

# INDUSTRY UPDATE

## OWNERS CORPORATION LOSE ALL RIGHTS



Building & Construction | Corporate & Commercial | Commercial Litigation | Debt Collection | General Litigation | Insolvency | Insurance  
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### **BUILDERS NEGLIGENCE**

### **OWNERS CORPORATION LOSES ALL RIGHTS**

You may remember our previous industry update in the matter of *The Owners – Strata Plan No 61288 v Brookfield Australia Investments Pty Ltd (2013) NSWCA 317* where the Court of Appeal found that the builder of a commercial apartment block owed a duty of care to the Owners Corporation to avoid causing it to suffer loss resulting from latent defects in the common property which were structural or constituted a danger to persons or property.

The effect of this decision was that an Owners Corporation's (and potentially Bodies Corporate generally) were able to pursue builders and others for defective works where there is no other contractual or statutory warranty provisions provided or available (ie the Home Building Act).

In making its decision the Appeal Court looked at many previous decisions and found that:

- the builder owed a duty of care to the developer as well as contractual obligations;
- an Owners Corporation (as a successor in title) was also owed the same duty of care;
- the Owners Corporation was vulnerable (in a legal sense) in the circumstances ;
- that the Owners Corporation (and individual owners) could not be expected to carry out inspections of the entire building to see if there were defects;
- that the liability for economic loss (cost of repairs in this case) would be available;
- that the statutory warranties (in the Home Building Act in this case) did not limit any other duty that a builder may owe to successors in title (so this suggests that the decision of the Supreme Court in *Owners Corporation SP72535 v Brookfield Limited* known as the Star of the Sea case which we reported about before may also be open for reconsideration which is to the benefit of Owners Corporation particularly under the current Statutory warranty scheme).

#### **High Court Decision**

The Court of Appeal Decision was the subject of an appeal to the High Court which was heard on 16 June 2014. The High Court has published its decision in the matter of

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*Brookfield Australia Investments Limited (A.C.N 008 687 063)(Brookfield) v The Owners – Strata Plan No 61288 Proceedings Number S66/2014 HC*

***In its decision, the High Court unanimously allowed the appeal and set aside the Court of Appeal decision.***

### **Position for Owners Corporations prior to the High Court decision**

#### *Residential buildings*

Residential Buildings are subject to the *Home Building Act 1989 (HBA)* whereby certain statutory warranties apply allowing an Owners Corporation to take action against a builder and developer within a certain time frames for any issue relating to defects (6 years for structural defects and 2 years for other defects).

Further, the HBA provides a further protection to owners corporations for buildings which are less than 3 storeys high, whereby in circumstances where a builder becomes insolvent an insurance claim can be made to recover the damages suffered.

While also having available a claim for any contractual rights against a builder or developer, prior to the High Court decision, an owners corporation may also have had a separate right to make a claim against a builder or developer in negligence. Such a claim allowed for wider timeframes than the HBA in bringing a defect claim against the builder or developer in that a claim in negligence allowed an owners corporation to make a claim within 6 years of becoming aware of the structural defect.

#### *Commercial Buildings*

An Owners Corporation in respect of common property in a strata titled 'commercial' complex is not covered by the protections given to residential buildings under the HBA. Prior to the High Court decision, the only avenues available to an owners corporation to make a claim to recover loss arising from building defects in a commercial building was to take action against a builder or developer under a breach of contract and/or in negligence.

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Often, contractual terms which enable an owners corporation or lot owner to make a claim against a builder or developer are limited and are made in favour of a builder and developer and at the expense of an owners corporation or lot owner (ie: they can be limited to a period of 1 year or 6 months from the buildings completion date). This may not afford enough time for the defects to become apparent or for a claim to be made.

Prior to the High Court decision, an owners corporation also had a separate right to make a claim against the builder or developer in negligence for structural defects and could make that claim within 6 years of becoming aware of the defect.

### **The High Court Decision**

A decision has been handed down in the decision of *Brookfield Multiplex Ltd v Owners Corporation Strata Plan 61288 [2014] HCA 36* finding against the Owners Corporation and allowing the Appeal.

In a unanimous full bench decision, the High Court has determined that the Owners Corporation or the lot owners were not vulnerable as the lot owners had sufficient bargaining power to change the contractual terms they entered into with the developer.

The decision included four separate judgments which each came to the following conclusions:-

- a. That an owners corporation holds the common property as a trustee or agent for the lot owners in the scheme;
- b. The builder and developer, and the developer and subsequent purchasers (ie commercial lot owners) were each subject to detailed contractual arrangements including clauses which limited the defects liability period to dates much shorter than would be available in an action for negligence (ie: design and construct contract and sales contracts which in some instances limited the period of defect

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liability to seven months from completion). A claim in negligence cannot be made in circumstances where such detailed contracts exist;

- c. The purchasers of lots from the developer were effectively investors under standard form sales contracts which contained limited defects liability clauses. Accordingly, they were not 'vulnerable' but rather they were sophisticated investors who could bargain by amending the terms of the contract or choosing not to purchase at all.

Chief Justice French described the role of the Owners Corporation as a 'trustee' and examined the lot owner's ability to protect its rights.

The original lot owner was in fact the developer who contracted extensively with the builder in relation to building defects. Subsequent purchasers who purchased individual lots off the plan were also considered to have had sufficient bargaining power as their standard sales contracts provided some limited protections regarding building defects.

French CJ states that *"the Corporation was controlled by Chelsea [the developer]...who was a party to the contractual arrangements and therefore can be taken to have been fully apprised of the contractual arrangements and in particular the extent and limits of Brookfield's [the builders] obligations and liabilities in relation to defects in the common property."* He goes on to describe the subsequent owners as *"effectively investors in a hotel venture"* who could not be regarded as vulnerable.

### **What does this High Court decision mean for Owners Corporations?**

#### Commercial Buildings

Lot Owners and Owners Corporation of commercial buildings now have no ability to make a claim against a builder for building defects unless a contractual right exists for the Owners Corporation to do so.

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There is no ability to claim in negligence against a builder for building defects as the Court has held that no duty of care is owed.

This has created significant risk for any investor looking to buy into a commercial building where it has no ability to bargain for rights to take action for building defects and investors should seriously consider their position and obtain individual advice when considering such a purchase. Given that most development arrangements require the off the sale plan to be in a certain form, it is unlikely that the off the plan purchaser will have any real power to change the contractual relationship under this type of purchase other than to refrain from entering into an agreement at all.

### Residential Buildings

While the HBA has not been effected by the recent High Court decision an Owners Corporation and a lot owner's right to also make a claim in negligence may be extinguished altogether by the High Court decision.

While the High Court decision specifically did not deal with residential buildings there is also a strong argument that an Owners Corporation cannot make a claim in negligence at all as the High Court has found that it is difficult to see how any damage is suffered where an Owners Corporation merely acquires the common property without consideration (ie: it vests on registration of the strata plan) and acquires the common property regardless of the quality it is in.

### For any current negligence claims in building defect matters

All current actions against builders and developers which contain a claim against them in negligence and relate to commercial, retail and industrial apartment complexes will in all probability need to be withdrawn.

Serious consideration should be given to the impact of the High Court decision on any negligence claims involving residential apartment complexes.

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### **Broader Considerations**

The High Court decision has removed the rights of Owners Corporations in commercial buildings and residential buildings to make a building defect claim in negligence.

Anyone who owns or is considering owning a residential or commercial apartment, will be effected by these changes. All investors in commercial and residential buildings should now consider their position and obtain independent legal advice on their rights to make a claim for building defects and the possibility of having no claim at all to rectify building defects.

**For further information please contact Daniel Radman or Colin Grace on 9284 2700.**