PIKES & VEREKERS
LAWYERS

WHAT EFFECT WILL THE *BROOKFIELD* DECISIONS HAVE ON THE LIABILITY OF CERTIFIERS?

Paper given by Brian Walton

to the Australian Institute of Building Surveyors Annual Conference
12-13 August 2013

INTRODUCTION

Following the recent NSW Supreme Court decisions in *Owners Corporation Strata Plan 72535 v Brookfield Australia Investments Limited* [2012] NSWSC 712 (**the Star of the Sea case**) and *Owners Corporation Strata Plan 61288 v Brookfield Multiplex Limited* [2012] NSWSC 1219 (**the Chelsea case**), it is currently the law in NSW that builders and developers do not owe a duty of care to subsequent property owners, such as Owners Corporations, and are therefore not liable for claims in negligence for defective building works brought by successors in title to developers.

It remains to be seen whether the reasoning in the *Brookfield* decisions will be extended to certifiers who are arguably in a different position to that of builders and developers because of their statutory duties but until one of the many test cases currently being litigated in the NSW Supreme Court is decided, one thing is certain: Owners Corporations and subsequent property owners, particularly those who are outside of the six year statutory warranty period, will be increasingly looking to bring negligence claims against certifiers, who make attractive defendants due to their professional indemnity insurance.

Until the position regarding the liability of certifiers for defective building work is resolved certifiers will need to take particular care to ensure that their liability is limited in their contracts of engagement to the fullest extent possible under the law.

THE *STAR OF THE SEA* CASE

Background

The *Star of the Sea* case involved a resort-style development known as the "Star of the Sea", which comprised 52 residential units in four low-rise buildings in Terrigal. The development was designed and constructed by Brookfield, the first defendant, in accordance with a D&C contract entered into with the developer and property owner, Hiltan, the second defendant. Upon completion a strata plan was registered

and title to the property passed to the Owners Corporation. Sometime thereafter, a number of structural defects in the building work became apparent.

As is commonly the case (or at least it was prior to this case) the plaintiff Owners Corporation commenced proceedings against both Brookfield and Hiltan claiming:

1. Breach of contract because they had each breached the statutory warranties contained in Section 18B of the *Home Building Act* 1989 (NSW) (**HBA**) implied into all residential home building contracts and owed to the Owners Corporation by reason of Section 18D of the HBA; and

2. Negligence because the defective building work constituted a breach of the common law duty of care they each owed to the Owners Corporation by reason of the High Court decision in *Bryan v Maloney* [1995] 182 CLR 609 (***Bryan v Maloney***).

Duty of care – state of the law prior to the *Star of the Sea* case

The salient facts of *Bryan v Maloney* were that the builder, Bryan, had built a house for his sister-in-law, Mrs Manion who later sold the property to Mrs Maloney. Shortly after purchasing the property Mrs Maloney noticed severe cracking which was found to be the result of subsidence due to defective footings. The High Court held that Bryan owed Mrs Maloney a duty of care to prevent pure economic loss because sufficient proximity existed between the builder and the subsequent owner.

Bryan v Maloney has been extensively criticised and not widely followed.

In *Woolcock Street Investments Pty Limited v CDG Pty Limited* [2004] HCA 16 (***Woolcock***) the High Court unanimously held that the duty of care owed by the builder in *Bryan v Maloney* did not extend to commercial premises. In *Woolcock* the High Court held that the concept of "proximity" was no longer the "conceptual determinate" of whether a duty of care will be imposed and that there were specific policy concerns portioned against extending a duty of care to a commercial context.

Importantly, *Woolcock* made it clear that an analysis of the relationship between the builder and the original owner must first be carried out. If no duty of care exists between owner and original owner, a subsequent purchaser is unable to apply the reasoning in *Bryan v Maloney* to establish a duty of care owed to it by a builder.

In addition to the demise of the concept of proximity the continued operation of *Bryan v Maloney* in NSW has been doubted since the statutory warranties were introduced into the HBA in 1996 but although the question as to whether the statutory warranties displace the "vulnerability" of a plaintiff and thereby displaced duties of care for the purposes of negligence actions had been discussed (eg. in *Eko Investments Pty Ltd v Austruc Constructions Ltd* [2009] NSWSC 208 and *Atkinson & Crowley*) it was not until the *Star of the Sea* case that a Court of superior jurisdiction was specifically required to decide it.

The decision

In *Star of the Sea* Justice McDougall dismissed the negligence claim brought against the builder and developer on the grounds that neither Brookfield nor Hiltan owed the Owners Corporation a duty of care because:

(a) the Owners Corporation had the benefit of the statutory warranties under the HBA and "In circumstances where the legislature has considered, and made clear provision for, the extent to which a builder is liable to a subsequent owner, I think that the courts should be slow to substitute their own judgment for the legislature" (see para. [144]).

In other words, McDougall J concluded that the parliament intended the statutory warranties to be the vehicle for a claim for defective building work and the Court should not hold "*some additional common law duty of care should be imposed*" (see para. [114]).

(b) the decision in *Bryan v Maloney* was based upon the concept of "*proximity*" which has since been discarded as the basis for imposing a duty of care (per *Woolcock*).

(c) as set out in *Woolcock* the finding that a duty of care was owed by the builder to the subsequent owner of the house in *Bryan v Maloney* rested on the "anterior step" of finding a duty between the builder and the original owner. McDougall J held that no such "anterior" duty could arise as Brookfield and Hiltan "*had negotiated, on what seems to be in equal footing, a detailed contract in which each bargained for what it would give as the price for what it would receive*" (see para. [146]).

Although His Honour held that the issue did not need to be decided, and His Honour's views on this point must be considered dictum, McDougall J further said that, since he had held that the Owners Corporation had the benefit of the statutory warranties, it was questionable whether the Owners Corporation was "vulnerable" in the sense considered in *Perre v Apand* (1999) 198 SLR 180 and *Woolcock* (see paras. [149]-[150]). This aspect of His Honour's decision appears consistent with the approach taken by Bergin J in *Eko Investments Pty Limited v Austruc Constructions Limited & Ors* [2009] NSW SC 208.

THE *CHELSEA* CASE

Background

The plaintiff in the *Chelsea* case was the Owners Corporation of serviced apartments located in Chatswood operated under the name "Mantra Chatswood Hotel" which had been built by Brookfield in accordance with a D&C contract with the developer and original property owner, Chelsea Apartments Pty Limited.

Unlike in the *Star of the Sea* case it was common ground between the parties that the Owners Corporation did not have the benefit of the statutory warranties in the

HBA due to the fact that the apartments were used for the purposes of overnight accommodation (i.e. a commercial use).

Again, the Owners Corporation sought to rely upon *Bryan* in support of the existence of a duty of care owed by a builder to a subsequent owner (in this case of commercial property).

The Decision

The *Chelsea* case was again decided by McDougall J who held that Brookfield did not owe a duty of care to the Owners Corporation for negligently causing economic loss on the following grounds:

(a) The Owners Corporation was unable to point to an authority (apart from *Bryan v Maloney*) in support of the existence of such a duty.

(b) *Bryan v Maloney* was not authority for the imposition of a duty of care for the reasons His Honour set out in the *Star of the Sea* case, namely that:

    (i) the conclusion in *Bryan v Maloney* that the builder owed a duty of care to a successor in title to the persons for whom the house had be constructed depended upon the ulterior conclusion that the builder owed a duty of care to the original owner.

    (ii) As in the *Star of the Sea* case, in circumstances where Brookfield and Chelsea Apartments had carefully negotiated out, in detail, the terms of their bargain, there was no reason for imposing separate duty of care as between the parties.

As will be seen, of major importance to the decision in the *Chelsea* case was the fact that Chelsea and Brookfield were both sophisticated and experienced parties that had negotiated with each other at arms-length and on equal footing, a detailed D&C contract containing, in particular detailed contractual provisions relating to the quality of the services that Brookfield was to provide. In coming to the conclusion he did, McDougall J endorsed the dissenting view of Brennan J in *Bryan v Maloney* to the effect that a finding of such a duty would be "tantamount to the imposition on the builder of a transmissible warranty of quality" (at para. [92]).

McDougall J also observed that the NSW legislature had put in place a comprehensive regime for the protection of those who buy residential property and had specifically decided to exclude commercial developments such as the Mantra Chatswood Hotel from that statutory scheme. The invitation by the Owners Corporation was thus not only for McDougall J to identify and impose a novel duty of care as a judge at first instance, but for His Honour to go where the legislature decided, as a matter of policy, it would not.

The issue of vulnerability of the Owners Corporation was raised by *Brookfield* in opposition to the identification of a novel duty. His Honour indicated that while the argument relating to vulnerability was ventilated fully in submissions, there was no purpose in offering an opinion on that issue when His Honour had already

concluded it was not appropriate to undertake the imposition of a novel duty of care at the trial level.

WHAT DOES THIS ALL MEAN FOR CERTIFIERS?

In short, we don't know yet. Whilst there is little doubt that the reasoning in the *Brookfield* decisions extends to subcontractors, such as plumbers and electricians and even project managers and construction managers, the position held by the certifier, who is required to independently carry out his or her statutory duties which include carrying out critical stage inspections and certifying a building is suitable for occupation is, for the time being at least, uncertain.

The uncertainty is a result of the fact that although McDougall J in the *Brookfield* decisions ventured that he did not think that an owner of residential property could be "vulnerable" to a builder's or developer's negligent building work because they had the protection of the statutory warranties, he said that his decisions in those cases did not turn on a determination of whether the statutory warranties extinguished common law rights.

There are currently many cases being run in the Supreme Court of NSW involving negligence claims brought by owners corporations and other successors in title against PCAs and accredited certifiers for defective building works. We are currently involved in a number of these cases and I am pushing to have the question whether certifiers owe subsequent owners a duty of care decided, most likely by McDougall J, as quickly as possible to remove the current uncertainty.

My view is that the reasoning of McDougall J in the *Brookfield* decisions should be extended to apply to certifiers, for it would be anomalous for certifiers to be liable for building works negligently carried out by builders and developers where builders and developers cannot be liable for their work. However, the Chelsea case is currently on appeal and this may limit or quash the operation of the *Brookfield* decisions.

The Victorian Position

The current position in Victoria is that a building surveyor does owe a duty of care to prevent subsequent owners from suffering loss caused by negligent building works.

In *Moorabool Shire Council v Taitapanui* (2004) VSC 239 (***Moorabool***), the Victorian Supreme Court held that a private building surveyor, Mr Mellis, who in exercising his statutory functions under the *Building Act* 1993 (Vic) owed a duty of care to the subsequent owners of residential property, the Taitapanuis, even though the Taitapanuis had the benefit of the statutory warranties under the *Domestic Buildings Contract Act* 1995 (Vic).

In stark contrast to the reasoning of McDougall J in the *Brookfield* decisions, in *Moorabool*, Smith J held that "*the imposition upon a private building surveyor of a duty of care to subsequent purchasers would help to secure the intended comprehensive and fair operation of the statutory scheme. It would also reinforce the statutory and regulatory obligations. That is of particular importance in relation*

to private building surveyors where the profit motive, while encouraging the desired efficiency, will also tempt the cutting of corners" (see para. 121).

Of particular importance to the decision of Smith J was that Mr Mellis voluntarily accepted, for a fee, appointment under the statutory scheme to carry out the statutory and regulatory role of issuing a building permit and carrying out inspections for the particular building. He voluntarily assumed the responsibilities of that role and purported to carry it out. Before he could issue a building permit, he had to be satisfied that the building work and the building permit would comply with the Act and Regulations and so comply with all the relevant standards. "*In performing these functions he was expressly required to work in a competent manner and to a professional standard.*" (at para. [124]).

Smith J held that the standard of care held by a building surveyor was even higher than those that ordinarily undertake the exercise of statutory powers or provide professional services because "*the private building surveyor was required to do more than provide information or advice or to exercise statutory powers should facts that came to his attention warrant actions. The statutory powers he voluntarily assumed and exercised were intended to ensure that the builder did its work in accordance with the Act and Regulations and the standards they impose. He was required to look for problems and deal with them. His role was critical. He was the gatekeeper and watchdog and the only one. He was, or should have been, well aware of his responsibilities and the critical nature of them.*" (see para. [125]).

The Position in NSW

However, as I am currently arguing in the cases we are running on behalf of certifiers defending negligence claims, the position is different in NSW because:

1. *Moorabool* was decided on the grounds that *Bryan v Maloney* was authority for the imposition of a general duty of care owed by builders to subsequent owners whereas McDougall J held in the *Brookfield* decisions that *Bryan v Maloney* was not authority for the imposition of a general duty of care but was rather decided on the basis that the builder owed the original owner a duty of care.

   In *Moorabool* Smith J held that "*assuming Brian v Maloney do be good law, it seems to me that ordinary members of the public would regard it as unreasonable that a building surveyor, not only closely involved in, but ultimately responsible for allowing negligent design and construction of the building, should not find himself liable for breach of duty of care to a subsequent purchaser <u>when the builder would be so liable</u>*" (see para [117]).

   In light of the fact that the *Brookfield* decisions are authority for the proposition that, in NSW, a builder (or developer) is not liable for the negligent design and construction of a building I would argue that *Moorabool* has no application in NSW.

2. Moreover, McDougall J in the *Brookfield* decisions held that courts should not impose an additional common law duty of care in circumstances where subsequent owners have the protection of the statutory warranties.

Possible Fire Safety exception

The waters are further muddied by the one and only case in NSW where the Supreme Court held a certifier was liable to an owners corporation for negligently performing its duties: *The Owners Corporation of Strata Plan 62254 v Rockdale City Council* [2008] NSWSC 392. However, in that case the Council was the PCA and it had negligently issued an occupation certificate despite the fact it was aware that the building did not have fire sprinklers fitted or any of the other fire safety requirements for a building in excess of 25 metres.

I would argue that the operation of *Rockdale City Council* is limited to the very specific set of facts present in that case and has no application to cases that most commonly involve defects arising from poor workmanship.

CONCLUSION

Although I am concerned that the *White Paper* appears to suggest that certifiers can be liable for defects arising from poor workmanship even when the statutory warranty period expires, I believe that based on the reasoning of McDougall J in the *Brookfield* decisions a certifier cannot be liable for defective building work in NSW. But at the same time the *Brookfield* decisions reinforce the importance of the contract as the determinative source of liability between parties in a commercial context. Therefore, to ensure their liability is limited as per *Brookfield* certifiers need to make sure that they have detailed contracts in place limiting their liability to the specific performance of their obligations.