SUBMISSION ON A RE-WRITE OF THE HOME BUILDING ACT 1989

TO: **RE-WRITE OF THE HOME BUILDING ACT 1989**
NSW Fair Trading Policy Division
Department of Services, Technology and Administration
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SUBJECT: The NSW Office of Fair Trading "Consultation Paper: A re-write of the *Home Building Act 1989"* February 2010.

Institute of Strata Title Management Ltd

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SUBMISSION

CONTEXT

1. We refer to the Office of Fair Trading "Consultation paper: A re-write of the *Home Building Act 1989"* February 2010 ("**consultation paper**") and the options for amendments to the *Home Building Act 1989* and regulations discussed therein.

2. This submission aims to highlight and discuss number of key issues raised by the paper, identified in turn below.

ACCESS RIGHTS FOR CONTRACTORS AND INSURANCE FOR RECTIFICATION WORKS

3. We refer to section 5.1.2 and the sixth bullet point under section 6.2 of the consultation paper and comment as follows.

4. The statutory warranties are not promises to return to rectify defective building work. They are promises to do that building work in a particular manner, and to achieve a particular result or outcome.

5. As confirmed in recent Court of Appeal authorites (*Allianz v Waterbrook* [2009] NSWCA 224 (10 August 2009); *Building Insurers Guarantee Corporation v The Owners Strata Plan No. 57504* [2010] NSWCA 23 (2 March 2010)) a breach of statutory warranty gives rise to a right in the beneficiary of that warranty to sue for damages according to the ordinary contractual measure set out in *Bellgrove v Eldridge* [1954] HCA 36 and followed in *Tabcorp Holdings Ltd v*

Bowen Investments Pty Ltd [2009] HCA 8. (That measure is in essence the financial cost of necessary and reasonable rectification work plus any consequential losses.)

6. This then is the starting point: A breach of statutory warranty gives rise to a right to sue for financial compensation. Any mechanism whereby the contractor is given an opportunity to undertake rectification work is a deviation from the underlying legal principle.

7. Ordinarily a building contract itself provides for very limited—if any—rights for the contractor to undertake rectification works. Whilst the contract is on foot and works are underway, the contractor ordinarily has a right to access the site to do works. During this phase the builder is often described as being "in possession" of the site. Many contracts provide for a state of "practical completion", which triggers a "defects liability period". During this period the contractor may have an express (but more likely implied) right to enter the site and undertake works. After this period has expired, there are ordinarily no contractual rights for the builder to attend the site and undertake works.

8. It should also be noted that certain breaches or defaults may give rise to a right in the principal to exclude the contractor from site or to terminate the contract as a whole.

9. In any event, depending on the contractual provisions, at some point the contractor's opportunity to complete the works satisfactorily comes to an end, and any failure to do so crystallizes as damages for breach of contract. Often the point where damages crystallize is said to be when the contractor returns the site to the possession of the principal, however the particular terms of any "defects liability period" may vary this basic concept.

10. At general law, an order from a court to allow a contractor to return to site to undertake works will only arise through the doctrine of *specific performance* in equity. This doctrine will only ever apply where there is a contractual right on foot. As indicated above, if such a right exists, it will only ever exist for a specific and limited period.

11. Moreover, *specific performance* is on principle only available in extraordinarily rare circumstances in relation to building contracts. Ordinarily, factors such as breaches of the contract by the contractor, breakdown in the relationship between the parties and the fact that any order may require the provision of personal services by the contractor mean that a

contractor will not—even if a right is on foot under the contract—be able to obtain an order to allow for entry into site to undertake works.

12. In this context, the powers of the Consumer, Trader and Tenancy Tribunal under section 48O of the *Home Building Act 1989* are understood to be a substantial departure from the underlying legal position. The purpose of these powers is of course clear—to allow for the resolution of building disputes by means other than traditional legal contenst.

13. However the departure from legal principle gives rise to many critical issues. Given these issues, in our view, amendments should be made to ensure that orders for the contractor to access site and undertake works are subject to appropriate conditions.

14. Foremost of these critical issues is that the contract is most likely not on foot. As indicated above, equity will not make orders for *specific performance* unless there is an underlying contractual right in operation.

15. Most disputes in relation to breaches of statutory warranty arise after the contract has been executed (all of the obligations are complete) and the only ongoing issue is the entitlement to damages for breach. In rare circumstances a claim may arise during a "defects liability period", but in practical terms that period is likely to have expired long before the issues in dispute actual come to be heard.

16. Moreover, statutory warranties are often enforced by successors in title—either through section 18C or 18D of the *Home Building Act 1989*. Crucially, the owners corporation of a strata scheme *always* proceeds for breaches of statutory warranty as a successor in title.

17. In this circumstance, not only has the original building contract ceased, but the person bringing a claim for breach was never a party to that contract to begin with.

18. Without ongoing contractual protections, in the event of the contractor returning to site, homeowners and successors in title are exposed to very substantial risks. Allocation of these risks is the foremost point of negotiation when a construction contract is being entered.

19. A brief list of such risks would include:

19.1 risk of the rectification works not being completed or being completed inadequately;

19.2 the nature, extent, and any applicable time limits in relation to any cause of action in respect of 19.1;

19.3 risk of the owner suffering loss, injury or damage caused or contributed to the contractor;

19.4 risk of the owner bearing liability for loss, injury or damage caused by the contractor to third parties;

19.5 risk of the owner bearing liability for demands, suits, claims, penalties, fines etc., by third parties caused by the contractor;

19.6 risk of the owner bearing liability under legislation or other law (for example, in relation to Occupational Health and Safety, workplace injury, public authority consents and approvals, claims by subcontractors under the *Contractors Debts Act 1997)*.

20. I note in respect of many of the above issues, owners corporations bear an extra burden due to their strict liability to repair and maintain common property under section 62 of the *Strata Schemes Management Act 1996*, which may quite easily lead to liability for the owners corporation for many kinds of loss or damage caused by the contractor—including damage to the common property, or loss, injury or damage to third parties caused by damage to common property.

21. Owners corporations are also bound by statutory regulation of their ability to provide access to common property that is only accessible through lots.

22. There is authority from the Consumer, Trader and Tenancy Tribunal to the effect that an order for works to be done under section 48O of the *Home Building Act 1989* may be accompanied by ancillary orders regarding, for example, the standard of those rectification works (such as, in accordance with the statutory warranties).

23. Construction contracts are complex and heavily contested documents and every clause contained within them is the subject of extensive case law.

24. It is an unnecessary demand on the Tribunal to make orders to cover those matters in every instance, there is substantial opportunity for dispute, and many days of hearing may be lost in contesting the particular content and wording of orders to be made. If orders are made on a case-by-case basis, there is significant inconsistency and resulting uncertainty for contractors and home owners in relation to the actual obligations that may apply.

25. Whilst it is not possible to suggest that such orders can practically be made to cover all the terms that would be contained in a negotiated construction contract, the resolution of disputes by way of rectification works may be substantially facilitated if the *Home Building Act 1989* provided for a set of minimum conditions applying in circumstances where works are ordered under section 48O.

Insurance for rectification work

26. Works to rectify defects that result from breaches of statutory warranty are in themselves residential building work (see paragraph (c) of the definition in the *Home Building Act 1989*, in particular the word "repairing").

27. If done under contract, those rectification works must be insured under section 92 of the *Home Building Act 1989* (subject to the works meeting the threshold value).

28. In any event, if done otherwise than under contract, those works must be insured under section 96 of the *Home Building Act 1989* (subject to the works meeting the threshold value).

29. We cannot see that there is any reason to remove this protection.

30. If the protection is to be removed:

    30.1 What protection is to be offered to homeowners instead?

    30.2 Is it suggested that amendments will be made to provide that the works will be covered under the original policy?

30.3 If they are to be covered under the original policy, what will the period of cover be?

30.4 What, for example, would occur where rectification works are done after the expiry of the period of cover under the original insurance?

COMMENCEMENT OF TIME LIMITS

31. We agree that the inadequate definition of when relevant time limits and periods of cover commence under the *Home Building Act 1989* requires amendment.

32. We note that any amendment should not retrospectively apply to claims on foot or finalised.

33. Clause 61(1) of the *Home Building Regulation 2004* presently provides:

> *(1) For the purposes of determining the period of cover to be provided by an insurance contract in relation to residential building work, work is taken to be complete:*
>
> *(a) on the date that the work is completed within the meaning of the contract under which the work was done, or*
>
> *(b) if the contract does not provide for when work is completed or there is no contract, on the date of the final inspection of the work by the applicable principal certifying authority, or*
>
> *(c) in any other case, on the latest date that the contractor attends the site to complete the work or hand over possession to the owner or if the contractor does not do so, on the latest date the contractor attends the site to carry out work*

34. This clause has also been incongruously applied in relation to the time limit to commence proceedings for breach of statutory warranty (see the District Court decision of Elkham SC DCJ in *Abrahams v Degan* [2009] NSWDC 315 (5 June 2009)).

35. In our view this test is inappropriate primarily due to the reliance on the contractual meaning.

36. A given contract may ascribe no particular meaning to completion, it may have a number of express versions of completion (including practical completion and perhaps even final

completion) and there may be a variety of implied meanings. This results in both significant dispute as to the contractual terms (which may not even be available to be put into evidence) as well as significant inconsistency between decisions and the attendant lack of certainty for contractors and consumers that results.

37. Section 109ZK(1) of the *Environmental Planning and Assessment Act 1979* provides for the commencement of its particular time limit as follows:

> *1) Despite any Act or law to the contrary, a building action may not be brought in relation to any building work:*
>
> *(a) more than 10 years after the date on which the relevant final occupation certificate is issued, or*
>
> *(b) in a case where no final occupation certificate is issued, more than 10 years after:*
>
> *(i) the last date on which the building work was inspected by a certifying authority, or*
>
> *(ii) if no such inspection has been conducted, the date on which that part of the building in relation to which the building work was carried out is first occupied or used.*

38. The key element of this test—the occupation certificate—is in our view the clearest and most easily evidenced option and provides the greatest degree of clarity and certainty.

ALIGNING PERIODS OF COVER AND TIME LIMIT TO COMMENCE PROCEEDINGS

39. The consultation paper appears to suggest 'aligning' periods of cover and time limits to commence proceedings for breach of statutory warranty by reducing the later to match the former.

40. We fail to see how clarity in this regard either should, or could, be achieved by reducing the rights of homeowners.

41. Significantly, the consultation paper refers only to the 2 year non-structural, and 6 year structural periods of insurance cover, and fails to mention the 1 year period of cover for non-completion claims.

42. Is it proposed to replace one statutory time limit with three, each delineated by definitions of completion, structural and non-structural?

43. Moreover, these three new time bars would sit beside the existing time bar for proceedings for breach of the construction contract itself—which is 6 years under the *Limitation Act 1969*.

44. Accordingly such a proposal would substantially extinguish homeowners rights under the *Limitation Act 1969* to sue for breach of the building contract for 6 years from breach.

45. Rather than serving as consumer protection legislation, the *Home Building Act 1989* would be actively destroying consumer's rights, leading to the absurd conclusion that principals contracting for construction of commercial premises would have stronger rights under their contracts than homeowners.

46. Rather than achieving clarity, the proposal would provide in essence for the most complicated scheme of statutory time bars in New South Wales.

47. We fail to see how clarity is achieved by the creation four separate categories of breach of contract, creating fertile ground for dispute and litigation. We fail to see how it can achieve clarity to require parties to argue whether each particular issue in dispute is (a) a breach of statutory warranty by way of non-completion, (b) a breach of statutory warranty resulting in a non-structural defect, (c) a breach of statutory warranty resulting in a structural defect, or (d) any other breach of contract.

48. Surely if the true motivation is to achieve clarity, the most appropriate route would be the opposite—to bring the periods of insurance in line with the time limit to commence proceedings for statutory warranty.

49. Short time limits to commence proceedings, such as 1 or 2 years, are in themselves substantial injustices.

50. For strata schemes in particular, there is very little prospect of ever being able to commence proceedings within a time limit of 1 or 2 years.

51. Until the First Annual General Meeting, an owners corporation is under the control of its developer. That First Annual General Meeting, in practice, may be many months after the building is complete. Depending on the size of the scheme, and the speed of sales of the units, it is conceivable that an owners corporation may remain under the control of its developer beyond the expiry of a 1 year time limit, and even (given the right circumstances) beyond the expiry of a 2 year time limit.

52. Owners corporations are bound to make decisions in accordance with the *Strata Schemes Management Act 1996*, which requires meetings to be held and has strict requirements for notice.

53. Even if immediate action is taken, and appropriate meetings put in place as soon as possible, proceedings must be commenced with sufficient particulars. This will ordinarily require an expert's report to be obtained. Depending again on the size of the scheme, the process of obtaining a report alone may take many months.

54. In strata schemes it is not uncommon for delays to occur in this process due to the need to obtain access to units. If access is disputed, the *Strata Schemes Management Act 1996* sets out required procedures for the owners corporation to gain access—which include the need to obtain adjudicators orders through processes overseen by the Consumer, Trader and Tenancy Tribunal.

SUCCESSOR IN TITLE AND REED CONSTRUCTIONS

55. The consultation paper proposes that some unspecified amendments may be made to replace the term "successor in title" with "warranty beneficiary". The concept of "successor in title" is a core concept to sections 18C and 18D and has an intimate effect on their operation.

56. *The Owners Strata Plan 61424 & Anor v Reed Constructions Pty Limited* [2009] NSWSC 692 considered certain arrangements, which are not uncommon in practice, that seek to rely on

the operation of the term "successor in title" to avoid liability under sections 18C and 18D of the *Home Building Act 1989*.

57. The case highlighted various deficiencies in the structure of both sections 18C and 18D of the *Home Building Act 1989* that allow, or may allow, for the intention of the act to be circumvented by the creation of specific relationships between parties involved in the construction of residential buildings.

58. The case is presently in the Court of Appeal with judgment expected shortly.

59. In summary, if the party who contracts with the builder, and the party who owns the land the subject of the development, are different parties, it is possible for successors in title to be excluded from their rights under section 18C and 18B of the *Home Building Act 1989.*

60. This may occur under section 18C as the successor in title (assuming they are the immediate successor to the "developer") may not be a successor to a party on whose behalf the work was done for the purposes of section 3A of the *Home Building Act 1989* as its predecessor in title did not contract with the builder.

61. This may occur under section 18D as the successor in title may not be a successor to a party entitled to the benefit of the warranties as its predecessor in title did not contract with the builder.

62. Regardless of the decision of the Court of Appeal in *Reed*, we suggest that amendments be made to ensure that the liability of builders and developers cannot be avoided as indicated above.

PROPORTIONATE LIABILITY

63. The *Home Building Act 1989* imposes a special liability on certain developers as if they were contractors who had done the work under a contract with immediate successors in title (sections 18C and 3A of the *Home Building Act 1989).*

64. If Part 4 of the *Civil Liability Act 2002* applies to claims for breach of statutory warranty, it may be that any liability on the developer is in effect illusory and at significant risk of being reduced by the operation of that Part to a very low proportion, or no proportion at all.

65. In our view this cannot be the intended operation of the *Home Building Act 1989* and accordingly amendments should be implemented to ensure that claims for breach of statutory warranty are excluded from the operation of Part 4 of the *Civil Liability Act 2002*.

DEFECTS VISIBLE AT THE TIME OF PURCHASE

66. Owners corporations should clearly be exempt from any exclusion in policies for defects reasonably visible at the time of purchase as they are successors in title by force of statute who came into existence at the time of acquiring the property (and accordingly had no opportunity to inspect).

ACCESS TO INSURANCE IN EVENT OF INSOLVENCY

67. There is a degree of uncertainty in relation to the interaction between insolvency, death, or disappearance of a contractor and the period of cover under last resort insurance policies.

68. Amendments should be made to ensure clarity as to whether, for example, the contractor must become insolvent within the period of cover for a claim to be available.

MULTI-STOREY EXEMPTION

69. The consultation paper discusses making changes to the multi-storey insurance exemption in relation to part-residential/part-commercial buildings.

70. We are however of the view that the exemption for the requirement to obtain insurance for multi-storey buildings should be removed.

71. Substantial numbers of home-owners across New South Wales find themselves without protection of insurance in these schemes.

72. Owners corporations in buildings without insurance due to this exemption are particularly vulnerable to single-use vehicle developments, arrangements such as those considered above in relation to *The Owners Strata Plan 61424 & Anor v Reed Constructions Pty Limited* [2009] NSWSC 692, and "phoenix" company activity by builders as discussed in the consultation paper.

73. It has been the position of the ISTM for an extended period that the exemption is substantially unjust in operation, having an unjustifiable harsh impact upon many innocent homeowners in New South Wales.

74. With the passage of time those affected by the exemption simply continues to mount.

75. The Institute and its members stand willing to provide numerous examples of the injustice of this exemption at work and invite the Office of Fair Trading to enter into discussions with the Institute in this regard.

ABOUT ISTM

INTRODUCTION

The Institute of Strata Title Management (ISTM) is the peak industry body for strata and community title management in New South Wales representing strata managers and other stakeholders.

The ISTM's 1300-strong membership includes strata managers, who hold either a license or a certificate of registration, employees of strata management businesses, and suppliers of products or services to both the strata industry and owners corporations.

ISTM has a range of capabilities and undertakes activities in education, representation and provision of information.

EDUCATION

ISTM provides entry level training into the industry and ongoing professional development. ISTM is Registered Training Organisation and provides a vigorous professional development program linked to levels within the Centre of Professional Development and a range of management training.

Additionally ISTM will negotiate educational pathways within the secondary and tertiary sectors.

REPRESENTATION

ISTM currently represents the industry in NSW through membership and representation on the national body for strata, body corporate and community title management, the National Community Titles Institute (NCTI), liaison with all levels of government and representation of the views of

members through public relations activities. ISTM is engaging with a broader range of strata sector stakeholders and aims to speak with one voice as the expert on a number of issues.

INFORMATION AND DECISION SUPPORT

ISTM is currently a point of reference for the industry for information and interpretation of strata legislation and regulations. ISTM provides information through newsletters, online and by telephone.

ISTM is developing a Knowledge Hub and Research Centre that collates strata industry data and drives research in the sector. This data will be provided exclusively to members and forms a key aspect of the ISTM member value proposition and engagement strategy. In addition the ISTM supports academic research for emergence of research based rather than reactive legislative change.

MEMBERSHIP SCOPE

The strata industry has a wide range of stakeholders beyond strata title managers and their employees. These include property developers, architects, local government planning officers, solicitors, accountants, tradespeople, insurers, bankers, property valuers, quantity and land surveyors, tourism policy-makers, hotel owners and retirement village operators.

ISTM's membership is organised across the industry sectors as follows:

- Licensed Managers (Licensed Manager Chapter): Open to strata managers in their own business, and employed strata managers who hold a License. (311 members).
- Suppliers (Supplier Chapter): Suppliers of goods & services to the Strata industry. (266 members).
- Strata Certificate holders (Associate Chapter): Open to holders of a Strata Certificate, who generally include employed strata personnel. (370 members).
- Students (Associate of the Institute): Open to trainees and students planning to become strata managers. Non-voting membership (133 members).

- Corporate (Corporate Members): Open to a company or corporation controlled by a member of ISTM and to strata companies and to suppliers of goods and services to the strata industry. Non-voting membership. (205 members).
- Group Title Scheme: Open to strata and community title schemes, not to individual persons. (7 members).