Protect your Statutory Warranties - 2% Building Bond Scheme

Owners Corporations in NSW can protect their statutory rights by initiating legal proceedings against builders and developers under the Home Building Act 1989, even while utilising the Building Bond Scheme.

An Owners Corporation can commence legal proceedings against a builder and developer to protect its statutory warranties pursuant to the Home Building Act 1989 (NSW) (**HBA**), even if it has rights under the Strata building bond and inspections scheme **(Building Bond Scheme**).

An owners corporation should thoughtfully consider when commencing legal proceedings alongside working with the Building Bond Scheme is appropriate in its circumstances.

Background: Building Bond Scheme

Established under the Strata Schemes Management Act 2015 (NSW) and commencing its operation in NSW on 1 January 2018, the Building Bond Scheme applies to building contracts entered into from 1 January 2018 for building work to construct residential or partially residential strata properties that are four storeys or more.

The Building Bond Scheme was introduced to address the inequity of buildings of more than 3 storeys having no home building compensation cover (formerly known as home warranty insurance). Under the Building Bond Scheme, developers of new 4 storeys and higher residential strata buildings are required to pay a building bond to NSW Fair Trading equal to 2% of the construction contract price.

The building bond is used to secure funds that may be drawn upon and used to pay for the rectification costs of any defective works identified in a final inspection report. If no defects are identified, the building bond is released in full to the developer.

Stages of the Strata Building Bond Scheme

Within 12 months of commencing the strata development, developers must source and appoint an independent building inspector from the strata inspector panel, with the approval of the owners corporation. The building inspector will conduct two inspections of the building, being an interim and final inspection.

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The **interim inspection** takes place between 15 and 18 months after the building works have been completed of the strata property. Following the inspection, the building inspector is to prepare an interim report identifying any defective building work. If no defects are identified, the building bond may be released to the developer two years after the date of completion. If defects are identified, they must be rectified by the developer.

A **final inspection** and report is provided usually between 21 and 24 months after the building work has been completed. If no defects are identified, the building bond may be released in full to the developer. If defects remain, the building bond may then be used to pay the costs of rectification.

Considerations Strata Scheme's should make regarding the Building Bond Scheme

Protect your Statutory Warranty Period

The scheme must consider commencing legal proceedings against the builder and developer to protect its statutory warranty rights for non-major defects pursuant to the *HBA* within its two year statutory warranty period, subject to any extensions. Under section 18E of the *HBA*, a strata scheme can commence legal proceedings against the builder and developer for a breach of statutory warranty. Contrary to the *HBA* allowing a claim to be brought against both the builder and developer, the Building Bond Scheme relates only with respect to the developer, who is then responsible for arranging with the builder to rectify defective building work before the final inspection is carried out.

The scheme's 2 year statutory warranty period for non-major defects runs from the date at which the first occupation certificate was issued and is extended until the end of 90 days after the end of the period within which a final inspection report on the building work under Building Bond Scheme is *required*. A building inspector is *required* to provide a final report not earlier than 21 months and not later than 24 months after the completion of the building work.

Failure to initiate legal proceedings against the builder and developer could significantly limit the scheme's ability to claim for non-major defects against a developer and builder. Noting that the final inspection of the building occurs between 21 and 24 months after the building work has been completed, the time period is sensitive in light of the statutory warranty period for non-major defects. Therefore, if a scheme relied only on the Building Bond Scheme, and it did not cover all non-major defects, the scheme may have lost its rights under the HBA to pursue the developer and builder for non-major defects if it did not commence proceedings within its 2 years + 90 days statutory warranty period, unless the duration for the preparation of the final report is extended by the Secretary of the Department of Finance, Services and Innovation, who may vary the period within which a final report is to be provided.

2% Contract Value

The Building Bond Scheme only requires the developer to pay a building bond fee of 2% of the contract value to the Department of Fair Trading. Subject to the final inspection report and any identified defects, often the 2% building bond is insufficient for the rectification of all identified defective works.

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If the 2% building bond does not sufficiently cover the rectification costs, the scheme may be left out-of-pocket if the final report came late, and the scheme had not commenced legal proceedings alongside working with the Building Bond Scheme.

Conclusion

If the building inspector appointed does not sufficiently identify all non-major defects, the scheme may lose its rights to pursue the developer and builder under the HBA for non-major defects, in light of the time sensitivity between the final report due date and the requirement to commence proceedings to protect statutory warranty rights. Once proceedings have been commenced, the non-major statutory warranty period is preserved, and a scheme can investigate further non-major defects it may wish to claim.

The Building Bond Scheme only alleges liability to the developer of the building for rectification works to the building, should there be any, whereas, an owners corporations has statutory warranty rights against both a developer and builder under the HBA.

Commencing proceedings within the non-major defect period alleviates any arguments whether a defect claimed is major or non-major. Such arguments can be very lengthy in proceedings which are only commenced within the 6 year statutory warranty period for major defects, hence why it is recommended to commence legal proceedings pursuant to the HBA, whilst making an application for the Building Bond Scheme.

Key takeaways

- The Building Bond Scheme requires developers of new residential strata buildings to pay a bond to secure funds for rectifying defects.
- Owners corporations can initiate legal proceedings against builders and developers to protect statutory warranties within a two-year period.
- The statutory warranty period for non-major defects begins from the date of the first occupation certificate.
- Independent building inspections are mandatory at specified intervals to identify any defects in the building work.
- If defects are found, the building bond can be used to cover rectification costs.

****The information contained in this article is general information only and not legal advice. The currency, accuracy and completeness of this article (and its contents) should be checked by obtaining independent legal advice before you take any action or otherwise rely upon its contents in any way.*

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