SEMINAR PAPER

RECENT DEVELOPMENTS IN CONSTRUCTION LAW

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Introduction

1. New Zealand's economic expansion in the latest quarter was helped by a 12.5 per cent rise in construction, which accounted for two-thirds of GDP growth and marked its largest increase in 14 years[1]. And that growth is not just coming from Christchurch. In value terms, residential building activity was up 31 percent in Canterbury and 12 percent in New Zealand excluding Canterbury. Non-residential building activity was up 15.8 percent in Canterbury and 19 percent in New Zealand excluding Canterbury[2].

2. Auckland's downtown skyline is peppered with cranes again, and there are some massive residential projects – eg Long Bay and Hobsonville.

3. The construction industry is also, in my view, one of the most dispute-prone. Leaky homes and Construction Contracts Act 2002 ("CCA") claims are constantly in the Courts. And, probably more than any other sector, construction disputes also have a high level of "under the radar" conflict, though the CCA adjudication process, contract engineers' decisions, and arbitrations.

4. Why? Large amounts are often at stake – for individuals and companies, a major construction project may well be their highest value undertaking. Construction projects are technically complex, a great deal can go wrong, and it can be very difficult to know why (no two experts in a leaky home claim will ever agree entirely). The applicable law is also difficult to be across. There are multiple relevant statutes, shifting case law, and even "standard form" contracts can be very hard to follow.

5. Many property and commercial lawyers are called on to give advice on construction disputes. Construction disputes also impact on, and are affected by, property transactions, particularly via warranties. The stakes can be very high.

6. This seminar outlines some recent developments in construction law, including:

   (a) The new consumer protection measures to be introduced to the Building Act 2004 by the Building Amendment Act 2013;

   (b) Recent cases on agreement for sale and purchase warranties;

   (c) The amendments to the CCA to be introduced by the Construction Contracts Amendment Bill 2013; and

   (d) Other recent major cases.

The new consumer protection measures to be introduced by the Building Amendment Act 2013

7. The Building Act 2004 already contains various consumer protection provisions. Most significant is the warranty regime at ss396-399. This regime applies to all building work on household units, and to also to the sale of household units by developers[3].

8. Section 397 of the Building Act 2004 states:

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[1] Statistics New Zealand 19 June 2014
[2] Ibid
[3] Building Act 2004, s396

> ***"397 Implied warranties for building work in relation to household units***
>
> *.....the following warranties about building work to be carried out under the contract are implied and are taken to form part of the contract:*
>
> *(a) that the building work will be carried out—*
>
> *(i) in a proper and competent manner; and*
>
> *(ii) in accordance with the plans and specifications set out in the contract; and*
>
> *(iii) in accordance with the relevant building consent:*
>
> *(b) that all materials to be supplied for use in the building work—*
>
> *(i) will be suitable for the purpose for which they will be used; and*
>
> *(ii) unless otherwise stated in the contract, will be new:*
>
> *(c) that the building work will be carried out in accordance with, and will comply with, all laws and legal requirements, including, without limitation, this Act and the regulations:*
>
> *(d) that the building work will—*
>
> *(i) be carried out with reasonable care and skill; and*
>
> *(ii) be completed by the date (or within the period) specified in the contract or, if no date or period is so specified, within a reasonable time:*
>
> *(e) that the household unit, if it is to be occupied on completion of building work, will be suitable for occupation on completion of that building work"*

9. Via s398 of the Building Act 2004, the above warranties can be enforced by subsequent owners of the building, ie the warranties are automatically transferred. So, if you buy a house, you can, via this provision, sue the builder, even if the builder was employed by a previous owner.

10. The warranties are implied into subcontracts as well.

11. The warranties cannot be contracted out of, unless the breach was known, or ought reasonably to have been known, by the person to exist at the time the agreement or instrument was executed[4]. As an aside, it might be possible for a developer seller to work around this, by requiring the buyer to warrant that s/he has undertaken such investigations as would enable them to ascertain any issues. But no doubt that would scare many buyers.

12. The Building Amendment Act 2013 retains the above warranties, but shifts them within the original Act. The Building Amendment Act 2013 also aims to further improve this consumer protection regime, with four key new provisions to be inserted into the original Act. These provisions are not yet in force, but are expected to come into force later this year[5]. They are as follows.

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[4] Building Act 2004, s399

[5] MBIE factsheet on the Building Amendment Act 2014, June 2014 update

Written contracts, with prescribed content, for building work over a certain value

13. Under new ss362F and 362G, there will be new minimum requirements for residential building contracts over a certain value. That value has yet to be set, but may be as low as $20,000. The requirements are that such contracts must:

    (a) Be in writing and dated;

    (b) Comply with new regulations as to content which will be issued. Those regulations may require that the contract specify:

        (i) A dispute resolution process;

        (ii) How the contract can be varied;

        (iii) The timeframe for performance; and

        (iv) The payment process.

14. The regulations may also imply such clauses into contracts that should have them. And such implied clauses will not be able to be contracted out of.

15. A building contractor can be fined up to $2000 for not complying with these requirements.

Building contractors will be required to provide disclosure information and a checklist before a contract is entered into

16. Under new ss362D and 362E, for residential building contracts over a certain value (again, yet to be set, but assume it will be low), or if the client asks for it, the building contractor must provide prescribed *disclosure information*, and a prescribed *checklist*.

17. The disclosure information has yet to be prescribed, but will likely include:

    (a) The legal status of the building contractor (eg whether they are a company, individual, partnership etc);

    (b) The "dispute history" of the building contractor. It will be interesting to see whether this term is further defined in the regulations, because it is new, otherwise undefined, and plainly open to wide interpretation. Dispute history is very much in the eye of the beholder – just ask your spouse for their version of your last argument. Moreover, CCA adjudications, and arbitral awards are confidential by statute[6], and many negotiated/mediated settlements have contractual confidentiality requirements;

    (c) The skills, qualifications and licensing status of the building practitioners who will be doing the work; and

    (d) If the building contractor is a company, the role of each director, and the business history of each director. Again, it seems to me that the terms "role" and "business history" could be open to wide interpretation. Perhaps here though will be an opportunity for directors of sole operator

[6] Arbitration Act ss14-14I, CCA, s68

and small companies to insulate themselves from the "veil piercing" personal exposure that so many now face in leaky homes disputes. They may be able to do so by making it clear in the disclosure information that they are working on behalf of the company, and not in a personal capacity.

18. The checklist has also yet to be prescribed, but will likely include:

    (a) An explanation of the parties' legal obligations in relation to the building work;

    (b) An outline of the risks associated with payment in advance of completion;

    (c) A summary of dispute resolution options (some cross-over here with s362G regarding what might be required to be in the contract too); and

    (d) A list of sources of further information.

19. Failure to provide the disclosure information and checklist when required to do so can attract a fine of up to $2000.

20. Making a false statement in the disclosure information can attract a fine of up to $20,000.

There are specified remedies for breaches of the implied warranties

21. New specified remedies for breaches of the implied warranties are set out in ss362L-362P. Just like the warranties, these remedies are available to subsequent owners, as well as the party who contracted with the builder.

22. Under s362M, if the breach of warranty can be remedied, the client can require the building contractor to remedy the breach. If the building contractor will not remedy the breach, or fails to do so within a reasonable time, the client can have someone else do it and claim the costs back from the building contractor, or cancel the contract. The client can also sue for damages.

23. Under s362N, if the breach of warranty cannot be remedied or is a "*substantial breach*", the client can cancel and/or claim damages.

24. The meaning of "*substantial breach*" of warranty is set out in s362O. It is broad, and includes work that "*cannot be expected to produce the desired result stated in the building contract*". So, if you are acting for a client, it would be useful to have some statements as to the desired result in the building contract, eg: "*the building is to be constructed to a high standard, using high quality materials, and is to be weatherproof, durable and well-finished throughout*". Certain cases may well allow for even greater specificity, eg: "*the rustic theme is to be continued throughout, save for the bathrooms, where a sense of Tuscan chic must prevail*".

25. Section 362P even allows for the client's cancellation to be oral, unless the contract specifies that written notice is required (which any good contract should, for the protection of both parties).

There will be a new 12 month defect remedy period

26. Section 362Q will require that a building contractor must remedy a defect if given notice to do so within 12 months of completion of the building. The remedy has to be effected within a reasonable time.

27. The most extraordinary aspect of this provision is the approach to the burden of proof. Under s362Q, it is presumed unless the contrary is *proven* that, inter alia:

    (a) The building work is defective; and

    (b) The defect is able to be remedied.

    This could place a heavy burden on building contractors dealing with unreasonable clients.

28. The building contractor can also be liable to remedy defects in the work of others within his/her control, including subcontractors (s362R).

Recent cases on agreement for sale and purchase warranties

29. In theory, a house sale is a classic case of *caveat emptor*[7]. But most standard form agreements for sale and purchase contain warranties that abrogate that principle.

30. Such warranties have come under the spotlight in leaky homes litigation over the last few years. This has happened as claimants have sought to spread the net as wide as possible in their search for solvent respondents. Because the WHT is essentially a no costs regime, there is a real incentive to get as many solvent respondents as possible. Once an individual or entity is a respondent to a WHT claim, they are incentivised to pay to settle, irrespective of the merits of the case against them.

31. Most significant here are the warranties about work done while the vendor owned the home. The seventh edition of the ADLS standard agreement for sale and purchase provided as follows:

> *6.2. The vendor warrants and undertakes that at the giving and taking of possession:*
>
> *....*
>
> *(5) Where the vendor has done or caused or permitted to be done on the property any works for which a permit or building consent was required by law:*
>
> *(a) The required permit or consent was obtained; and*
>
> *(b) The works were completed in compliance with that permit or consent; and*
>
> *(c) Where appropriate, a code compliance certificate was issued for those works; and*

[7] *Ford v Ryan* (2007) 8 NZCPR 945 (HC) at 16-17

> *(d) All obligations imposed under the Building Act 1991 were fully complied with."*

32. The eighth and ninth editions contain similar wording, save that subclause (d) has been deleted. In the ninth edition, subclause (b) has also been modified such that the warranty is only that "*to the vendor's knowledge*" the "*works were completed in compliance…*".

33. These warranties have been looked at closely by the Courts. The key battleground has been over whether they amount to a warranty that the house complies with the Building Code. This is important because, typically, a leaky home, by definition, will not comply with the Building Code requirement as to weathertightness.

34. Claimants have tended to argue that:

    (a) The warranty that works were completed in compliance with any permit or consent imports an obligation to comply with the Building Code. This is because such permits and consents will almost always stipulate that works done under them must comply with the Building Code; and

    (b) The warranty that all obligations under the Building Act were complied with also imports compliance with the Building Code, because the Act requires compliance with the code[8].

35. These arguments seem to me to have a real literal coherence. They have been accepted in some cases. An example was the 2012 High Court decision in *Van Huijsduijnen v Woodley*[9], where Ronald Young J stated "*the vendor warrants compliance with the* [Building] *Act and, therefore, the Code*"[10].

36. But, in large part, the Courts have preferred to undertake some apparent logical yoga to get past these arguments, and come to pro-vendor decisions.

37. As a starting point, the Courts have stated that such warranties are not as to the quality of a home, or that it is watertight – see the 2013 High Court decision in *Newton v Stewart*[11].

38. The 2013 WHT and High Court decisions in *Saffiotti v Ward* further illustrates the pro-vendor approach. The defendants, the Wards, had the subject house built for them using an architect and builders. They obtained a CCC. They then sold it to the Saffiotis. The agreement contained the above seventh edition ADLS warranty. The Saffiotis subsequently discovered that the house leaked, and sued the Wards (amongst others) in the WHT for breach of the warranty.

39. The WHT[12], found that the house leaked, and that it had multiple defects which had caused those leaks. However, it also found that the Wards were not in breach of the warranty they had given. Key passages included the following:

> *[55] …….We do not consider that there are sufficient grounds on which to assume that when Mr and Mrs Ward and Mr and Mrs*

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[8] Building Act 2004, s17, Building Act 1991, s7
[9] *Van Huijsduijnen v Woodley* [2012] NZHC 2685
[10] Ibid, at para 33
[11] *Newton v Stewart* [2013] NZHC 970, at 98
[12] *Saffiotti v Ward* [2013] NZWHT Auckland 17

> *Saffioti signed the sale and purchase agreement in September 2004 they intended that the scope of the warranty in sub-clause (b) should extend to compliance with the Building Code.*
>
> ....
>
> *[56] Although sub-clause (d) refers to obligations under the Building Act, Mr and Mrs Saffioti say that the warranty extends to the Building Code. They rely on s 7 of the Building Act 1991, which says that all building work must comply with the Building Code to the extent required by the Building Act.*
>
> ...
>
> *[64] .....We consider that there was no intention for the warranty in sub-clause (d) to include compliance with the Building Code beyond the compliance necessary to obtain the consents referred to in the preceding sub clauses. At the time of settlement there had been no failure by Mr and Mrs Ward that would have prevented the CCC from being issued and the CCC demonstrated that the Building Code had been complied with.*

40. The High Court[13] agreed with the WHT's decision on the warranty, and, if anything, read down the effect of such warranties yet further. Pertinent passages included the following:

> *[43] I conclude that subcl (d) does not either expressly or by implication provide a warranty by the Wards of compliance with the Building Code.*
>
> ...
>
> *[51] I consider that as a matter of contractual interpretation, the warranty at subcl (b) did not impose a warranty that the Building Code had been complied with.*
>
> ...
>
> *[55] I conclude that the works had to be completed in compliance with the plans and specifications attached to the consent, and the relevant conditions and endorsements expressly recorded by the Council or certifier on that consent. But subcl (b) is not thereby converted into a warranty by the vendor that the works also comply with the provisions of the Building Code."*

41. So, for now at least, the Court environment is pro-vendor in relation to such warranties. If you are acting for a buyer of a house that may have issues, consider the inclusion of some more specific/express warranties as to weathertightness, and compliance with the Building Code.

The amendments to the CCA to be introduced by the Construction Contracts Amendment Bill 2013

42. The CCA largely came in to force on 1 April 2003. It was enacted in response to construction firm collapses which left many subcontractors broke. Its stated purpose[14] is:

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[13] *Saffiotti v Ward* [2013] NZHC 2831
[14] CCA, s3

(a) To facilitate regular and timely payments between the parties to construction contracts;

(b) To provide for the speedy resolution of disputes arising under construction contracts; and

(c) To provide remedies for the recovery of payments under construction contracts.

It also bans "pay when paid" provisions[15].

43. The most notable, and the most litigated, features of the CCA have been:

(a) The payment claims regime. Once a payment claim is properly made by a contractor under the CCA, it must be responded to, typically within 20 working days, with a payment schedule. The payment schedule has to be in writing, it has to identify the payment claim to which it relates, and, if it is intended that less than the claimed amount is to be paid, the payment schedule has to set out why, and how that is calculated[16]. A failure to respond within time with a correctly constituted payment schedule turns the payment claim into a due debt. The Courts have enforced these provisions quite rigorously, and typically in favour of contractors, eg *Metalcraft Industries Ltd v Christie*[17]. An issue which has surprised me is the number of engineers to contracts (ie those fulfilling that formal and sometimes independent role) who do not fully understand, or adhere to, this regime – at real risk;

(b) The provision for quick-fire decisions on construction disputes with tight, drop-dead, timeframes, by specially appointed adjudicators[18]; and

(c) The no set-offs or counterclaims rule in relation to due debt enforcement action. If a party (typically a contractor) has a due debt payable under the CCA (via an unmet payment claim, or an adjudicator's decision), they can enforce that through the Court (including by statutory demand and liquidation), without heed for any set-off or counterclaim[19]. This rule has been the subject of many cases, eg *Halls Earthworks Ltd (in liq) v Donovan Drainage and Earthmoving Ltd*[20], and in the Supreme Court in *Laywood v Holmes Construction Ltd*[21]. These cases have fallen heavily in favour of claimants – upending a long tradition in the construction industry of "muddying waters" with set-offs and counterclaims.

44. The Construction Contracts Amendment Bill 2013 ("Bill") is intended to amend the CCA in key respects. The Bill is currently awaiting a third reading. It is scheduled to come into force, in large part, on 1 November 2014.

45. Three aspects of the Bill are particularly significant.

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[15] CCA, s13
[16] CCA, s21
[17] *Metalcraft Industries Ltd v Christie* HC Whangarei, CIV 2006-488-645, 15/02/07, Harrison J – "*An assertion that remedial work is required at a cost which would exceed the payment claim could never constitute a valid reason...for withholding payment*"
[18] CCA, ss25-71
[19] CCA, s79
[20] *Halls Earthworks Ltd (in liq) v Donovan Drainage and Earthmoving Ltd* HC Whangarei, CIV 2007-488-144, 18/07/07, Faire AJ
[21] *Laywood v Holmes Construction Ltd* [2009] NZSC 44 (15 May 2009)

Distinction between residential and commercial construction contracts largely removed

46. Firstly, the current distinction in the CCA between residential and commercial construction contracts is to be removed (save for a somewhat anomalous provision regarding charging orders). This will make the CCA more contractor-friendly for residential construction. It is currently slightly kinder to residential owners than it is to commercial owners – with possibly more flex on default provisions, and no statutory entitlement for contractors to suspend work[22].

47. But there is a fish-hook for contractors here. It relates to the information that has to be provided with payment claims. Under the CCA at the moment, extra information (as to the process, and consequences of non-compliance) must be provided with payment claims made to residential owners[23]. The Bill will amend the CCA such that this extra information will have to be provided to all owners[24]. Failure to do so can invalidate a payment claim – so prime any contractor clients in this regard.

CCA will be expanded to apply to consultants

48. Secondly, the CCA will be expanded to apply to professional consultants. This will be achieved by changing the definition of "Construction work" in section 6 of the CCA to include design, engineering, and quantity surveying work[25].

49. This amendment takes the CCA into new territory. The CCA payment, disputes and enforcement regime will be a new way of doing business for professional consultants. They will have to look at amending the way they charge – ensuring that their bills are valid payment claims, so as to get the benefit of the CCA. It will also be interesting to see whether there is conflict between the CCA adjudication/enforcement regimes and professional disciplinary processes eg under the Chartered Professional Engineers of New Zealand Act 2002. Will the existence of an extant formal complaint against an engineer be a basis for a client to avoid payment?

Changes to the adjudication process

50. Thirdly, the Bill makes changes to the adjudication process. These are largely technical, but one is of particular significance. It relates to the timing of the Adjudication Response. The Adjudication Response is the document by which the respondent sets out its position on the claim. The CCA mandates that respondents typically have only five working days to provide their Adjudication Response.

51. The Bill will add a *requirement* that adjudicators allow respondents (typically the owner/client) additional time for their Adjudication Response if it is necessary given the size, complexity or timing of the claim[26].

52. This may provide some relief to owners/clients. Sophisticated contractors can currently use the quick and "drop-dead" nature of the CCA adjudication process

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[22] CCA, s10
[23] CCA, s20(3)
[24] Bill, s9
[25] Bill, s6
[26] Bill, s16

to their advantage, by spending weeks preparing complex claims that respondents will have only five days to respond to.

Other recent major cases

53. Contractors seem to be in the courts almost as often as gang members and politicians, and there is a steady stream of case law. Three recent cases from the Court of Appeal and the Supreme Court are of particular interest.

Johnson & Ors v Auckland Council [27]

54. This December 2013 Court of Appeal case related to contributory negligence by buyers of leaky homes.

55. The buyers in this case had taken some particular risks, including failing to obtain a pre-purchase report or a LIM reports, when they were aware that the home might be leaky. In the High Court they had been found to be contributorily negligent, and had their claim reduced by 70% as a consequence. This was seen as a high water mark for contributory negligence in this area.

56. The Court of Appeal was kinder to the buyers. It was only prepared to reduce the claim by 40% on account of their contributory negligence.

57. Despite the Court of Appeal being kinder to the buyers, this case serves to further emphasise the importance of encouraging buyer clients to undertake full due diligence.

Blain v Evan Jones Construction[28]

58. This was another decision issued by the Court of Appeal in December 2013.

59. It related to alleged faults in the construction of an aquatic centre for the Grey District Council. A claim in negligence had been brought against the builder. That claim was struck out in the High Court, on the basis that the law did not recognise a cause of action in negligence against a builder of a commercial building.

60. The Court of Appeal overturned the strike out, and ordered that the issue should go to trial. It found that a claim in negligence against a builder of a commercial building was arguable.

61. Commercial builders may well react to this by ramping up the limitation of liability provisions in their contracts. Watch for this if you are acting for developers.

Osborne v Auckland Council[29]

62. This was a Supreme Court decision issued just a month ago. It related to limitation periods for leaky home claims.

63. The subject home in this case was substantially completed, and habitable, by August 1996. It received code compliance certificates in February and April

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[27] *Johnson & Ors v Auckland Council* [2013] NZCA 662 [18 December. 2013]
[28] *Blain v Evan Jones Construction Limited* NZCA 19 December 2013
[29] *Osborne v Auckland Council* [2014] NZSC 67

1997. The appellants, the Osbornes, bought it shortly after the CCCs were issued. They initiated a WHT claim in February 2007.

64. Section 14(a) of the Weathertight Homes Resolution Services Act 2006 requires that a claim must relate to a house that was "built" within the period of 10 years before the day the claim is brought.

65. The WHT, the High Court, and the Court of Appeal, knocked the claim out as out of time. But the Supreme Court disagreed. It found that the word "built" encompassed certifications, including the CCCs, so the claim was in time.

66. Given that CCCs are sometimes issued long after homes are otherwise complete, this decision may open the door to many leaky homes cases which might otherwise have been time-barred.

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