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RECENT DEVELOPMENTS CONCERNING THE LIABILITY OF BUILDING PROFESSIONALS IN NSW

Paper given by Brian Walton

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Introduction

The past year has seen further significant changes to the law in NSW as it relates to the liability of building professionals for defective building works carried out by a builder or head contractor:

- On 25 September 2013, the NSW Court of Appeal handed down a landmark decision in *Owners - Strata Plan No 61288 v Brookfield Australia Investments Ltd* [2013] NSWCA 317, unanimously overturning the NSW Supreme Court's finding that a builder (or developer) did not owe a duty of care to subsequent property owners, such as Owners Corporations, to avoid negligent building works resulting in latent defects causing pure economic loss (NB. different principles apply to negligence causing personal injury).¹
- This decision has implications for building professionals contracted by the builder or developer, such as architects, engineers and surveyors, who are found to have contributed to the loss and may be held liable by virtue of the proportionate liability regime contained in Part 4 of the *Civil Liability Act 2000* (NSW). This is of particular significance as such professionals make attractive defendants by reason of their professional indemnity insurance.
- The *Home Building Amendment Bill 2014* (NSW) was passed unamended by the NSW Parliament on 28 May 2014. This Bill, once proclaimed, significantly amends the *Home Building Act 1989* (NSW) and accredited building surveyors should be aware of the changes and how they may affect their business.

¹ The NSW Supreme Court decision of McDougall J in *Owners Corporation Strata Plan 61288 v Brookfield Multiplex Limited* [2012] NSWSC 1219 was the subject of the paper presented by the author at the AIBS 2013 Annual Conference.

Owners – Strata Plan No 61288 v Brookfield Australia Investments Ltd [2013] NSWCA 317

This case concerned the construction of a mixed-use retail, restaurant, residential and serviced apartments building in Chatswood, New South Wales by Brookfield Multiplex in 1999. The appellant, the Owners Corporation for the serviced apartments, came into existence after completion of the building work on registration of the strata plan for the serviced apartments. Some years later, it discovered latent defects in the common property and, in 2008, brought proceedings against Brookfield in negligence for pure economic loss.

Prior to the hearing, the parties agreed that the Owners Corporation was not a residential building under *Home Building Act 1989* (NSW) and so it was not entitled to the benefit of statutory warranties prescribed in s18B of the Act.

What gives rise to the duty of care?

The Court held that the vulnerability of the purchasers was a key factor in identifying the scope of a duty of care for pure economic loss. Vulnerability refers to the purchaser's inability to protect itself from the consequences of the builder's failure to exercise reasonable care when carrying out the building work; whether that be in a physical sense (controlling the physical events that gave rise to the loss) or a legal sense (negotiating a contractual arrangement imposing liability on the builder).

The Owners were found to be vulnerable in that:

- the defects were latent and could not have been discovered by a purchaser exercising reasonable care;
- the Owners Corporation was unable to enter into a contract with the developer prior to it becoming the owner of the common property in order to protect itself from the risk of defects; and
- the developer was itself vulnerable to the acts or omissions of Brookfield (in the absence of any contractual limitation to the contrary).

The Court, albeit in *obiter*, went on to recognise the potential for:

- a concurrent duty as between the developer and Brookfield beyond that anticipated by the building contract (in the absence of clauses limiting liability for latent defects); and
- a subsequent purchaser being entitled to rights against Brookfield which were not rights held by the developer.

What is the scope of that duty?

However, a builder will not be liable to subsequent owners for all defects in the construction of a building. The Court of Appeal found that a builder had a duty to avoid causing a property owner loss resulting from latent defects in a building that were:

1. structural defects;
2. defects which constitute a danger to persons or property in the vicinity of a building; or
3. defects which render a building uninhabitable.

The Court left open the possibility that a builder could be found liable for latent defects that did not fall within these three classes if the circumstances warranted and it will be interesting to see whether the recent departure from the concept of "structural defects" by the legislature in the *Home Building Amendment Bill 2014* (NSW) (see below for a more detailed explanation) has the consequence of broadening the scope of the tortious duty.

How does this affect the liability of certifiers?

The Court of Appeal's decision is authority for the proposition that a property owner can be owed a common law duty of care even when it has the benefit of the statutory warranties scheme and affirms the importance of the concepts of "vulnerability" and "reliance" in determining whether building professionals will be liable to subsequent owners (successors in title to the developers) if their negligence caused, or were a cause, of the owners' loss resulting from latent defects of the classes above.

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 arguably in a different position to other building professionals because the certifier plays no active role in the design or construction of a building. On the contrary, the certifier is placed in a most difficult position where, for the most part, he or she is forced to rely upon the engineer or architect engaged by the builder or developer to have performed their duties with due care and skill. In many respects, the role of the certifier is more that of a compliance officer than quality control. In these circumstances, it is difficult to see how the certifier could be said to have assumed any responsibility for the risk of latent defects or that a developer places any reliance on the certifier to protect it from the risk of latent defects.

Nevertheless, 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, particularly in circumstances where the builder or developer, or both, have become bankrupt or been placed into administration. This is because building professionals have professional indemnity insurance making them attractive defendants. Accordingly, certifiers should take the following practical steps to limit their liability for latent defects:

- (a) express provisions in their contracts of engagement excluding or limiting liability for latent defects;
- (b) express provisions in their contracts of engagement excluding liability in negligence to subsequent purchasers contracts; and
- (c) express provisions in their contracts excluding proportionate liability.

Finally, the Court of Appeal's decision is itself the subject of an appeal to the High Court, which was heard by the full bench on 18 June 2014, meaning that there could be further changes to the extent of a certifier's liability for the defective building works of others when the High Court's decision is handed down later this year.

Home Building Amendment Bill 2014 (NSW)

The *Home Building Amendment Bill 2014* (NSW) became law on 28 May 2014. Upon its commencement, the precise date of which is not yet known, the Bill will introduce a number of significant changes to the *Home Building Act 1989* (NSW), in particular, to the scope of the statutory warranties scheme found in Part 2C of the Act. The statutory warranties scheme establishes legally enforceable standards for the quality and performance of building work. The three key changes the new Bill introduce into this scheme are:

- (a) replacing "structural defect" with "major defect" to ensure cover is afforded for a significant defect that may not be considered a structural defect;
- (b) extending the statutory warranties to subcontractors; and
- (c) the introduction of a new statutory defence for builders if they reasonably relied on the care and skill of building professionals contracted by the developer including PCAs and accredited building surveyors.

"Major defect" replaces "structural defect"

The *Home Building Amendment Bill 2014* (NSW) replaces the definition of "structural defect" in section 18E of the HBA with the concept of "major defect". A "major defect" is defined in new section 18E(4) as:

- (a) *"a defect in a major element of a building that is attributable to defective design, defective or faulty workmanship, defective materials, or a failure to comply with the structural performance requirements of the National Construction Code (or any combination of these), and that causes, or is likely to cause:*
 - (i) *the inability to inhabit or use the building (or part of the building) for its intended purpose, or*
 - (ii) *the destruction of the building or any part of the building, or*
 - (iii) *a threat of collapse of the building or any part of the building, or*
- (b) *a defect of a kind that is prescribed by the regulations as a major defect."*

A "major element" is also defined in section 18E(4) as:

- (a) *“an internal or external load-bearing component of a building that is essential to the stability of the building, or any part of it (including but not limited to foundations and footings, floors, walls, roofs, columns and beams), or*
- (b) *a fire safety system, or*
- (c) *waterproofing, or*
- (d) *any other element that is prescribed by the regulations as a major element of a building.”*

Accordingly, whether a defect is a “major defect” will be determined by a two-step test:

1. Is the defect in a major element of the building such as load bearing walls, fire safety systems and waterproofing? and
2. What is the severity of the consequences of the defect to the building?

The Bill contemplates a regulation making power to prescribe other major defects and other major elements so it remains to be seen to what extent the scope of the above definitions may change as litigation under the new regime is decided.

The limitation period for commencing proceedings for an alleged breach of a statutory warranty remains 6 years for a “major defect” and 2 years for defects that are not major defects.

Statutory warranties by subcontractors

The Bill provides that the statutory warranties will be implied into every contract to do residential building work, not just contracts between the builder and the owner of the land. Accordingly, subcontractors will also be responsible to the principal contractor for any breach of the statutory warranties by the subcontractor, hence providing back-to-back protection for the principal contractor.

Builder not liable for defects if reasonable reliance placed on building professionals contracted by the developer

The Bill introduces a new statutory defence of reasonable reliance into section 18E of the *Home Building Act 1989* (NSW):

Section 18E Defences:

1. *In proceedings for a breach of a statutory warranty, it is a defence for the defendant to prove that the deficiencies of which the plaintiff complains arise from:*
 - (a) *instructions given by the person for whom the work was contracted to be done contrary to the advice of the defendant or person who did the work, being advice given in writing before the work was done, or*
 - (b) *reasonable reliance by the defendant on instructions given by a person who is a relevant professional acting for the person for whom*

the work was contracted to be done and who is independent of the defendant, being instructions given in writing before the work was done or confirmed in writing after the work was done.

2. *A relevant professional is independent of the defendant if the relevant professional was not engaged by the defendant to provide any service or do any work for the defendant in connection with the residential building work concerned.*
3. *A relevant professional is not independent of the defendant if it is established that the relevant professional:*
 - (a) *was engaged on the basis of a recommendation or referral of the defendant to act for the person for whom the work was contracted to be done, or*
 - (b) *is, or was within 3 years before the relevant instructions were given, a close associate of the defendant.*
4. *In this section, relevant professional means a person who:*
 - (a) *represents himself or herself to be an architect, engineer or surveyor, or*
 - (b) *represents himself or herself to have expert or specialised qualifications or knowledge in respect of residential building work or any particular aspect of residential building work, or*
 - (c) *represents himself or herself to be engaged in a profession or to possess a qualification that is recognised by the regulations as qualifying a person as a relevant professional.*

The increasing involvement of building professionals in residential home building means that it will quickly become common practice for builder defendants to plead reliance on building professionals and the test of reasonableness implicit in this defence is certain to become a key focus of litigation alleging a breach of the statutory warranties under the *Home Building Act 1989* (NSW).

The result may well see an increase in concurrent negligence claims being brought against building professionals including PCAs and accredited surveyors (classes A1 - A3) in proceedings brought by property owners alleging breach of the statutory warranties by a builder or developer in order to alleviate any risk that a builder may successfully avail themselves of this new statutory defence.

For the reasons stated above, the author would argue the extent to which a builder or developer relies on the PCA or accredited surveyor to protect it against the risk of latent defects is limited at best, but the introduction of this new statutory defence serves only to increase the importance for certifiers to ensure their contracts expressly limit their liability for defective design and/or construction to the fullest extent permitted under the law.

Pikes & Verekers Lawyers would be happy to offer their assistance in drafting contracts ensuring you are adequately protected or to advise you on your legal rights in defence of claims alleging you bear responsibility for building defects.