

CONSULTATION RESPONSE



OFT Market Study HBF Response to OFT Questionnaire

24 September 2007

OFT MARKET STUDY HBF RESPONSE TO OFT QUESTIONNAIRE 'CONSUMER MATTERS'

Summary

New home buyers have a very high level of legal, financial and product protection, much of it via professional third parties:

- Legal representation for all buyers and a written legal contract for each sale;
- Mortgage lenders' own requirements – confirmation of Building Regulations and warranty, valuation – reinforcing the consumer's protection;
- Housebuilders' contractual obligation to build in accordance with planning permission, building regulations approval and to specified standards;
- Home information packs before commitment to purchase;
- Direct consumer contact with the builder/producer, providing information, answers to questions and problem solving;
- Building Regulation standards;
- Extended new home warranty;
- Warranty provider's independent dispute resolution and arbitration procedures;
- Protection through legal requirements such as Unfair Terms in Consumer Contracts Regulations 1999 and Property Misdescriptions Act;
- Enhanced buyer bargaining position from extensive market information available on the internet on product availability, prices and house builders.

We suggest current systems generally work very well. Britain has not suffered any systemic or widespread residential building failures since the public sector system-built failures of the 1950s and 1960s. This suggests the systems in place to ensure building quality are working extremely well. We understand there have been only four OFT referred contract complaints and determinations in respect of new homes.

While we understand, and indeed support, steady, planned and properly managed improvements to standards over time, introducing major changes to systems that, the evidence suggests, are working well risks unintended adverse consequences which might undermine the current successful system.

1. Consumers' experience of buying a new home and their satisfaction with the process and the quality of the home itself.

Most house builders give a high priority to customer satisfaction, and awareness of the need to achieve and maintain high levels of satisfaction has grown in the last few years. Customer expectations have risen across all products and services, so that buyers demand more from their home builders. In addition, the Housing Forum Surveys in the early 2000s, Barker Recommendation 32 and HBF's subsequent involvement in this area, have further focused the industry's attention on the issue.

HBF's Consumer Satisfaction Survey reveals a high level of satisfaction with the new home buying process and the new home product. In the survey covering the 12 months October 2005 to September 2006, drawing on the experiences of some 26,000 new home buyers from 20 larger home builders:

Service

- 78% of buyers were either very (37%) or fairly (41%) satisfied with the serviced provided during the home buying process (Q1), with only 11% dissatisfied (and 11% "neither");
- 65% were very (31%) or fairly (32%) satisfied with the service provided after moving in (Q5), while 23% were dissatisfied (12% "neither");

Quality of Product

- 70% rated the standard of finish as very (29%) or fairly (41%) good (Q4), with 18% rating it as poor (13% "neither");
- 76% were very (36%) or fairly (41%) satisfied with the overall quality of the home (Q7), while only 14% were dissatisfied (10% "neither");
- 77% would recommend their builder to a friend.

In addition, although 94% of buyers reported problems to their builder after moving in, 22% said there were fewer problems than expected, 39% said the number was in line with expectations, while 39% said there were more than expected.

Most home buyers understand that there may be snags with a new home which is largely hand built, on site, in all weathers, and involving a range of different materials and trades. While it is disappointing that 39% of buyers experienced more problems than expected, nonetheless a large majority (61%) regard the number as in line with, or less than their expectations.

There is a clear message from all the results above: a large majority of new home buyers is satisfied with the service and the product, but an important minority is not satisfied. The industry needs to concentrate particularly on reducing problems encountered after handover and improving after-sales service. We are often told,

although HBF does not have direct evidence, that dissatisfaction is frequently the result of failure to rectify faults in a reasonable time, or the failure of tradesmen to turn up when a home owner has taken the day off work, rather than a failure to put problems right at all. In other words, these problems are often a failure of procedures, not product.

HBF believes the annual Customer Satisfaction Survey will help drive up house builders' awareness of problems or areas of weakness, and reinforce company efforts to address these problems. HBF's survey names individual house builders, giving them star ratings, for Question 7 (overall satisfaction) and Question 8 (recommendation to a friend), so that companies with weaker records have a strong incentive to improve their practices and procedures.

In addition to the Customer Satisfaction Survey, HBF drew up a voluntary Customer Service Code of Conduct for its members, which included a model Customer Charter, and developed model contract terms to help member companies ensure their consumer contracts comply with best practice.

HBF's three customer satisfaction initiatives (Survey, Code, Contracts) represent only the visible tip of the iceberg. Individual companies have a wide range of measures designed to achieve high levels of consumer satisfaction. For example, most larger companies have their own customer service departments, most have their own customer survey carried out by an independent third party (in addition to the HBF survey), many have customer charters, customer satisfaction scores are often included in staff incentives/bonuses, NHBC operates quality awards (Pride in the Job Awards for site managers), and some companies operate their own construction quality incentive schemes.

2. The level of consumer/legal protection that exists for homebuyers purchasing new homes.

As noted in the introduction, new home buyers have a range of consumer and legal protections, some direct, some indirect.

- Virtually all buyers have legal representation (we understand DIY legal representation is very rare), with the cost of this representation falling over the last two decades. This legally qualified person cannot act for the house builder in the same transaction, so the representation is independent. Where a mortgage is involved, the lender will investigate title.
- Three quarters of all home buyers – and probably a similarly high proportion of new home buyers – require a mortgage. Because a mortgage lender requires adequate security for a loan, the mortgage process highlights the protection offered to the home buyer by requiring evidence of a Final Completion Certificate for Building Regulations and an NHBC, Zurich or Premier new home Warranty before releasing funds. The borrower will also benefit by seeing the lender's valuation. Buyers who do not require a mortgage receive the same warranty and building regulations protection.
- Consumer advice on mortgages is regulated by the Financial Services Authority.

- Because new home buyers are buying from the company constructing the product, they are provided with information, and are able to seek further information, about their home and the estate both during and after the buying process. They have the benefit of a final inspection before completing the purchase, they will usually have a formal hand-over in which the builder or his representative will explain how to operate equipment in the home and how to ensure the best performance of the home, and they will receive documentation about the home, equipment, new home warranty and other warranties. None of these benefits is available to second-hand home buyers, nor buyers of most other products. Also, buyers will usually be able to see examples of a house builder's finished product as a show home and they can visit their new home as it is being built.
 - All new homes must meet planning requirements, Building Regulations (incorporating the most up-to-date) standards and warranty construction standards, thus offering consumers a high level of product protection. The product and workmanship standards defined in Building regulations, and more particularly the NHBC building standards, incorporate compliance with British Standards Institute, British Board of Agreement, and many other Product and process approved schemes and standards, all giving the end consumer a high level of assurance.
 - Almost all new homes have an extended warranty, such as the NHBC's 10-year Buildmark warranty, offering a high level of protection, both financial and product quality. NHBC's warranty includes free dispute resolution procedures which, in the vast majority of cases, avoid the need and expense of bringing in a lawyer or going to court. It also offers an initial two year responsibility for the house builder to attend to issues arising in the 'running in' period of the new home.
 - The customer benefits from manufacturers' guarantees and warranties for items such as the boiler, white goods and other components in the new home.
 - Further legal requirements, such as the Unfair Terms in Consumer Contracts Regulations 1999 or Property Misdescriptions Act, provide additional protection for new home buyers.
- 3. The level of consumer/legal protection that exists for homebuyers purchasing new homes in the light of the nature of the transaction, the level of protection in other sectors and/or international comparisons**

There are several important differences between the new home transaction and purchases of other products or services.

- The most obvious is the high price and the long-term financial commitment made by most buyers. However this applies equally to second-hand homes.
- As with any product or service, buyers must take responsibility for ensuring the price they are paying is a fair market price and is affordable. Most buyers will do their own research in the local market, often using the internet, gaining an idea of local prices. For home buyers taking out a mortgage, because the lender will require a valuation to ensure there is adequate security for the loan,

the buyer will have access to an independent valuation. Buyers of new and second-hand homes also have the option of commissioning their own professional valuation. Buyers of second-hand homes are able to have a full survey carried out, but it appears only a minority do so because of the expense. New home buyers do not need a survey, and so avoid this expense, as they can rely on the new home's 10-year warranty.

- It could be argued that the complexity of the new home product, and most consumers' limited knowledge about the product, is a key aspect of the new home transaction. However this applies equally to second-hand homes, and to many other products – cars, computers, electronic equipment, appliances, etc. And new home buyers have a number of sources of information and protection not available to buyers of many other complex products, as discussed above and below.

As discussed in 2. above, new home buyers have a number of independent sources of product protection, both while the home is being built and for 10 years after completion, notably Building Regulations and the new home warranty. Because these are enforced by professional inspectors, and must meet Government Building Regulations standards and the warranty provider's standards, new home buyers have a very high level of protection.

- One important difference, noted above, is that the new home buyer has direct contact with the producer of the product. Such direct contact is rare for most products, although common for services. Buyers are able to seek information about the product they are buying and about progress with the building. Snagging and hand-over procedures offer added information and protection. And after-sales procedures, whether directly from the builder or via the warranty, give a very high level of protect for the first two years of a warranty, and structural protection for a further eight years (in the case of the NHBC warranty).

HBF does not have information on international comparisons. However we understand that the NHBC warranty is regarded as one of the best new home warranties in the world, it is employed as a model for warranty schemes in other countries and NHBC is frequently asked for advice by other countries.

4. The extent to which homebuyers *are aware* of the level of consumer/legal protection available to them when purchasing a new home.

While we do not have research evidence of such awareness, we believe home buyers are aware of the range of different forms of protection, given the legal and professional representation they receive in the buying process.

Virtually all new home buyers will be represented by a solicitor. We understand it is a Law Society requirement that the solicitor explains the transaction details, risks and protection to their client. In addition, many home builders, and the principle warranty providers, publish informative guides for consumers explaining their protection during the purchase process.

As stated above, most house builders want to maintain high product and service standards and want satisfied customers. Product defects are costly to put right after

the event, and dissatisfied customers are costly in terms of staff time and company reputation. Most people working for a house building company take pride in their work.

New home buyers will usually deal with trained sales and customer service representatives who will hold a great deal of information about the product, and will be able to assist the buyer with the home buying process. It is in the financial interest of the house builder to make sure the sale goes smoothly and efficiently. Also, the buyer is offered protection by the Unfair Terms in Consumer Contracts Regulations and the Property Misdescriptions Act, although the buyer may not be aware of either source of protection.

There are also built-in safeguards. Virtually all buyers have legal representation and they will be made aware of their legal rights by their lawyer. The lawyer will also inform the buyer about the warranty, planning permission for the new home and building regulations. The majority of buyers require a mortgage, and because lenders require proof of Building Regulations compliance and a new home warranty, the buyer is further protected. The buyer will receive information at move in, including details of their warranty which protects them well into the future.

5. The extent to which model house purchase terms agreed between the OFT and the Home Builders Federation are used and the reasons for and against use.

The model terms were distributed to all HBF members and HBF publicised them both at the time and subsequently. We have not surveyed member companies to ask how many have adopted the model terms. However we are aware that many companies have taken legal advice on compliance with the Regulations, and a number of the larger firms have indicated to us that they have adopted the model terms.

The Regulations were designed to protect consumers. Most house builders will have taken legal advice to review their contracts in the light of the Regulations before HBF became involved. However the model terms drawn up in consultation with the OFT will have provided further guidance for HBF members and are likely to have been of particular benefit to smaller house builder members.

6. Other features which impact on a homebuyer's bargaining position when purchasing a new home from a homebuilder.

We can only repeat that there is a great deal of protection for new home buyers, direct and indirect, and that most home builders seek to produce quality products and have satisfied customers. Active buyers, who undertake basic research into local market prices to ensure they are paying a fair market price, who seek appropriate professional advice and follow it, who seek information from the house builder, and who read the material provided about getting the best performance out of their home and the terms of their warranty, should be in a much stronger 'bargaining position' than buyers of most other products or services which do not offer anything like the same level of consumer protection.

Potential new home buyers always have a choice of second-hand products in the local market competing with the new homes offered for sale by house builders.

Home builders operate in local markets and their brand and reputation is of major importance to them in competing with other house builders.

There is an increasing level of sophistication, particularly among second-time and subsequent house buyers who are prepared to bargain over selling prices and seek additional sales incentives. House builders, having paid for land, materials and labour, cannot afford to have stock properties standing unsold because the price is too high, locking up working capital and incurring finance charges. Most HBF members are speculative house builders and have to ensure their new homes are competitively priced to stay in business.

The information available to potential home buyers on new and second-hand products available in their search area, local prices (including actual selling prices) and individual house builders has been enormously increased by the internet, thereby increasing the bargaining position of today's home buyers.

We would add that fundamental conditions of supply and demand influence the relative bargaining strength of all home buyers and sellers, whether new homes or second-hand. In a rising market sellers are in a stronger position, while in a weak market buyers will be at an advantage.

More importantly for the new homes sector, if the Government's planning reforms are successful and produce a step-change in housing supply, new home buyers will be in a stronger position and competition will intensify among house builders. The current system of severe land – and therefore new home – rationing by the planning system is not in consumers' best interests as it will tend to restrict choice and competition. The only permanent solution is to ensure more land is granted planning permission so that housing supply becomes more responsive to demand and there is a better balance between supply and demand.

JCS

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