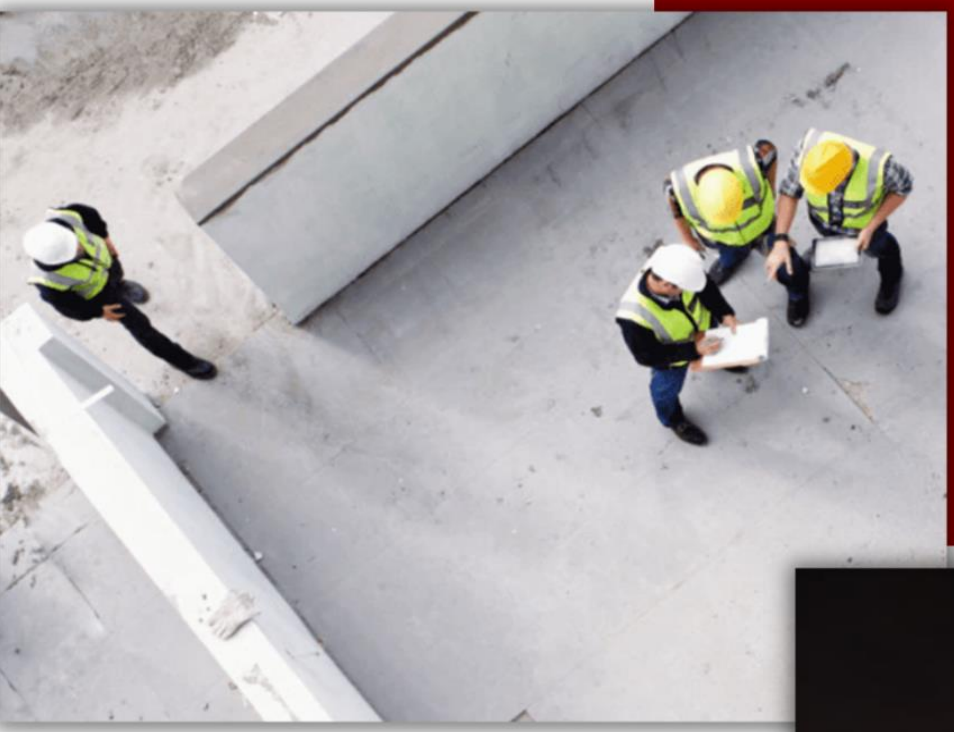
A Critique of the

Residential Apartment Building (Compliance and Enforcement Powers) Act 2020 (NSW)

& *Home Building Act 1989* (NSW)



Newsletter

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CRISP LAW

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In this Newsletter, we explore the concept of a "serious defect" and "major defect" as the expressions are in the Residential Apartment Buildings (Compliance and Enforcement Powers) Act 2020 (RAB) and the Home Building Act 1989 (HB) respectively. We explore the likely response to an Owners Corporation commencing proceedings despite the presence of an Undertaking Deed.

Whilst longer than our usual Newsletters, the detail is justified as the RAB Act is evolutionary. It dramatically changes for all stakeholders, the requirements for construction, given the much improved quality and durability of apartment buildings which can be compelled by the RAB Act.

An Undertaking Deed pursuant to s28 of the RAB Act (between the Developer and Secretary of the Building Commissioners Office) is the Building Commissioners preferred means of resolving prohibition, stop work and building work rectification orders which have issued. The workings of such an Undertaking Deed are detailed in the Schedule 1 to this Newsletter. In summary the Undertaking Deed requires the rectification of so called immediate and interim defects funded by the Developer ("backed" by security), co-ordinated and managed by an Undertakings manager. The beauty of an Undertaking is all rectification work requires design compliance and building practitioner certificates, so Owners can be assured by the rectification works completed.
s28 to the RAB Act is set out in Schedule 2 to this Newsletter.

*By way of background to this Newsletter and the issues posed, there is no provision under the Residential Apartment Building (Compliance and Enforcement Powers) Act 2020 (NSW) to prevent an Owners Corporation (**OC**) from commencing a claim under s18B of the Home Building Act 1989 (NSW) against a developer concerning defects the subject to an "Undertaking", per s28 of the RAB Act. However, it is likely that NCAT or NSW Court would order any proceeding commenced by an OC for the defects the subject of a s28 Undertaking to be dismissed or struck out and a cost order made against an OC as we will explain below.*

What remains a "puzzle" is what might happen when an OC forgoes an Undertaking Deed "hell-bent" on prosecuting claims under the HB Act. We explore this issue at the end of the Newsletter.

1. "Serious defect" under RAB Act

The Second Reading Speech[1] states that Part 1, Clause 3 of the RAB Bill defines a serious defect as "a defect in a building element that is attributable to a failure to comply with the performance requirements of the Building Code of Australia, the relevant Australian Standards or the relevant approved plans".[2]

The definitions of "serious defect" under s3 are at Schedule 2 to the Newsletter.

1.1 Major defect under HB Act

The definitions of "major defect" and "major element" under s18E(4) of the HB Act are at Schedule 3 to the Newsletter.

Vella v Mir [2019]

The Appeal Panel stated a "major defect" is a conclusion of law and an expert's opinion cannot be decisive.[3] The Appeal Panel concluded that Expert evidence is clearly relevant to whether a claimed defect is in a major element of a building and whether it meets the definition of a major defect in s18E(4). However, it is not determinative of the issue.[4]

Ashton v Stevenson [2019]

The first step in the analysis is that the defect must be part of a "major element" of a building. The definition of "major element" includes "waterproofing". This does not, however, mean that any, or all, defects involving an imperfection in the system of waterproofing of a building is a "major defect".[5] The extent to which a defect in the waterproofing system of a residence impacts on habitability or the integrity of the building needs to be proved by the proponent of a "major defect".

The consequences of the defect must be shown to have, or to probably have, a proven consequence for the habitation, or use, of the building, or to the integrity of the building. This is a matter for evidence which must be adduced to prove all the elements required to establish a "major defect".[6] The proponent of a "major defect" should be required to prove that the defect will have the prescribed consequence, or that it probably

[1] The Hon. Damien Tudehope (Minister for Finance and Small Business), Second Reading Speech, Thursday, 4 June 2020, page 2376.
[2] Ibid.
[3] Vella v Mir [2019] NSWCATAP 28, 30.
[4] Ibid 49.
[5] *Ashton v Stevenson* [2019] NSWCATAP 67, 69.
[6] Ibid 71.

will have the prescribed consequence.[7] There needs to be evidence that the consequences are imminent or probable, and that expert evidence may assist in that analysis, but is not conclusive.[8]

Does it matter if it is a "serious defect" or a "major defect"?

In reality, there is not much difference between the definitions of "serious defect" and "major defect". The substantial difference is that an Undertaking avoids the successful proof of evidence that NCAT or the Courts compel. Once an Undertaking Deed has been entered, the defects to be rectified and the standard to be achieved from the rectification work is crystal clear. All fully backed by substantial security for the Developer's performance. Compare this to an Owners Corporation before NCAT or the Supreme Court who has the costs of experts and lawyers and the lengthy delays in expert conclaves and hearings. The success of this "alternative" depends on the quality and success of the Expert Reports.

Given the above reality, if there is an enforceable Undertaking under s28 of RAB Act can the OC then bring a proceeding in relation to a "major defect", in NCAT or the Supreme Court against the Developer? Given that the rectification works pursuant to the Undertaking Deed will be completed and comply with the BCA, and so certified all at no cost to the "Owners Corporation", it is unlikely an Owners Corporation could justify maintaining Proceedings in NCAT or the Court, for the reasons which will be discussed below.

2.2 Power to Make Cost Orders

The powers of both NCAT and the Supreme Court to strike out a proceeding is set out in Schedule 4. The case of *Unilodge Australia (No 2)* [2020][9] explores some of the "special circumstances" outlined in section 60(3) of the Act where a Tribunal may order a person to pay the other party's costs. Accordingly, it assessed on OC's unreasonable prolonging of the proceedings to justify such a cost order.

There is a NSW Court of Appeal decision that might provide guidance as to how the Supreme Court might proceed and allow a costs order against an Owners Corporation who commences proceedings in the circumstances as we have described them.[10] In summary an adverse costs order was made against a (successful) applicant in the Supreme Court proceedings as the claim in the proceedings could have been prosecuted before NCAT relying upon the Strata Schemes Management Act which made "adequate provision" for

[7] Ibid 74.
[8] Ibid 75.
[9] *Unilodge Australia Pty Ltd v The Owners Corporation Strata Plan 54026 (No 2)* [2020] NSWCATAP 80. (*'UniLodge'*)
[10] *EB 9 & 10 Pty Ltd v The Owners Strata Plan 934* [2018] NSWCA 288.

enforcement of the applicant's rights as the Supreme Court proceedings were not justified, costs should not be awarded. The Court of Appeal stating: "… a finding of "adequate provision" will be available even if it the means …are, by comparison, less secure or less effective.[11]

What are the conclusions to be made?

We expect a Developer would successfully argue for the dismissal of the proceedings and an adverse cost orders against the OC. Arguing that the OC could have availed themselves of an Undertaking Deed at no cost and in any event any "expert" evidence the Owners Corporation intend to rely upon will be challenged given the Developers earlier actions to resolve the Building Commissioners punitive orders which would allow the opportunity for apartments to be completely sold. (Understandably that pathway would have been followed as if it failed to do so the Developer faces its own proceedings in the Land and Environment Court).

You are now asking rhetorically where does that leave individual Owners with their own complaints? We will discuss these issues in our Newsletter in early 2023.

[11] Ibid 43-44.

Schedule to the Residential Apartment Building (Compliance and Enforcement Powers) Act 2020 (NSW)

Schedule 1: Undertaking Deed

As was said in the Newsletter an Undertaking Deed pursuant to s28 of the RAB Act (between the Developer and Secretary of the Building Commissioners Office) is the Building Commissioners preferred means of resolving prohibition, stop work and building work rectification orders which may have issued. The Undertaking Deed is between the Developer and Secretary of the Building Commissioners Office. It usually identifies two classes of defects immediate and identified. The Undertakings manager, an appointee of the Building Commissioners Office, is a well regarded Industry Expert, who manages the performance of the Undertaking Deed. (There is usually a Superintendent to controls the identification and performance of the rectification works). The Undertaking Deed only takes effect of its agreement by the Owners Corporation signified by its agreement in a separate Deed Poll. The Owners Corporation is then bound by the Undertaking Deed including the dispute resolution provisions of the Undertaking Deed. (Which escalate from direct discussion, mediation and then determination by the Undertaking Manager).

The costs of the defects rectification work including the costs of any experts retained and builders and of the Building Commissioners Office is to the Developers account. This is backed by very substantial security equivalent to the estimated and "total" costs of the assessment, carrying out and certification of the defects rectification works. So there are no costs incurred by the Owners Corporation. Worthy of comment and mention is that all rectification works will need to comply with all legislations including the *Design and Building Practitioners Act 2020*, in particular, for any "Design Works".

Any disputes are dealt with under a mandatory dispute resolution regime detailed in the Undertaking Deed. Which escalate from direct discussion, mediation and then determination by the Undertaking Manager.

Schedule 2: Excerpt from Residential Apartment Buildings (Compliance and Enforcement Powers) Act 2020 (NSW)

s3 - serious defect

s3 serious defect in relation to building means:

(a) a defect in a building element that is attributable to a failure to comply with the performance requirements of the Building Code of Australia, the relevant Australian Standards or the relevant approved plans, or

(b) a defect in a building product or building element that—

(i) is attributable to defective design, defective or faulty workmanship or defective materials, and

(ii) causes or is likely to cause—

(A) the inability to inhabit or use the building (or part of the building) for its intended purpose, or

(B) the destruction of the building or any part of the building, or

(C) a threat of collapse of the building or any part of the building, or

(c) a defect of a kind that is prescribed by the regulations as a serious defect, or

(d) the use of a building product (within the meaning of the Building Products (Safety) Act 2017) in contravention of that Act.

s28 - Undertakings

(1) The Secretary may accept a written Undertaking from a developer regarding the carrying out of building work.

(2) Without limiting subsection (1), the Secretary may accept a written Undertaking given by the developer that the developer will do one or more of the following—

(a) refrain from conduct that constitutes a contravention of this Act or the regulations,

(b) take action to prevent or remedy a contravention of this Act or the regulations,

(c) provide the Secretary with a rectification bond that may be claimed or realised by the Secretary to meet the costs of eliminating, minimising or remediating a serious defect or a potential serious defect in a residential apartment building.

(2A) If an Undertaking requires a developer to provide a rectification bond, the Undertaking must include—

(a) the circumstances in which the rectification bond may be claimed or realised, and

(b) the procedure for claiming or realising the rectification bond.

(3) A developer who contravenes an Undertaking accepted by the Secretary commits an offence.

Maximum penalty—1,500 penalty units (in the case of a body corporate) or 500 penalty units (in any other case).

(4) In this section—***rectification bond*** means a bank guarantee, bond or other form of security acceptable to the Secretary.

Schedule 3: Excerpt from Home Building Act 1989 (NSW)

s18B Warranties as to residential building work

s18B - Warranties

(1) The following warranties by the holder of a contractor licence, or a person required to hold a contractor licence before entering into a contract, are implied in every contract to do residential building work--

(a) a warranty that the work will be done with due care and skill and in accordance with the plans and specifications set out in the contract,

(b) a warranty that all materials supplied by the holder or person will be good and suitable for the purpose for which they are used and that, unless otherwise stated in the contract, those materials will be new,

(c) a warranty that the work will be done in accordance with, and will comply with, this or any other law,

(d) a warranty that the work will be done with due diligence and within the time stipulated in the contract, or if no time is stipulated, within a reasonable time,

(e) a warranty that, if the work consists of the construction of a dwelling, the making of alterations or additions to a dwelling or the repairing, renovation, decoration or protective treatment of a dwelling, the work will result, to the extent of the work conducted, in a dwelling that is reasonably fit for occupation as a dwelling,

(f) a warranty that the work and any materials used in doing the work will be reasonably fit for the specified purpose or result, if the person for whom the work is done expressly makes known to the holder of the contractor licence or person required to hold a contractor licence, or another person with express or apparent authority to enter into or vary contractual arrangements on behalf of the holder or person, the particular purpose for which the work is required or the result that the owner desires the work to achieve, so as to show that the owner relies on the holder's or person's skill and judgment.

(2) The statutory warranties implied by this section are not limited to a contract to do residential building work for an owner of land and are also implied in a contract under which a person (the
"principal contractor") who has contracted to do residential building work contracts with another person (a "subcontractor" to the principal contractor) for the subcontractor to do the work (or any part of the work) for the principal contractor.

s18E

major defect means—

(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, or
(c) the use of a building product (within the meaning of the Building Products (Safety) Act 2017) in contravention of that Act.
Note—The definition of **major defect** also applies for the purposes of section 103B (Period of cover).

major element of a building means—
(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.

Schedule 4: Excerpt from Civil and Administrative Tribunal Act 2013 (NSW) and Uniform Civil Procedure Rules 2005 (NSW)

NCAT Power to Strike Out a Claim

The Tribunal has the power to strike out a claim under ss 36 and 55 of the *Civil and Administrative Tribunal Act 2013* (NSW):

s36 Guiding principle to be applied to practice and procedure
(1) The guiding principle for this Act and the procedural rules, in their application to proceedings in the Tribunal, is to facilitate the just, quick and cheap resolution of the real issues in the proceedings.

s55 Dismissal of proceedings
(1) The Tribunal may dismiss at any stage any proceedings before it…
(b) if the Tribunal considers that the proceedings are frivolous or vexatious or otherwise misconceived or lacking in substance.

NSW Courts Power to Strike Out a Claim

General nature of the power of NSW courts to strike out pleadings comes from the following laws:

UCPR - r14.28 Circumstances in which court may strike out pleadings:
(1) The court may at any stage of the proceedings order that the whole or any part of a pleading be struck out if the pleading-
(a) discloses no reasonable cause of action or defence or other case appropriate to the nature of the pleading, or
(b) has a tendency to cause prejudice, embarrassment or delay in the proceedings, or
(c) is otherwise an abuse of the process of the court.
(2) The court may receive evidence on the hearing of an application for an order under subrule (1).

The test for whether a proceeding is vexatious is set out by Roden J in *Attorney General v Wentworth* at 491, included the third limb as follows: [12]

"3. They are also properly to be regarded as vexatious if, irrespective of the motive of the litigant, they are so obviously untenable or manifestly groundless as to be utterly hopeless."

[12] Roden J in *Attorney General v Wentworth* (1988) 14 NSWLR 481 at 491.