



## SOME GOOD NEWS... HOME WARRANTY INSURANCE RIGHTS CONFIRMED!

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Home warranty insurance generally protects an owners corporation from being out of pocket for the cost to repair building defects where the builder has been made bankrupt. But what happens when an owners corporation makes a home warranty insurance claim after the builder's bankruptcy ends. Is it then too late for the owners corporation to make the insurance claim? The answer is "no" according to a very recent decision of the NSW Supreme Court.

### Introduction

Home warranty insurance is intended to allow an owners corporation to be indemnified by the insurer for any loss it suffers as a result of incomplete or defective building work where the builder has become insolvent. In practice, this normally gives an owners corporation a right to require a home warranty insurer to organise for defects to be repaired (at the insurer's cost) or to pay compensation to cover the owners corporation for the costs it will incur repairing the defects. However the right for an owners corporation to make a home warranty insurance claim only arises if the builder has become insolvent, for example, because the builder has been made a bankrupt, as a result of which the owners corporation cannot recover its losses from the builder.

### The Typical Scenario

Typically, an owners corporation discovers defects in its building, the builder is already or becomes bankrupt, and the owners corporation lodges a home warranty insurance claim (where that insurance cover exists) whilst the builder is in bankruptcy. But what happens if the owners corporation does not lodge its home warranty insurance claim until after the builder's bankruptcy ends? Is it then too late for the owners corporation to make the home warranty insurance claim because it could recover its losses directly from the builder now that the builder is no longer a bankrupt? In the very recent case of *The Owners – Strata Plan 80647 -v- WFI Insurance Ltd t/as Lumley Insurance* [2015] NSWSC 1161, the NSW Supreme Court held that in those circumstances it was not too late for the owners corporation to make its home warranty insurance claim and obtain an indemnity from the insurer under the insurance policy.

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### **The Lumley Case**

The *Lumley* case involved a residential strata building in Silverwater, Sydney. In about May 2006 the builder, Mr Crestani, entered into a contract with the developer, Versace Developments Pty Ltd, to construct the building. A policy of home warranty insurance was taken out with Lumley Insurance to cover the residential building work to be done by the builder in constructing the building. In August 2008, a strata plan was registered in respect of the building. In 2009, the builder was made a bankrupt. The builder was discharged from bankruptcy in June 2012.

Subsequently, the owners corporation made a claim on the home warranty insurance policy taken out with Lumley Insurance. Lumley denied the claim essentially for two reasons. First, Lumley said that because the builder's bankruptcy had ended, the owners corporation was still entitled to recover compensation from him to cover the cost of repairing the defects as a result of which the owners corporation was not able to claim an indemnity from the insurer under the home warranty insurance policy. Lumley argued this because it said that the owners corporation could not have proved its claim in the builder's bankruptcy and therefore its claim would not have been released when the bankruptcy came to an end. Second, Lumley argued that the owners corporation had made its insurance claim too late and, to be valid, the claim could only be made whilst the builder was still bankrupt.

### **The Decision**

The Supreme Court rejected Lumley's arguments. The Court held that the owners corporation's claim against the builder to recover compensation for the defects that arose from the statutory warranties in the home building legislation was able to be proved in the builder's bankruptcy as a result of which the claim was released when the builder's bankruptcy came to an end. In broad terms, this was because the bankruptcy legislation was meant to give the builder a fresh start, free from most of his debts, once his bankruptcy ended.

Therefore, whilst the bankruptcy legislation said that compensation claims that arose except by reason of a contract are not affected by bankruptcy, the compensation claim of the owners corporation did arise by reason of a contract (being the contract between the builder and developer) and therefore the claim was released when the builder was discharged from bankruptcy. This meant that the owners corporation could not recover compensation from the builder as a result of his bankruptcy and therefore the owners corporation was eligible to make a claim under the home warranty insurance policy held with Lumley.

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The Supreme Court also rejected Lumley's argument that the owners corporation needed to make its home warranty insurance claim whilst the builder was still bankrupt. The Court said that the purpose of the home warranty insurance policy was to allow the owners corporation to obtain an indemnity from the insurer for loss it could not recover from the builder because of his bankruptcy. The Court said that was exactly the predicament in which the owners corporation found itself because of the builder's bankruptcy.

Further, the Court said that the insurance policy did not actually state that a claim needed to be lodged at the time the builder was bankrupt. For those reasons, the Court held that the owners corporation could lodge its home warranty insurance claim with Lumley after the builder's bankruptcy had come to an end.

### **Conclusion**

The Lumley case is good news for owners corporations. The Court decision confirms that owners corporations will generally be able to lodge home warranty insurance claims within the required time limit even if the claim is lodged after the builder's bankruptcy has ended. The Lumley case also confirms that once a home warranty insurance policy has been triggered, the insurer generally cannot claim that the trigger has been undone because of subsequent events, such as the builder's bankruptcy having come to an end.

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