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30 January 2018

Off-the-plan Contract Review
Office of the Registrar
McKell Building
2-24 Rawson Place
SYDNEY NSW 2000

Dear Sir/Madam

DISCUSSION PAPER – OFF-THE-PLAN CONTACTS FOR RESIDENTIAL PROPERTY NOVEMBER 2017

1. Introduction

Strata is the fastest growing form of residential property ownership in Australia. Over half the new dwellings to be built in our metropolitan areas over the next decades will be strata titled. The growth of this sector raises increasingly important questions over property ownership and governance.

The Owners Corporation Network of Australia Limited (OCN) is the peak consumer body representing existing and future owners of residential strata properties, primarily in NSW. As such, OCN is the key stakeholder in this review.

OCN's overriding position, based on the experience of our members, is that protections offered to purchasers of new residential strata in NSW are very weak and the reputation of strata living as an option to meet residential housing demand remains at risk as a result. Consumer protections for the purchase of an appliance or motor car are far stronger than currently apply to the purchase of a new residential strata property.

In the case of off-the-plan purchase arrangements, the risks faced by prospective purchasers are particularly poor. This form of sale opens the way for unscrupulous developers to take advantage of inexperienced and ill-equipped home buyers to increase access to their funding and reduce the cost of those funds. The purchaser carries many commercial risks without any compensating return on funds. While this is potentially beneficial to purchasers generally by enhancing supply, they have no way of knowing whether their individual purchase arrangement is a good one as a result. Indeed, the balance of power between purchaser and developer in these arrangements is extremely one sided in favour of the developer.

Many OCN members actively advise against anyone buying off the plan as a result of their own negative experiences. Unless things change significantly, the OCN may well formalise this position as standing advice from the OCN to prospective purchasers of off-the-plan strata developments.

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It should therefore come as no surprise that the OCN supports many of the key proposals in the Discussion Paper and is seeking stronger protections than even those currently proposed.

It is against this backdrop that each of the issues raised in the Discussion Paper is addressed in turn. Further additional protections are then briefly canvassed for consideration.

2. Responses to Questions Raised in the Discussion Paper

Q.1 Is a separate mandatory disclosure regime needed for off-the-plan contracts?

Yes. The current practice of providing a weighty, non-standard contract document with a raft of risks for the prospective purchaser is unreasonable.

Q. 2 Is there benefit in mandating a prescribed disclosure statement for all off-the-plan contracts?

Yes. Many developers rely on risks to the purchaser not being expressly disclosed to help make the sale based on slick marketing and the emotion of unwary and inexperienced purchasers. In time this ends in tears as the risks to the purchaser reveal themselves.

Q. 3 If so, what should be included in the Statement?

The key problem for many purchasers buying off the plan is that they do not have the time or skill to appreciate the risks to the purchaser implied by these types of contracts. And, unfortunately, lawyers and conveyancers are not paid enough to review the contract thoroughly.

All material risks should be explicitly disclosed in the Statement. While these risks are too numerous to set out fully here, they usually include the failure of the contract to clearly specify precisely what the purchaser is getting (e.g. room dimensions, finishes, vehicle locations etc), project timing risks, the financial risk to the purchaser if the developer fails, the absence of warranty regarding the quality of the final as built product, and the costly and time consuming processes that can arise in the event of a contractual dispute.

Q. 4 Would buyers have more certainty if the following documents were included as part of mandatory disclosure:

• **proposed plan showing the proposed lot -** Yes, provided all the plan dimensions and finishes are clearly specified and subject to warranty.

• **proposed by-laws -** This may be of some assistance in regard to things like whether pet ownership is approved or prohibited, but it should be noted that by-laws can be changed at any time after the building is ready for occupation.

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• **proposed schedule of unit entitlement -** Yes, including subsequent changes that can and do occur prior to occupation.

• **estimate of proposed levy contributions -** Yes, including subsequent changes that can and do occur prior to occupation.

Q. 5 Are any of the documents unable to be provided or would impose significant cost on developers if required at the time contracts are prepared?

The developer is effectively getting the prospective purchasers to help secure project finance at a competitive rate. Therefore, the costs involved in providing purchasers (who are vital stakeholders) with sufficient information to make an informed purchasing decision ought to be a minor consideration. The alternative for the developer would be to provide prospective lenders with much more information in a situation where the power balance is more even and therefore more demanding on the developer.

Q. 6 Should developers be required to notify purchasers where a change is made to:

• **The proposed plan;**
• **The schedule of unit entitlements (for strata and community schemes) and**
• **The by-laws or management statement**

that is likely to have a material impact on the purchaser?

OCN sees no good reason why purchasers should not be informed of all changes, material or otherwise. This would remove the exercise of any discretion by the developer over what is or is not going to have a material impact on the purchaser. Indeed, the purchaser is best placed to determine what changes really matter to them.

Q. 7 Are there any other changes to the scheme that developers should be required to notify purchasers of?

Among other matters, purchasers should be kept informed of the progress of the project against the key project milestones and any implications this may have for the occupation dates in the contract.

Q. 8 Should notification of changes be required to be made at a set time before settlement can be enforced?

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Q. 9 What period of notice is appropriate; 14 or 21 days?

The purchaser should receive a minimum of 6 weeks' notice of changes prior to settlement. This is consistent with the usual period required to complete the legal and other searches associated with the contract to purchase an existing (ie completed) property.

Q. 10(a) Should the developer be required to provide a copy of the registered plan to the purchaser before a notice to settle can be issued?

Yes

Q. 10(b) Should the purchaser's ability to terminate a contract be based on the purchaser demonstrating "material prejudice"?

The issue here is to whom the purchaser needs to demonstrate 'material prejudice'. The developer is in a strong position of negotiating power on this question. Accordingly, independent third party binding arbitration of this question needs to be made available with costs borne by the developer except where the purchaser's issue can be shown to be trivial or vexatious.

Q. 11 Should any statutory termination scheme include, as an alternative, a claim for compensation?

Yes

Q. 12 Should the cooling off period be extended for off-the-plan contracts?

Yes

Q. 13 If so, should the cooling off period be 10 or 15 days?

Off-the-plan contracts are often complex and vary from one developer to another. To obtain sound independent legal advice on the risks in such contracts may require some time. For this reason, OCN would consider 21 days to be more appropriate.

Q.14 Should legislation mandate that the deposit be held in the trust account of a stakeholder?

Yes. The purchaser does not receive a return on the deposit provided to the developer that is sufficient to compensate for the risk of lending money to an entity with an unknown credit rating that is almost certainly lower than B-.

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Q.15 Should NCAT be allowed to make orders as suggested?

Only as a last resort. This regime requires a much quicker and cheaper form of dispute resolution that is currently provided by NCAT. Indeed, giving NCAT this role would only add another burden to an already struggling institution, particularly given the rate of growth in off-the-plan purchase arrangements.

Q.16 Should a condition be inserted in the contract for sale requiring parties to attempt to settle disputes through arbitration?

Yes. The arbitration role should be provided by an independent expert arbitration body funded primarily by the developers. Purchasers should only be required to pay the costs of arbitration when it can be shown that the matters raised by the purchaser are trivial or vexatious.

Q.17 Should legislation be introduced requiring parties to attempt to settle disputes through arbitration?

Yes, in line with the proposal in the response above to Q16.

Q.18 Should the definition of sunset date be expanded so that is covers other termination events?

The key point here is that most of the risks that lead to delays are best managed by the developer. Any given purchaser has no capability to influence completion milestones. Therefore, consideration should be given to mandating additional sunset provisions that enable purchasers to rescind the contract if key milestones are not met by a date defined in the contract. There should be no reciprocal provision in favour of the developer, as the developer is the only party to the contract that has the capacity to meet project milestones.

Q.19 Are there some termination points that a developer should be allowed to use to end a contract without seeking approval of the Court? If so, what are they?

Approval of the Court appears essential for any termination point that could be reasonably contemplated to ensure that the developer was not gaming the process. However, if there was also an independent arbitration process then this may provide scope for some matters to be determined by this body in the first instance while retaining scope to appeal the matter to a Court.

Q.20 Should s 66ZL be clarified or amended to allow the Court to make an award of damages to purchasers if the circumstances so require?

Yes

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3. Potential Additional Protections for Purchasers

There are at least four other further areas of protection for off-the-plan apartment purchasers that policy makers should consider:

a) Restricting the ability to offer 'off-the-plan' contracts to developers with an established positive reputation and capability.
b) Strengthening the statutory warranties required to be provided by developers to purchasers for the quality of the finished product.
c) Mandating standard minimum provisions in off-the-plan sales contracts.
d) Disclosing the potential role of any Building Management Committees and the significant challenges these may present for residential strata owners.

The OCN's position on each of these matters is briefly explained in turn:

a) Only Competent Developers Permitted to Offer off-the-plan Contracts

There needs to be a regime that supports the many competent and reputable developers in this market in the eyes of the consumer.

At present there are only fledgling internet comparator services and relatively immature accessible databases to help prospective purchasers know they are dealing with competent developer/builder partnerships. Also, the independence of these services is unknown. In addition, issues with building defects, particularly latent building defects, take time to become apparent and reflect on the original developer and builder. This provides too much of an opportunity for unethical developers supported by skilled sales promotion to exploit unwary purchasers.

Accordingly, for the time being at least, there is a strong case for a centrally administered licensing regime which only enables only licensed developers and builders to participate in off-the-plan offerings. The licensing body should be independent of developers and appropriately resourced with capable people. It could be funded by a levy on all residential developments.

Performance based criteria could be established that need to be met before a license is granted to a given developer/builder partnership to offer off-the-plan contracts to purchasers. These criteria could include purchaser satisfaction measures on projects over time as well as the right to rescind the license if performance criteria cease to be met.

b) Strengthening Statutory Warranties for Defective Construction

The severely limited statutory warranties from developers provided to purchasers of new apartments have been considered at length by various reviews. The OCN remains firmly of the view that the current regime offers entirely inadequate protection to purchasers. Horror stories

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are commonplace among our members and this continues to reflect poorly on Government, as well as undermining confidence in strata living more generally.

As a matter of principle, it should be incumbent on all developer/builder partnerships to deliver standards of construction that, as a minimum, meet the requirements of the Australian building codes. Liability for failing to do so should rest squarely with the developers and supported in their respective arrangements with building companies. No one else is appropriately placed to manage this risk, and certainly not the ultimate purchaser. Given the propensity of developers to cease operation this needs to be backed by meaningful insurance and licensing arrangements.

In this regard the OCN notes with dismay the Full Bench of the High Court of Australia decision in Brookfield Multiplex Ltd v Owners Corporation Strata Plan 61288 [2014] HCA 36. In this decision the Court unanimously held that a builder of strata-titled apartments did not owe an owners corporation a duty of care in tort to avoid pure economic loss caused by latent defects in common property. It is plainly absurd that purchasers of such significant assets should carry the risk of poor construction that is not visible at the time of purchase. And for the off-the-plan purchaser they are exposed to risks associated with all poor construction, visible or not at completion.

c) Mandating Minimum Standard Requirements in Off-the-Plan Contracts

One of the issues confronting prospective purchasers is the variability of off-the-plan contracts and the tendency for this to be crafted in terms favourable to the developer. This creates challenges for the purchaser in understanding the risk allocation between the parties and in negotiating changes to rebalance this risk allocation.

One way to address this is to establish a standard form of contract that allocates the risks between the parties to the party best able to manage the relevant risk. Some of these conditions could be mandated requirements and some conditions open to variation by the parties provided that such variation is made explicit. Queensland already has a standard contract.

d) Disclosing the Potential for the Operation of a Building Management Committee

The Owners Corporation Network has consistently pressed for reform of Building Management Committee (BMC) arrangements now common on larger sites accommodating multiple strata plans. The legal framework supporting these arrangements has not kept pace with the emergence of such sites and relies too much on negotiated multi-party agreements to manage property common to more than one strata plan. Any one party can undermine the efficient functioning of BMCs with only time consuming, costly and complex legal recourse for other BMC or potential BMC members. Furthermore, it is often feasible for one or more parties to be able to unduly influence or control BMCs to the disadvantage of other parties.

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Accordingly, it is imperative that off-the-plan purchasers, many of whom have little or no experience with these arrangements, to be made aware of this risk as well as the BMC arrangements as they emerge. While this disclosure should also apply to any purchaser entering into a contract with a developer for a completed apartment they are more likely to be able to observe whether a BMC has been established, as well as the terms and conditions of its operation.

It is not uncommon for OCN members to advise prospective strata owners to avoid buying into a stratum involved with complex BMC situations. The OCN itself advises extreme caution where these arrangements are required on a site.

4. Summary

OCN members report many negative experiences with new apartment purchases. Poor construction and lack of industry accountability for defects are far too common, and further reform is required if strata living is to succeed in accommodating the growth in demand for housing.

However, the experiences with off-the-plan contracts are particularly negative. Unlike many other purchase situations, the bargaining position of the purchaser is weak and the associated consumer protections very poor.

It is pleasing to see Government proposing reforms and these should be implemented as soon as possible. Indeed, as set out above, reforms beyond those proposed in the discussion paper need to be considered.

As the key consumer voice in this review, OCN welcomes this Discussion Paper and is eager to engage with government on any aspect of this submission, and to develop solutions to the issues identified.

Yours sincerely

K Stiles

Karen Stiles
Executive Officer