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Précis Paper

2017 in Review: Strata Case Law Update

A discussion of a number of 2017 decisions in relation to Strata.

Discussion Includes

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Précis Paper

2017 in Review: State Case Law Update

1. In this edition of BenchTV, Paul Jurdeczka (Partner – Mills Oakley, Sydney) and Carlos Mobellan (Barrister – 3 St James' Hall Chambers, Sydney) discuss a variety of 2017 decisions from NSW dealing with strata, the legislation and some of the general law principles that have been in issue over the past few years for practitioners.

Major defects

2. The statutory scheme we currently deal with in New South Wales came into place in 1997. In 2002 the Insurance Scheme changed and they brought in a definition of structural defect. This changed again in 2012 when the insurance definition was widened to deal with statutory definitions generally, and then it was retrospectively rewritten in 2015. The statutory definition of structural defect was rewritten to become 'major defect'.

3. The case of *AAI Ltd T/as Vero Insurance v Kalnin Corp Pty Ltd; Kalnin Corp Pty Ltd v AAI Ltd T/as Vero Insurance* [2017] NSWSC 548 involved a recovery being under taken by Vero Insurance as a home warranty insurer.

4. Vero had paid out a significant amount of money on a strata development and were looking to get it back, and sued some indemnifiers. It is quite common with home warranty insurance that the principals and related parties involved in the project would provide a deed of indemnity. Vero Insurance was suing Kalnin under these deeds of indemnity to try and recover these damages and costs.

5. Justice Stevenson dealt with the definition of 'structural defect', which had never really been the subject of any judicial decision of any note. The definition had changed now to 'major defect', as stated above, but the definition is still similar. Stevenson J looked closely at the part of the definition that states 'any internal or external load bearing component of the building that is essential to the stability of the building or any part of it'.

6. When looking at what fell into that load bearing component requirement, his Honour read it very narrowly. He held that things like paint or render, unless they were an essential part of bearing a load and being a structural element, cannot be a structural defect.

7. The particular part of what is a structural element, now a major element, is there in almost the same form. The definition of major defect will be read very narrowly as the definition of structural defect was in this case, which changes significantly how insurance companies and stratas, builders, developers, etc. will deal with issues relating to this.

8. For all works under a building contract since the 1st of February 2012, or works started after that date are covered by the reduced warranty scheme, they have two years cover to sue for completion under s 3C of the *Home Building Act 1989* (NSW) for what is not a major defect. A major defect has 6 years from completion to sue. However it is important to note that there are some further provisions contained within the Act about where the defect becomes apparent within the last 6 months and so forth.

9. If the owners are coming up to the two year period, they are going to have to have regard to Stevenson J's decision as to what classification the defect may fall under to see if time is going to run out at the two year mark. Once beyond the two year mark, anything that is not a major defect is now out of time pursuant to the statutory warranties.

10. What is considered a major defect is as much of a technical question as it is as a legal question, when looking at what is a very artificial definition. From a consumer protection point of view, it can be argued that it would have been better if the definition was wider, but at least there is now clarity.

The Owners Strata Plan No 66375 v Suncorp Metway Insurance Ltd (No 2) [2017] NSWSC 739

11. Post 2002 there was still a long tail of insurance claims and cases against builders and developers under the old seven year general defect warranty scheme. From a building consultant and building industry point of view, there seemed to be a shorthand jargon of what is considered a structural defect.

12. The case of *The Owners Strata Plan No 66375 v Suncorp Metway Insurance Ltd (No 2)* [2017] NSWSC 739 raised questions about whether a person or persons were developers within the meaning of the *Home Building Act 1989* (NSW) (the Act). This gave rise to a consideration of what s 3A of the Act says in relation to a developer.

13. In this case a strata plan was suing for defects. There was a developer company that had been set up by the owners of the property of Mr. and Mrs. King, and the developer company had entered into a tender process with a construction company called Beach Constructions, which inevitably went into liquidation. In the background to this was the home warranty insurance scheme that was being operated by Suncorp Metway.

14. There was a question as to whether or not the owners of the property, Mr. and Mrs. King, who were also the directors of the development company, were the actual people that had work done of their behalf. There was an issue about which entity or persons had entered into the building contract – was it the individuals or was it the company?

15. There was a building contract in evidence. The contract was signed by the representatives of the building company, however the signed version of that building contract by the owners or developers was not in evidence.

16. It was held that the Court could not rely upon the site meetings as a business record for the purposes of the *Evidence Act 1995* (NSW). This was because there was no actual evidence before the Court that could establish that the persons who authored the site meeting minutes had actual or personal knowledge of the facts represented in the site meeting minutes. The site meeting minutes were prepared by the architects for the owners, and there was no evidence that they knew as a matter of fact, or had witnessed the owners signing the building contract.

17. This case is going to appeal and it will be interesting to see what issues are raised, as his Honour set out quite comprehensively in the judgement that he has dealt with all of the potential arguments and alternative arguments that have been raised.

18. It was questioned whether Meridian, the development company, was doing the work or signing the building contract as an undisclosed agent for Mr. and Mrs. King. His Honour determined that they were not, principally because there was a provision in the development agreement that there was a bar on assignment. That was considered an exception to the principle that a principal could be liable for the actions of an agent in the circumstances where they are an undisclosed principal.

19. The first issue that arose in this case was the extent to which the statutory warranties that were implied by s 18B under the Act were the same statutory warranties that would have been implied in the notional development contract under s 18C of the Act between the developer and the strata plan. His Honour determined they were the same statutory warranties.

20. In this case a lot of the defects were actually defects in relation to design, rather than defects in relation to the carrying out of the building work. Therefore a number of those defects were found to not be the responsibility of Mr. and Mrs. King, even on the assumption that they had been parties to the building contract.

21. Systemic defects are attempted to be used as a shorthand version of proving something is a defect in every respect in relation to a building, when there has only been proof of some of those things.

22. The Court found that 25 to 35 bathrooms were leaking, and that 39 of 54 ensuites were leaking. There had also been destructive testing of two of the bathrooms, and the expert identified that the membrane was insufficiently thick in those bathrooms.

23. His Honour rejected the expert evidence put forward regarding the destructive testing, holding that it was not possible to apply the findings from that testing to the entirety of the properties. However, his Honour found that all else being equal or all liability found, the builder would have been responsible for replacing all the membranes because they had put it in a different membrane than had been specified.

24. His Honour referred to the case of *The Owners Strata Plan 62930 v Kell & Rigby Holdings Pty Ltd* [2010] NSWSC 612 in which case it was held that if you are only going to do a sample, or not inspect every occurrence, then you have to be able to explain your modus operandi. This also applies to instances of destructive investigation, as the expert is going to have to be able explain why they believe that what they have found applies to all other instances and for what reasons.

25. This point is important to keep in mind when you have strata claims because if you have 100-150 units in a big block, it is a lot of time and effort to and inspect them all. There is also an issue about the extent to which the building owners, and the strata plans themselves will tolerate destructive testing of more than a handful of apartments.

26. The next issue that arose was the question of quantification, particularly allowances being made for provisional sums and contingencies. In this instance his Honour formed the view that they were appropriate, given that it was very likely that the building work would have to be contracts out to a builder. The lump sum cost in that building contract would likely include those sums and say it was appropriate in this case to make an award if he ultimately found that Mr. and Mrs. King were liable for this work.

<u>Fresh warranties</u>

27. The case of *Kondouris v The Owners – Units Plan No 1917* [2017] ACTCA 36 is a useful guide on an issue that we have not had much guidance on in NSW. The ACT Home Building scheme is a lot shorter and simpler in many ways than it is in NSW, but is still similar.

28. This case concerned whether the builder who had come back and done some repair works to this strata scheme had provided fresh warranties for the work, as to do the works properly but also for the purpose of the warranty periods to be sued upon.

29. In New South Wales, when the original work is completed, s 3C of the *Home Building Act 1989* (NSW) says that the warranty period begins when an interim or final occupation certificate is issued. The Court of Appeal of the ACT found in this case that when the builder comes back and does repair work, they have to do it properly and under the statutory warranties.

30. An important aspect of this is keeping track of what the builder did, and when, in order to know exactly when the warranty periods start and finish for each element of the building. One way of doing this is by agreement to have someone certify the work that the builder is doing, such as a building consultant.

Mcelwaine v The Owners – Strata Plan 75975 [2017] NSWCA 239

31. The case of *Mcelwaine v The Owners – Strata Plan 75975* [2017] NSWCA 239 concerned a property in Newcastle that had issues relating to waterproofing dating back to 2007/2008. Rain had been leaking into Mr. Mcelwaine's property, and in 2013 there was some heavy rainfall that resulted in the rendering of the apartment unfit for habitation.

32. This decision was based on the *Strata Schemes Management Act 1996* (NSW). Section 61(1) and 6(2) of this Act have now been replicated in the new *Strata Schemes Management Act 2015* (NSW) under s 106(1) and 106(2).

33. Reference was made in this case to the decision in *Thoo v The Owners Strata Plan No. 50276 (No 2)* [2012] NSWSC 1313 which determined that there was no statutory duty of care that arose by reasons of s 62, which followed the earlier decision of the Court of Appeal in *Ridis v Strata Plan 10308* [2005] NSWCA 246; (2005) 63 NSWLR 449.

34. In *Mcelwaine*, Young AJ was forced to consider as a separate determination whether or not the claim could be made in nuisance, as opposed to being a claim for breach of statutory duty.

35. At first instance and on appeal the Court dealt with whether there was anything in the legislation that effectively took away the claimants common law rights based on the provisions of the *Strata Management Scheme Act 1996* (NSW). Young AJ agreed with this position, relying partly on the provisions in relation to Chapter 5, and the decisions in *Ridis* and *Thoo*.

36. However on appeal it was held that the Act did not express any intention to derogate from the rights of claimants for breaches of general law duties of care. White J held that there should be no difference between the duties that an Owner's Corporation owes to third parties than it owes to its own lot owners in relation to general law duties of care and nuisance. White

J relied on the provisions in Chapter 5 which made it clear that the adjudication process gave no power to the adjudicator or the Tribunal to award damages for a breach under s 62.

37. Section 226 of the *Strata Schemes Management Act 1996* (NSW) made it clear that a claimant's other rights and remedies are retained. This leads to a question about whether the same set of facts would lead to a different result under the current legislation.

38. Unlike the previous Act, the 2015 Act gives rise to a right to damages for breach of a statutory duty under s 106(5). It is clear that s 106(5) gives a claimant a right to damages for breach of a statutory duty, but does not expressly say anything about denying a claimant a right to their general duties of care.

39. The provision that retained a claimant's rights and remedies was also replicated in the new Act. This tends to support the view that the decision of this case would be the same as under the current legislation.

40. The s 106(5) ability to sue in damages only lasts for two years from when they become aware of the loss. In *The Owners – Strata Plan No 30521 v Shum* [2018] NSWCATAP 15 the appeal panel of NCAT determined that s 106(5) is a remedy that NCAT can provide. This would lead to a possible situation where you would have a claim potentially being brought in two different places for two rights to the same damages claim.

Standing of Owner's Corporations

41. The case of *Owners Corporation SP 79417 v Trajcevski* [2017] NSWCATAP 101 looked at the issue of, amongst other things, whether the Owner's Corporation had standing to sue for defects in a common property.

42. Cases such as *Brookfield Multiplex Ltd v Owners Corporation Strata Plan 61288* [2014] HCA 36; (2014) 254 CLR 185 and *The Owners – Strata Plan 84741 v Nazero Constructions Pty Ltd* [2017] NSWSC 1241 had dealt with the issues of standing of Owners Corporations briefly, but not in any significant detail.

43. This issue was resolved quite quickly because the NSW Supreme Court had dealt with this same issue in *Manbead Pty Ltd v The Owners – Strata Plan No 87635* [2016] NSWCATAP 167. In *Manbead* it was held, at [26], that there is no real question about strata plans having standing.

44. In *The Owners of Strata Plan 43551 v Fair Trading Administration Corporation; Walter Construction Group Limited v Fair Trading Administration Corporation* [2004] NSWSC 158, it

was held that Owner's Corporations basically have the ability to sue for repair costs by way of damages for defects in a common property.

45. Ultimately the Owner's Corporation is the one that is going to have to strike levies, raise money and pay the repair costs. It is the body that was created to deal with various things, including repairing and maintaining the common property. In *Manbead* the Court said they are the body that can sue for damages by way of repair costs.

Breach of statutory duty

46. The case of *The Owners Strata Plan Number 57164 v Yau* [2017] NSWCA 176 concerned a commercial lot owner, Mr. and Mrs. Yau. They wanted to access a grease extraction system and an exhaust system that was existing within the strata plan but doing so would require an upgrade in terms of becoming operational. The strata plan was against that idea, and went so far as to make a special resolution under s 62(3) that those works were not required.

47. As a result of this, Mr. and Mrs. Yau commenced proceedings seeking damages for breach of statutory duty. During litigation the Executive Committee had various meetings about what they should do about the matter. There had also been some settlement negotiations between the parties.

48. Just prior to the court hearing there had been a settlement offer made that was endorsed by Senior Counsel from the Owner's Corporation. However, the hearing still commenced and during the course of the first two days of hearing, Senior Counsel formed the view that the Owner's Corporation was almost certainly going to lose its case.

49. On the evening of the second day of the hearing an emergency meeting of the Owner's Committee was held and they resolved to give Senior Counsel instructions to settle the case. Senior Counsel for the Owner's Corporation and for the Respondents drafted a form of short minutes of order which revoked the resolutions it had previously made pursuant to s 62(3), agreed to undertake the relevant works that were required for upgrading the exhaust and grease extraction system, and also pay the Respondent's something in the vicinity of $200,000.

50. Following the entry of the consent orders and the judgement of the Court, the decision of *Thoo* was handed down. The Executive Committee then raised the question of whether it could and should pursue the setting aside of those consent orders. At the same time, they were required by the consent orders to make payment to the lot owners and start commencing work.

51. The first issue dealt with by the Supreme Court was whether the consent orders should be set aside. The Court formed the view that they could be set aside if the underlying agreement was void or voidable. This issue of voidability turned on whether the instructions to Senior Counsel gave the Senior Counsel ostensible authority to settle the proceedings.

52. The Court of Appeal then dealt with the issue of whether or not the failure of the Executive Committee to have 72 hours' notice of a meeting would invalidate the resolution that permitted Senior Counsel to negotiate and settle. The Court of Appeal formed the view that it did not invalidate this.

53. The Court of Appeal also dealt with whether there had been a contravention of two different provisions of the *Strata Scheme Management Act 1996* (NSW). Section 65A of the 1996 Act gave the Owner's Corporation power to amend the common property. Section 80A of the 1996 Act required the Owner's Corporation, not the committee, to make determinations about expenditure of fuds in relation to common property.

54. However, the Court of Appeal took a fairly narrow view of the facts in this case and determined that the only resolution that had been struck by the executive committee was limited to instructing counsel to settle, which did not involve any determination of expenditure of funds.

55. The last issue dealt with by the Court of Appeal was whether the Owner's Corporation had ratified the previous decision of the executive committee. The Court found that the Executive General Meeting in which the Owner's Corporation had made the resolution in relation to raising the special levy to deal with the damages claim and the works, was a ratification of the previous resolution.

BIOGRAPHY

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Paul holds a Bachelor of Arts and a Bachelor of Laws from Macquarie University, and was admitted as a solicitor in New South Wales in 1999. He practises primarily in insurance, construction and strata law, specialising in home warranty insurance, contract works insurance, residential construction disputes and defects claims, as well as strata advice and disputes.

Carlos Mobellan

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Carlos is a barrister who specialises in building cases with an emphasis on matters arising under the *Home Building Act 1989* (NSW), the *Building and Construction Industry Security of Payment Act 1999* (NSW) and the *Strata Schemes Management Act 2015* (NSW), Carlos was admitted as a solicitor in 1997 and was called to the Bar in 2004 where he was awarded the Bar Practice Course prize. Carlos has appeared for and against home owners, Owners Corporations, builders, government agencies and property development companies.

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Legislation

Home Building Act 1989 (NSW), s 3C, s 3A, s 18B, s 18C

Strata Schemes Management Act 2015 (NSW), s 106(5)

Strata Schemes Management Act 1996 (NSW), s 62(1), s 62(2), s 226, s 65A, s 80A