Civil Code³⁴ and other statutes.

3.62 With the enforcement of the HQAL, so the need for robust new home warranty systems became ever more prevalent. The Organisation for Housing Warranty (OHW) and other housing organisations and private companies emerged to fill the gaps as home warranty providers. These

³⁴ Japan Civil Code: the body of private law adopted in 1896 that, even after post-World War II modifications, remains in effect in present-day Japan.

new warranty providers include OHW, Houseplus Corporation Inc., Japan Federation of Architects & Building Engineers Association, Japan ERI Company, Limited, and others.

OHW Warranty for new homes: registration of homebuilders

- 3.63 Organisations selling new homes should be registered with OHW as a registered homebuilder in order that they may access the warranty scheme cover. Any homebuilder may be eligible for registration: the actual application for new home registration should be submitted to the representative organisation of OHW in the locality where the home is to be built (registration is normally executed some time between the issuance of the construction permit and commencement of the actual construction work). Where the home is being built for sale, then agreement will be reached between the sales agent and the homebuilder as to which of them will submit the application.
- 3.64 Warranty coverage, after home completion, has two main parts: the long-term warranty which is for a period of 10 years, covering major structural components and parts (for example, cladding) used to prevent rainwater leakage (as defined in the HQAL), and, a short-term warranty which exists for a period of between one and two years and covers items such as: paintwork, deformation (distortion from the original shape) of fittings, leaks in bathrooms, and defective equipment for example, air conditioning units.

Dispute settlement

- 3.65 Any dispute between the new homebuyer (of a registered OHW house) and the registered homebuilder over a defect in the house can be referred to the Technical Committee (of OHW), consisting of lawyers and construction specialists, for resolution.

Comparing Japan with the UK

- 3.66 The warranty providers in Japan operate under a performance based approach whereas in the UK there is still a reliance on a specification

based approach to quality in new homes. Japan has a series of new home benchmarks which are not found in the UK. The housing dispute resolution system in Japan differs from the UK.³⁵ Japan does not allow transfer of the warranty to subsequent home owners whereas in the UK this practice is the norm.

The United States of America

3.67 The picture with regard to home warranties in the USA is very similar to that found in Canada that is, each autonomous region has its own peculiarities and since there is no federal legislation covering home warranty insurance, it is left up to the individual states to implement the form of control they may feel is appropriate implementing. On a national basis, there appears to have been a reluctance to apply mandatory controls, with the exception of a few states for example, New Jersey and Louisiana, (other states for example, Washington, have drafted bills relating to new home warranties that is, Senate Bill 6385, but rejected the proposal). There are implied³⁶ (by reference to other state and federal legislation) warranties for completion of a habitable dwelling and correction of defects by homebuilders. The United States has also a general statute of limitations of around 10 years on claims for compensation for major structural faults in new homes. There are associations such as the National Association of Home Builders (NAHB) which provide advice to homebuilders for example, *Warranties for Builders* (Jaffe *et al.*, 2007) which provides homebuilders with guidance on the operation of home warranties and how to manage customers. NAHB do not get involved in registering their members nor providing warranty services. New home warranty insurance is freely available through numerous intra and inter state providers such as (in alphabetic order): Bank of America, First American, Fidelity, Home Warranty America, Quality Builders Warranty Corporation, US Home Warranty, etc.

³⁵ www.dced.state.ak.us/oed/forest_products/pub/tree12c.pdf

³⁶ www.Law.justia.com

New Jersey Home Warranty Legislation

- 3.68 Within the state of New Jersey, the New Home Warranty and Builders' Registration Act, enacted in 1977, aimed to provide a broad scope warranty provision for new homes and establish standards of construction and quality of the structural elements and components of the new homes for example, workmanship, materials, plumbing, electrical and mechanical systems, appliances, fixtures and equipment and major structural elements. The state law requires new homebuilders to register with the State of New Jersey before starting construction of any new home and before offering a warranty on any new home bought or sold in the State.
- 3.69 The Act³⁷ and relevant regulations include a provision for a limited 10 year warranty which covers defects in materials, workmanship and various systems in a new home. Homebuilders are required to warrant each new home and to provide warranty follow up services for example, repairing defects. In the event the homebuilder does not repair defects where the homebuilder has been found responsible the state New Home Warranty Program, then the State New Home Warranty Security Fund will act to cover the cost of making good these repairs. Also, the Act provides for a process through which the homebuilder and the homebuyer can resolve disputes over defects. If the homebuilder is found to be negligent and/or does not participate in the prescribed dispute settlement process, then the homebuilder's registration can be suspended or revoked, thus effectively preventing the homebuilder from building new homes in New Jersey.

Registration and cover

- 3.70 All homebuilders of owner occupied new homes, including single family, town house, duplex (two family), cooperative, condominium, factory built and modular residences are required, by the act, to register with the 'new home warranty insurance program'. The liability of the new homebuilder under a warranty is restricted to the purchase price of the home in the first good faith sale or the fair market value of the home on its completion

³⁷ http://egov.oregon.gov/DCBS/CCTF/docs/041106_exhibit_25_cctfstaff.pdf

date. During the first year of a new home's warranty, warranty cover extends to: defective systems, workmanship, materials, plumbing, electrical and mechanical systems, appliances, fixtures and equipment and major structural defects. From the commencement date of the warranty to two years from that date, the homebuilder is responsible for the mechanical, electrical and plumbing systems and major structural defects. During the period from years three through to 10, only major structural defects are covered.

- 3.71 A homebuilder who is registered with the state New Home Warranty Program must also enrol in a warranty insurance plan. This may be with the State Plan offered by the 'new home warranty program' or one of the numerous private warranty plans approved by the 'new home warranty program' (currently six are approved³⁸). Plans must offer the same warranty coverage as that required by the Act and performance standards that are specified in the new home warranty and Builders' Registration Act regulations apply for all such approved plans³⁹. The U.S. Department of Housing and Urban Development (HUD) approves 10-year warranty programs based on a set of guidelines they have developed⁴⁰. Whilst there has been movement towards a uniform warranty this is still not a reality in the USA.

Comparing the USA with the UK

- 3.72 In the USA there is no country wide approach to home warranties and mandatory controls appear to be far from the minds of the legislators. Individual states enact legislation to protect new home buyers and the setting up of home warranty programs, which require homebuilders to register before construction of the new home begins. The homebuilder's liability is restricted to the purchase price of the new home which differs from the practice in the UK. Homebuilders may purchase home warranty insurance from the state or from a number of private organisations: this

³⁸ www.state.nj.us/dca/codes/newhome_warranty/warplans.shtml.

³⁹ New Jersey Administrative Code 5:25

⁴⁰ www.hud.gov/offices/hsg/sfh/ins/hoctenyr.pdf

differs from the UK approach in that local government in the UK does not offer home warranties.

International comparison of the warranties

- 3.73 The following table, Table 3.4, summarises some of the main features of a range of the warranties available in each of the countries and states, discussed above. The table also illustrates the requirement for homebuilder registration and warranty provider approval.
- 3.74 What emerges from the international review is that there is a degree of commonality in the period of cover provided by the various warranties and the general building elements for example, roofs, walls, weatherproofing, and components for example, heating systems, included within the policy coverage. The countries considered also tend to agree on the need for registration of homebuilders and approval of warranty providers. The noticeable exception is the UK, where no such registration of homebuilders is required: warranty providers in the UK normally need only seek approval from CML, but not registration with them. Homebuilders do register with NHBC, but alternative approaches to securing release of mortgage funds are available to them for example, through the use of surveyors or architects certificates.
- 3.75 There is also a general movement towards provision of independent dispute resolution, with the UK again being the exception to the general trend. The independent resolution, in these other countries, is usually carried out by a range of tribunals, and stand-alone bodies.
- 3.76 The calculation of the home warranty premium to be paid is, in most cases, a market driven activity. The exceptions noted being Canada and France: Canada has a 'ready reckoner' available which makes the process of calculation clearly visible and open, and France has a central body which acts to ensure that the fees payable are realistic and value for money.
- 3.77 When the warranty has been issued the pattern that emerges with regard to transferability, is that most countries allow subsequent

homeowner to enjoy the cover provided by the warranty up until its expiry. The exception is Japan.

Table 3.4 Comparison of country specific warranties

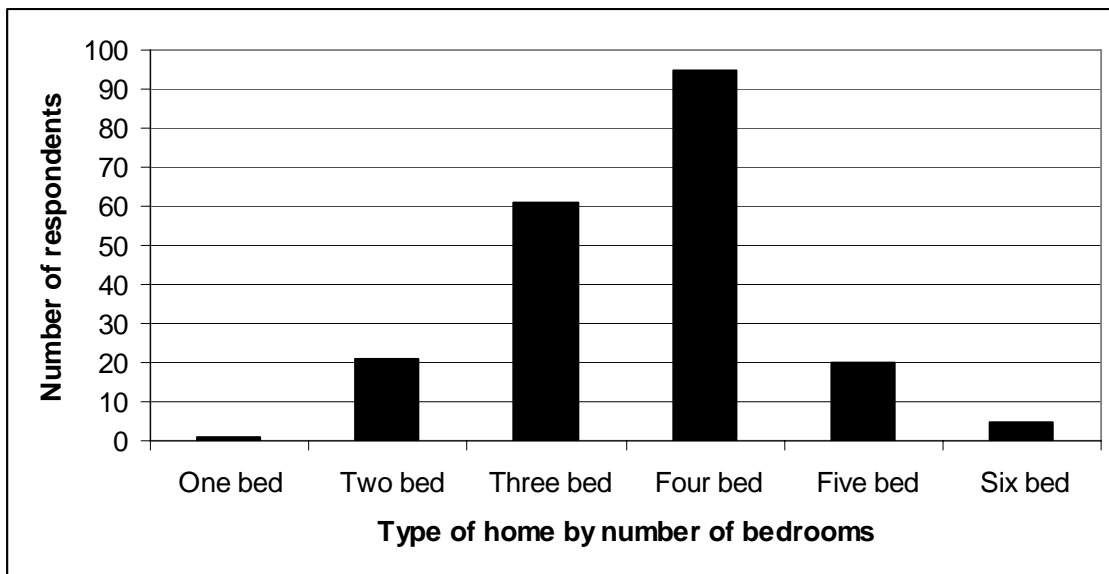
| Comparison of country specific warranties | | | | | |
|------------------------------------------------------------------------------------|-----------------------------|--------------------------------------------------------------|--------------------|---------------------------------------------------|----------------------------------------------|
| Country | Warranty period | Homebuilder/warranty-provider approval/registration required | Premium calculator | 3 rd Party dispute resolution facility | Warranty able to be passed to next homebuyer |
| Australia | two – six years * | Homebuilder and warranty provider | n.a. | Yes | Yes |
| Canada | One, two, five – 10 years * | Homebuilder and warranty provider | Ready reckoner | Yes | Yes |
| France | two – 10 years | Homebuilder | Central body | Yes | Yes |
| Japan | two – 10 years | Homebuilder | n.a. | Yes | No |
| UK | two – 10 years | n.a. | n.a. | n.a. | Yes |
| USA | one, two – 10 years ** | Homebuilder and warranty provider* | n.a. | Yes * | Yes |
| * varies from region to region. ** time period varies with the item being covered. | | | | | |

RESEARCH FINDINGS ON UK WARRANTY MATTERS

General data on the composite responses to the fieldwork

4.1 From data extracted from within Table 5.3 of the Annual Abstract of Statistics (ONS, 2007) the population of the UK is divided into 49 per cent males and 51 per cent females: within this research the respondent split on a gender basis was 55 per cent male and 45 per cent female. The length of tenure in the new home varied, with the minimum being one month and an average occupation of the new home of 18 months. These new homebuyers were located in diverse geographic regions of the UK (see Figure 1.1) and the distribution of house types are as shown in Figure 4.1.

Figure 4.1: Distribution of newbuild home types bought by respondents to the postal questionnaire (respondents = 204)



How significant a consideration are warranties when homebuyers are purchasing a newly built home?

- 4.2 The focus groups responses provide a range of reasons why people buy a new home and the questionnaire responses provide an insight into the significance of the warranty in the process that is buying a new home. Table 4.1 shows the underlying reasons as to why they bought their new home.

Table 4.1: Reasons given for buying a new home

| Reasons for buying a new home | | |
|-------------------------------|---------------------|----------------------------------------------------------------------------|
| Driver | Category | Reason |
| Lifestyle | Relationship | New, split, bereavement |
| | Family | Be closer to, be farther from |
| | Children | New one arriving, leaving home |
| | Type change | Flat, terraced, semi, detached, down-size, retirement |
| | Community | Leisure facilities, shops, schooling, transport |
| | Neighbours | New, fall out |
| | Health | Dentist, doctor, specific need, other |
| | Utility | Layout, age, space, on-costs ⁴¹ , value, garden, able to extend |
| | Nomadic | |
| | Inheritance | |
| Monetary | Jones ⁴² | Beating, keeping-up |
| | Deal | |
| | Investment | Long term, extra cash |
| | Rental | |
| | Location | |
| Work | Repossession | |
| | Income | Increase, decrease |
| | Age | |
| | New job | |

⁴¹ On-costs are the payments made by the homeowner, after the purchase of the new home, to heat, maintain, and repair it.

⁴² Keeping up with, or exceeding, the neighbours in terms of purchases, life style, etc.

- 4.3 It has to be emphasised that no single reason came through from the responses as the principal or largest driver of new home purchase⁴³. The responses (204) to the postal questionnaires may be perceived as small when compared to the number of new homes registered and completed each year (see Table 1.3). However, from the 204 responses to the questionnaires it is possible to derive a set of findings which help inform as to the views and position of the new homebuyer in the market place.
- 4.4 The respondents to the postal questionnaire were asked if they expected the new home to have a warranty, 99 per cent answered 'yes'. When asked why they expected the new home to have a warranty, the respondent was offered a choice of seven possible answers as shown in Table 4.2, with Table 4.3 showing the split of responses by gender. The seventh possible answer in Table 4.2 was 'none of the above, other' which elicited such a low response rate as could be considered negligible.

⁴³ A much greater timeframe and wider sample size would be required in order to establish the broader underlying patterns.

Table 4.2: Reasons for the warranty

| Reasons for the warranty | |
|---------------------------------------|------------------------------------|
| Possible answer | No of respondents agreeing* |
| The builder said it would have one | 72 |
| A warranty ensures standards | 51 |
| A warranty gives peace of mind | 51 |
| A warranty ensures quality | 27 |
| A warranty was required by the lender | 11 |
| It's the normal practice | 133 |
| Other | 6 |

Note * Respondents were able to select more than 1 possible answer, base count 195, postal questionnaire.

Table 4.3: Reasons for the warranty by gender

| Reasons for the warranty | | | | | | |
|---------------------------------|-------------------------------------------|-------------------------------------|---------------------------------------|-----------------------------------|-----------------------------------------------|---------------------------------|
| Gender | The builder said it would have one | A warranty ensures standards | A warranty gives peace of mind | A warranty ensures quality | A warranty was required by your lender | It's the normal practice |
| Female | 30 | 24 | 25 | 16 | 7 | 62 |
| Male | 42 | 27 | 26 | 11 | 4 | 71 |

Note * Respondents were able to select more than 1 possible answer, base count 195, postal questionnaire.

4.5 The largest reason given for the expected warranty was that it was seen as 'normal practice' for a new home to have a warranty. This is further supported by the large number of responses (72) who intimated that the 'builder said it would have a warranty' which reinforces the expectation,

shown in Table 4.3 above, that the new home would be available with a warranty. This could be construed as suggesting that the new homebuyers had no real concern over the importance of the warranty since it was viewed as custom and practice that is, they expected a warranty to be in place and that there was going to be a warranty in place for the various reasons shown in Table 4.3. Given that the new homebuyer had no real concern over the matter of the warranty being in place, we then have the possibility that with no warranty on it, the mortgage lender (if a CML member) would have withheld release of the mortgage sum. Only five per cent of the total cohort stated that the warranty was required by the lender, suggesting that the respondents did not understand the link between the warranty and release of funds from the mortgage lender that is, there was a robust financial reason for the need for a warranty which overrides the underlying reasons given by the new homebuyers.

- 4.6 The responses from the questionnaires throw up some interesting issues with regard to the significance of a warranty when purchasing the new home. The overwhelming response was that the warranty provision is something that was simply a matter of course that is, it was normal practice. Therefore, it may be inferred that the warranty played only a small part in the actual decision to buy the new home since it was anticipated that the new home would have a warranty in place or available and, that this warranty then brought the expected benefits with it. Only 13 per cent of the composite group of respondents (of this subgroup, 42 per cent were male and 58 per cent female) thought that the warranty being in place ensured quality within the finished home. Allied to this we have the fact that only 25 per cent of the total respondents indicated that they thought that the warranty ensured standards.
- 4.7 If this is considered in light of the 26 per cent of the total respondents who noted that the warranty gave 'piece of mind', then we are left with the situation that the majority of the respondents still do give the impression that they feel real strength of quality being driven by the warranty.

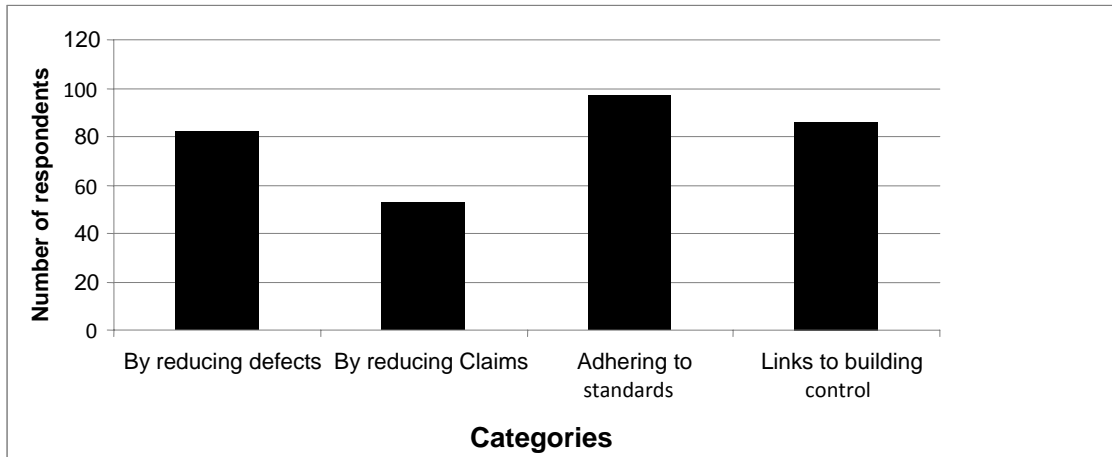
- 4.8 However, this to some extent contradicts the findings of a later question which asks about the relationship between the warranty and the quality of their new home.
- 4.9 The questionnaire respondents were asked if they thought the warranty affected the quality of their new home. Some 60 per cent of the respondents agreed that the warranty did influence the quality of the new home and their views are shown in Table 4.4 and Figure 4.2. A warranty will only be in place if the inspectors, operating on behalf of the warranty provider, have certified that the new home has met the criteria laid down in the building regulations and the warranty provider's technical standards. The warranty then can be seen as proof that the standards have been met and so the new home should be built to conform to requirements.
- 4.10 The respondents perceived that possession of a warranty could be responsible for homebuilders adhering to standards and the reduction in the incidence of defects. They also thought that the warranty linked the builder to Building Control (see above). This particular response could be attributed to the respondents' perception that the numerous and varied inspections carried out by Building Control and the warranty provider's inspectors (was a strong linking factor).

Table 4.4: Linkage between warranty and quality

| Linkage between warranty and quality | |
|------------------------------------------------------------------------|---------------------------------------------------------------|
| Do you think the warranty affects the quality of your new home? | Number agreeing (Per cent of all positive respondent)s |
| 1 By reducing defects | 83 (71) |
| 2 By reducing claims | 54 (46) |
| 3 Adhering to standards | 98 (84) |
| 4 Links builder to building control | 87 (74) |

Linkage between warranty and quality: base source, 117 respondents

Figure 4.2: Responses to question on link between warranty and quality

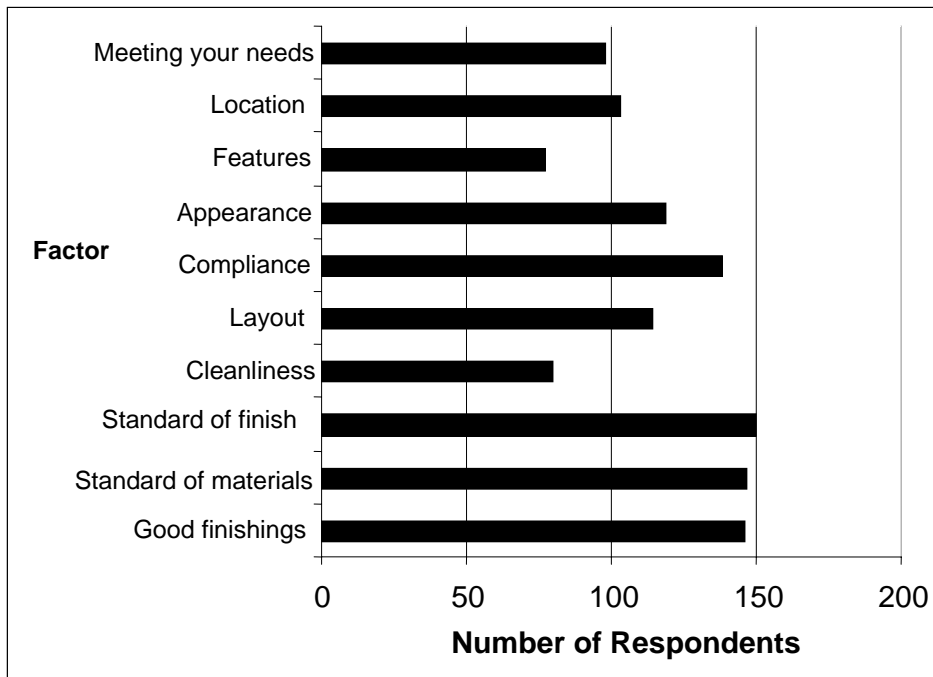


Linkage between warranty and quality: base source, 117 respondents

- 4.11 The contention that homebuyers value a home warranty was given support by previous research from the Consumers' Association in 1999 (cited in NHBC, 2008), which found that 97 per cent of prospective homebuyers felt having a home warranty plays an important part in their decision to purchase. Although on this occasion, the warranty appears to be a minor player in the overall matrix that is the decision to purchase a new house. Where the warranty does become a strong influence is when the new homebuyer considers the relationship between quality of the new home and the warranty that is, or is about to be, issued.
- 4.12 Nonetheless, whilst the provision of a new home warranty offers some form of reassurance, the findings from the research undertaken within this report suggest it ranks below location and design/size of the new home as a factor in the decision to purchase a particular new home. Supporting data for this contention is given below.
- 4.13 When given a list of possible quality elements and asked to note what they saw 'as quality in your new home?' the questionnaire respondents provided data as shown in Figure 4.3. Whilst the response rate is low (although in line with other academic research in the built environment),

and the general population is much larger than the base count (one hundred and ninety nine) nonetheless, from these responses it can be inferred that the standard of finish (workmanship), standard of materials and good finishings (for example, skirting boards made form mahogany as opposed to mdf), assume predominance for the new homebuyers who responded to the questionnaire survey.

Figure 4.3: Factors identified by new homebuyers that were seen to be measures of the quality



Factors of quality: base source, 199 respondents

The depth of understanding that homebuyers have about the extent of protection offered by warranties.

4.14 The majority (88 per cent), of the new homebuyers who were asked if they knew who provided their warranty replied positively that they did.

They answered that the builder provided the warranty. Of the 88 per cent, only 28 per cent positively identified an external warranty provider as the source of the new home warranty. There may be some confusion in the minds of the new homebuyers as to who is actually providing the warranty that is, the homebuilder who passes on the warranty from the provider, is perceived as the warranty provider.

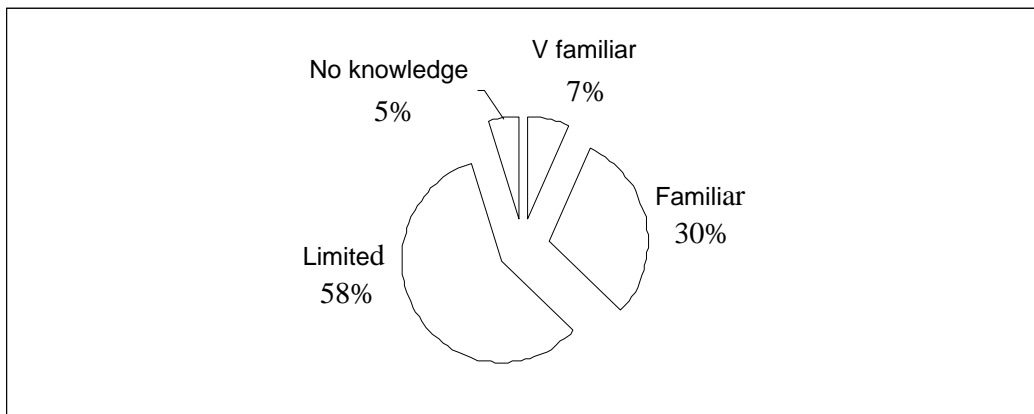
- 4.15 All respondents were asked how they felt about someone else, other than the homebuilder or current warranty provider, providing the warranty. The majority (62 per cent) indicated that it would not matter to them if someone else provided the warranty. Of those who responded with a 'No' (base count 127) as to the provider, some 55 per cent said that it would not matter because it was only an insurance policy. Some 35 per cent thought that any policy provider would provide a good problem solving service and six per cent saw an alternative provider (not specified) as offering a means towards reducing cost.
- 4.16 Of those respondents who thought that it would matter if someone else provided the warranty (71 respondents), some 70 per cent of them thought the alternate warranty provider would not know how the house was built. The premise underpinning this comment is that the warranty provider issues the warranty at the final-stage of the process and is not familiar with the building, where in fact, the warranty provider may be quite knowledgeable about the home that is, through independent inspections/Building Control. Some 43 per cent thought that an alternative warranty provider would not give them the service they needed to solve problems. Some 29 per cent thought that knowledge held by the homebuilder and their team would be lost and so reduce the service provided at later stages. Additionally, 21 per cent thought costs would rise if the warranty provider were to change (even though they had no cost comparator upon which to base such an assumption).
- 4.17 The respondents were asked as to who they thought would be a suitable alternative provider of new home warranties: they were able to express a choice across a number of possible providers. Some 36 per cent thought an independent insurance provider would suffice, 31 per cent thought that the Government should provide the warranty and, 27 per cent

thought that the buildings insurance provider should offer the warranty. The respondents saw insurance providers as the possible main route towards the provision of new home warranties.

4.18 The composite respondents were asked if they would be happy to obtain a warranty themselves from an approved supplier: 59 per cent thought that they would not be prepared to obtain the warranty from an approved supplier, relying on the warranty being in place beforehand. Some 29 per cent indicated that they would be prepared to search for a warranty from an approved supplier.

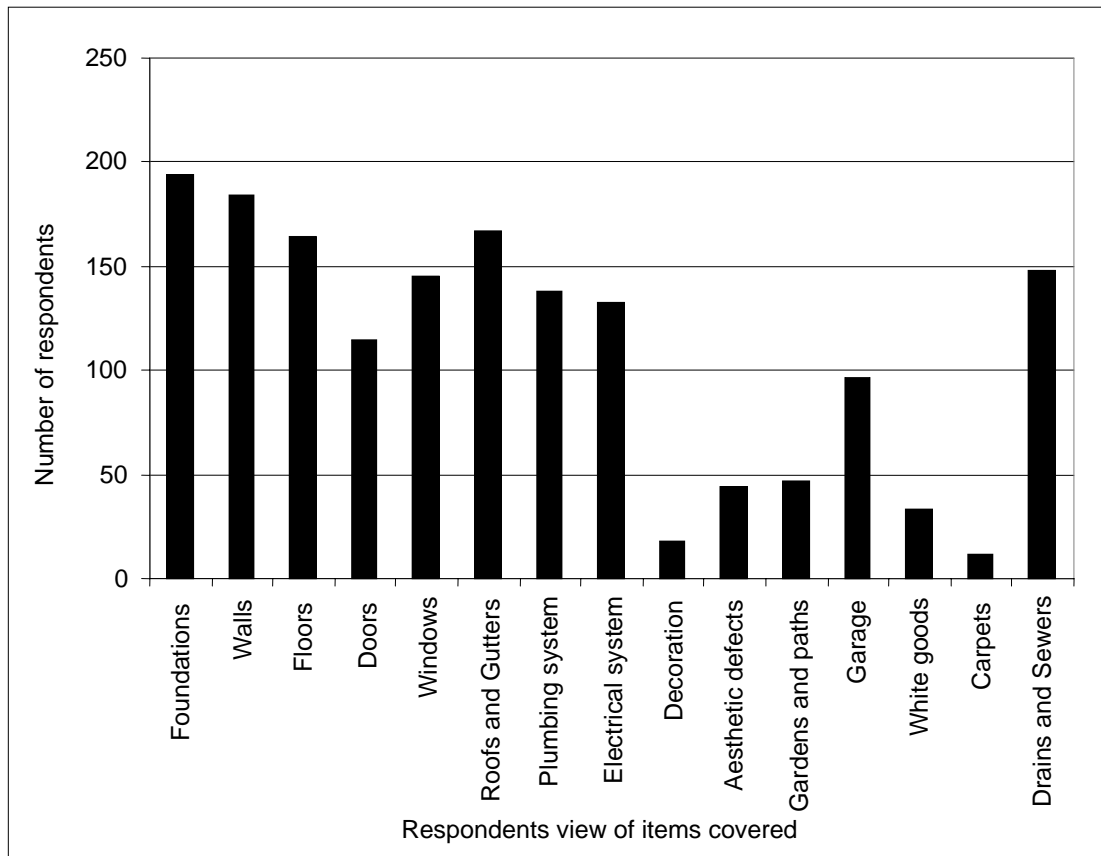
4.19 The new homebuyers responding were asked to decide how much they knew about the warranty cover and its operation, they had a range of possible answers, ranging from very familiar to no knowledge at all, as shown in Figure 4.4. The majority of the respondents, 63 per cent, openly admitted that they had limited or no familiarity with the warranty. This lack of familiarity is borne out by their responses to questions regarding the extent of cover provided by the warranty. When asked to indicate what items were covered within the new home warranty, the respondents were able to choose from the list items shown in Figure 4.5.

Figure 4.4: Understanding of the new home warranty



Understanding the new home warranty, base source 201 respondents

Figure 4.5: Respondents' view of items covered under the warranty



Respondents views of items covered, base source 199 respondents

4.20 The responses raise a number of questions regarding the homebuyers' perceptions of cover: although the new homebuyers were not technically grounded in house construction, the average person understands the importance of good foundations for a building, however, 5 owners did not think an item as important as foundations was covered by the warranty, 15 did not think the walls were covered (detailed analysis of replies to these points show that two of the respondents thought that both foundations and walls were not covered). Figure 4.5 shows the detailed responses and highlights areas where the respondents clearly misunderstood what the warranty covered for example, white goods (although these white goods are generally covered under a separate

insurance policy for example, contents insurance). When asked if there were additional items that the warranty should cover, some 22 per cent thought there were items to add in, but of this figure, only five per cent suggested additional or novel items.

- 4.21 The homebuyers were asked if the homebuilder explained to them what was covered by the warranty and the majority, 58 per cent, responded that the homebuilder did not indicate what items were covered by the warranty. Of the remainder, some 38 per cent of the respondents indicated that their homebuilder had in fact discussed what the warranty covered. What is not clear from the research is the nature and extent of these discussions. The NHBC, publish a Code of Conduct⁴⁴ for homebuilders within which page four refers to specifics that the new homebuilder should follow in order to meet the NHBC's Customer Service code of conduct. Specifically, this code requires the new homebuilder⁴⁵ to pass on detailed information to the new homebuyer of 'NHBC's Buildmark cover and any other guarantees and warranties from which they may benefit' (NHBC, 2008). The homebuilder may argue that they comply with this every time when they hand over the warranty policy and any 'welcome to your new home' materials or booklet/s.
- 4.22 The majority of the postal questionnaire respondents, (74 per cent) saw the duration of the warranty as lasting 10 years. Some 19 per cent saw the warranty as lasting only two years. The homebuilder's statements regarding how the warranty operates and their insistence that in the first two year period it was they (the homebuilder) who provided the remedial cover may cloud the perception of the new homebuyer as to the warranty's life and operation.
- 4.23 When asked how many years they would wish the warranty to last for, the majority (68 per cent) agreed that the 10 year period would suffice, some nine per cent suggested that the life of the home was preferred, 10 per cent saw the life of the mortgage as suitable and, nine per cent saw some other period that is, somewhere between three or 60 years as

⁴⁴ NHBC (2008c) Customer Service, a code of conduct for builders

⁴⁵ under point 10 on page four, of the code

preferable, with a further six per cent seeing a two year period as adequate.

The minimum standards homebuilders are required to meet in order to obtain warranty cover from providers - The influence that mortgage providers who require such cover have in determining these standards.

- 4.24 In reviewing the minimum standards homebuilders must meet in order to obtain a warranty there is a caveat. The number of warranty providers who actually set their own minima is limited. In essence there are two sets of standards which the homebuilder must meet or exceed when constructing a new home. These are the Building Regulations and the warranty provider's technical standards. The Building Regulations and the warranty provider's technical standards are not mutually exclusive. However, not all warranty providers issue bespoke standards. The NHBC have a distinctive set of standards which the registered builder is required to comply with in order that a warranty may be issued for the new home. The NHBC technical standards are set by a committee (of which the author is a member) who derive their powers from the NHBC Council (a body comprising representatives of the full spectrum of the homebuilding community and stakeholder organisations. This technical standards committee endeavours to represent all those relevant organisations who are interested in improving the quality of new and converted homes. Homebuilders, consumer organisations and professional institutions are represented on the technical standards committee: Table 4.5 illustrates the membership of the NHBC Council.

Table 4.5: Membership/representation on NHBC Council

| Membership/representation on NHBC Council | |
|--------------------------------------------------|--------------------------------------------------|
| Industry Category | Number of representatives on NHBC Council |
| Homebuilder representative | 20 |
| Appointed by NHBC | 20 |
| Finance/Law | 2 |
| Government/other | 3 |
| Consumer representation | 5 |
| CML | 8 |
| Construction industry* | 5 |
| Professional bodies | 13 |
| | 76 |

2008a, *The construction industry representatives include among others: The Chartered Institute of Building, The Home Builders Federation, The Federation of Master Builders, The Royal Institution of Chartered Surveyors and, The Construction Products Association.

4.25 NHBC technical standards take into consideration a plethora of guidance documents from the likes of Building Regulations, British Standards and NHBC's own claims record for organisations, materials and also records of defects. The actual composition of the technical standards committee is very much focused on the industry itself and those who lend to it. By far the majority of the technical standards committee membership is drawn from either homebuilder or CML representatives.

The relationship between the practice of issuing home warranties and the level of homebuyer satisfaction. The factors affecting the nature, extent and development of competition in terms of the cost of and cover afforded by warranties.

- 4.26 Typically, the homebuyer plays no part in the selection of the warranty provider. The homebuilder is the sole arbiter of choice on this matter, which very often is predicated by previous experience with the warranty provider and two other lesser factors: the warranty provider's acceptability to CML and, the premium likely to be charged.
- 4.27 In the past, in a large number of instances, the general rule held true that at the time of vital stages of home construction being undertaken (such as the foundations), the home had yet to be sold and the final purchaser was unknown or as yet unidentified. However, with the recent high demand for new homes this is not the case, new homes are often sold 'off-plan'⁴⁶. A number of the warranty providers, in their general literature and marketing materials, however suggest that if they are to be given the chance to manage the ensuing construction risk, through inspection and technical scrutiny of design and specifications, then it becomes self-evident that they need to be involved during the early design stages and actual construction activities.
- 4.37 Providers of new home warranties need to be able to demonstrate technical (building) experience, an actuarial knowledge and meet the Financial Services Authority's capital requirements⁴⁷. As mentioned above, having a warranty accepted by the majority of the CML members is a commercial imperative for any new warranty provider, undoubtedly CML influences the design and operation of home warranties since the

⁴⁶ A process whereby the purchaser simply visits the sales office, either onsite or located elsewhere, looks at models or illustrations of the site layout, and makes a commitment to purchase their prospective new home from these pieces of site data/drawings alone: there are very often no physical buildings to view. Indeed, many new homes are sold via the Internet.

⁴⁷ www.cml.org.uk/handbook/frontpage.aspx

standards that warranty providers have to meet are subject to interpretation and approval by CML⁴⁸.

- 4.38 As the home warranty forms an integral part of the homebuilder's supply chain it is likely that the cost of the warranty to the homebuilder will always be an issue. The typical cost of the warranty, at about 0.3 per cent of the home price for a homebuilder with a solid premium rating and low claims levels, means that the actual initial cost to the homebuilder is unlikely to be a driving factor, especially since premia rebates are often available after a period on no-claims (NHBC, 2008d). Given that NHBC account for the majority of new home warranties issued each year, then the figure NHBC offer as a 'typical premium' would appear to apply generally across the new homebuilding sector. However, a new homebuilder entering the new homes sector with no track record or one with a high claims record paying high premia, may well choose an alternative home warranty provider, provided this warranty is CML approved.
- 4.39 Analysis within Section 2 above illustrates that the actual level of cover afforded by a number of the warranty providers very similar. The only area where choice would appear to be available is in the level of premium charged and the potential for later rebates. The rebate mechanisms are not transparent and from the findings of the research it would appear that the new homebuyer does not see the cost of the warranty and does not appreciate the extent of cover afforded them.

The extent to which warranty providers package their warranty and building control functions together. The impact (if any) this has on the price and quality of warranties and/or building control.

- 4.40 There is no hard evidence to suggest that Building Control services are packaged with the provision of a new home warranty. What there is, is a market for new home building control that is divided between NHBC and the numerous local authorities.

⁴⁸ www.cml.org.uk/cml/media/press/277

- 4.41 The discussion in Chapter 2 above highlighted the number of warranty providers who also provide Building Control services or an approximation to that service. Within England and Wales there is the potential for Approved Inspectors to be either individuals in their own right, or corporate Approved Inspectors. Currently there are some 23 individual Approved Inspectors and 41 Corporate Approved Inspectors registered with the Construction Industry Council (CIC). Also, the Association of Consultant Approved Inspectors shows some 43 bodies registered⁴⁹. These approved inspectors fulfil the same functional roles with differentiation between them being centred around the size of project undertaken and the geographical spread of their operations.
- 4.42 In its published materials⁵⁰, the NHBC claim to have secured approximately 50 per cent coverage of all new homes that are built in England and Wales on an annual basis, as being checked and inspected by NHBC for building regulation purposes. The Building Control inspections carried out by NHBC Building Control are in addition to their normal checks carried out under the auspices of the NHBC warranty. 'NHBC employs 450 inspection staff, 60 building surveyors, 50 engineers and 225 other technical and professional specialists, many of whom support its building control business'.⁵¹
- 4.43 There are a number of independent Corporate and Individual Approved Inspectors (see above) who offer a plethora of such building control services in England and Wales. However, most of these providers tend to operate predominantly in the commercial building sector, thus leaving NHBC with a relatively uncrowded playing field in the new homebuilding sector. Where these independent Approved Inspectors do offer real competition is in offering a service to homebuilders and to homebuyers who are having extensions or improvement works executed (there will be no new warranty works or services being undertaken).

⁴⁹ www.acai.org.uk/Members/members.html

⁵⁰ www.nhbc.co.uk/Homewarranties/Abouthomewarranties/

⁵¹ www.nhbc.co.uk/aboutus

ANNEXE(S)

A ANNEXE 1 - MAKING A CLAIM AND THE CLAIMS PROCESS: CASE STUDIES

- A.1 Of the eight case studies undertaken seven were new homes that had had snagging inspections carried out on them, the remaining one replied directly to the author's request for information about claims they may made under their new home warranty.
- A.2 From analysis of the responses, generated by postal questionnaires to new homebuyers, on claims it becomes evident that the new homebuyers who responded to the postal survey were frustrated by the process of making a claim. Although the number of responses specifically dealing with claims is low (8), there is no robust data set available in the public domain by which to analyse further the proportion of problem sales of new homes. However, in 2005 NHBC carried out 7382 resolutions, if we take the NHBC completions for year 2005 as 172,100, then the percentage of claims to completions is four per cent. We have no data on the geographic spread of these claims. These resolutions can only be based upon claims of some description having been made to the warranty provider. What we do not know is when these claims were initiated and therefore no further analysis is made on them.
- A.3 In 2006/7 NHBC inspectors identified over 600,000 defects (NHBC, 2007c) so the number of defects divided by the number of new homes registered as forming part of the NHBC warranty in the UK in 2006/7 (178,832) = $600,000/178,832 = 3.4$ defects found per new home, and these defects, the NHBC indicate, could lead to more serious problems at a later stage.
- A.4 The penalties for non-compliance or a lack of inspections can be high to the homeowner but not necessarily the warranty provider. The amount paid out in claims situations in 1998 amounted to over £15m (Column 794, Houses of Parliament debate, 1998), in 2005 the NHBC carried out 7,382 resolutions involving disagreements on technical issues between home owners and NHBC registered builders and in 70 per cent of the cases found in favour of the homeowner (NHBC, 2007b). Payments in

respect of claims from homeowners in 2004/2005 reached over £35m and can be broken down as follows (all claims involved breaches of the NHBC technical regulations):

- Claims in the first two years which the homebuilders must put right totalled £9.7m.
- From years 3-10, the NHBC provides direct insurance cover. Claims from insurance totalled over £24.7m.
- Insolvency claims totalled £0.7m.

A.5 In 2005/2006 the NHBC found in favour of the homebuyer in nearly 72 per cent of cases although payment in respect of claims rose by over £2m and can be broken down as follows:

- Claims in the first two years totalled £12.5m.
- Claims in years 3-10 totalled £24.2m.
- Insolvency claims totalled £0.6m.

A.6 Despite identifying over 600,000 defects at early stages of the new home build process (before handover of the new home to the owner), the NHBC still paid more than £37.3m (year 2005/2006) in claims to home owners as a result of breaches of the Technical Standards and Buildmark warranty. Some 33 per cent of all homeowner claims related to the superstructure, 30 per cent related to the foundations and substructure, 22 per cent related to roofs, 12 per cent related to services, fixtures and fittings and four per cent ancillary buildings.

A.7 Data from eight case studies have been collected as part of the overall data collection process that is, the respondents who completed the warranty questionnaire were invited to take part in a follow-up questionnaire only if they had, or were making, a claim against the warranty. They were invited to complete a second questionnaire which related only to their claims experience, whether positive or negative. Tables A1, A2, A3 and A4 illustrate the Claimants' responses

Table A.1: Explanation of the claims process

| Explanation of the claims process | |
|---------------------------------------------------------------------|--------------------|
| When you bought the house, was the claims process explained to you? | |
| No, the claims process was not explained | C1, C2, C4, C6, C7 |
| Yes, the claims process was explained | C3, C5 |
| By the sales team | C3, C5 |

Table A.2: Handling of the claim

| Handling of the claim | |
|-----------------------------------------------------------------|----------------------------|
| You have made a claim under the warranty. How was this handled? | |
| Swiftly? | |
| Slowly? | C1, C2, C3, C5, C6, C7 |
| Not at all? | C4 |
| Professionally? | |
| With Reluctance? | C1, C2, C3, C4, C5, C6, C7 |
| Neutrally? | |

Table A.3: Feelings about the claims process

| Feelings about the claims process | | | |
|--------------------------------------------------------------------------------|----|-----------------------------------------|----------------------------|
| During the claim, did you find the process: (please select any/all that apply) | | | |
| | OR | | |
| Easy and simple to follow? | | Hard and complex to follow? | C2, C6, C7 |
| Welcoming and heartening? | | Cold and Frustrating? | C1, C2, C3, C4, C5, C6, C7 |
| Aimed at a positive outcome? | | Driving for a negative outcome | C2, C3, C4, C6, C7 |
| Supporting your reasons to buy? | | Detracting from you enjoying the house? | C3, C4, C5, C6, C7 |
| Responsive to your needs? | | Squashing what you wanted? | C3, C4, C6, C7 |
| Supporting your claim? | | Aimed at refusing your claim? | C2, C3, C4, C6, C7 |

Table A.4: Views on the claim outcome

| Views on the claim outcome | |
|------------------------------------------------------|------------------------|
| Were you happy with the outcome of the claim? | |
| Yes, we were happy with the outcome | C5 |
| No, we were not happy with the outcome of the claim | C1, C2, C3, C4, C6, C7 |

A.8 The home owner faces the prospect of having to pay, in advance, a fee to have their claim processed by the warranty provider. This fee, if the claim is upheld, will be returned, but nonetheless, the claimant still has to lay this sum out. The onus being on them to have a solid claim.

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