HERBERT SMITH FREEHILLS

AUSTRALIAN CONSTRUCTION DISPUTE RESOLUTION NEWSLETTER

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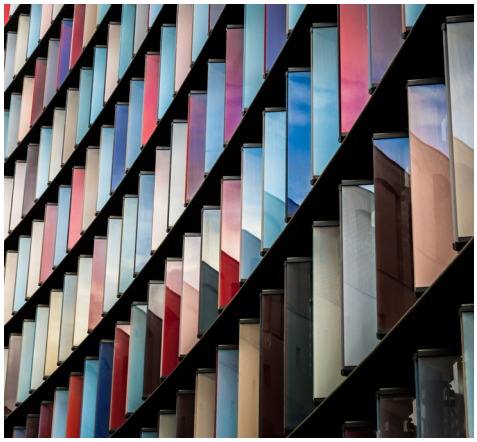

DECEMBER 2016

WELCOME

Welcome to this issue of Herbert Smith Freehills' Australian Construction Dispute Resolution Newsletter.

This newsletter updates you on legal developments relevant to your industry by featuring Australian court decisions and legislative developments of particular interest.

In this issue, we look at:

- A recent decision of the Supreme Court of New South Wales considering whether and to what extent an owners corporation could amend its statement of claim to include new particulars of breach of the statutory warranties afforded by the *Home Building Act 1989* (NSW) despite the expiry of the statutory warranty period and long-stop for 'building actions'.
- The first raft of reforms to the *Construction Contracts Act 2004* (WA) which have been passed by Parliament and many of which come into effect on 15 December 2016.
- A decision of the Victorian Supreme Court which considered an application to strike-out a claim for misleading and deceptive conduct where the representations were the terms of a construction contract, and the offending conduct was essentially the failure to meet them.

We trust that you will enjoy this and future issues of the Australian Construction Dispute Resolution Newsletter.

ABOUT HERBERT SMITH FREEHILLS

Herbert Smith Freehills offers clients involved in engineering and construction projects a track record of providing innovative and commercially astute advice across a range of industries and legal issues.

The practice is diversified and balanced between contentious and non-contentious work in many jurisdictions around the world. Our team has advised clients on many of the world's largest and most complex engineering and construction projects.

Our contentious work encompasses a broad mix of complex, high value disputes which are resolved in a variety of jurisdictions, applying such processes as litigation, arbitration, adjudication (including adjudication boards), expert determination, early neutral evaluation and mediation.

DEFECTS AND LIMITATION PERIODS: CAN CLAIMS BE EXPANDED TO INCLUDE NEW DEFECTS AFTER THE EXPIRATION OF LIMITATION PERIODS?

In *The Owners — Strata Plan 76841 v Ceerose Pty Ltd* [2016] NSWSC 1545, Justice Stevenson of the Supreme Court of New South Wales considered whether to grant leave to an Owners Corporation (**OC**) to amend its statement of claim to include new defects after the expiry of the warranty period under the *Home Building Act 1989* (NSW) (the **HBA**) and the 10 year 'long stop' under the *Environmental Planning and Assessment Act 1979* (NSW) (the **EPAA**).

Background

Proceedings were commenced by the OC of an eight storey building, comprising 64 residential lots, in Waitara, NSW. Ceerose Pty Ltd, the first defendant, was the builder, and Prisand Pty Ltd, the second defendant, was the developer.

Building work commenced in September 2005, and the final Occupation Certificate was issued on 10 April 2006.

In February 2012, the OC commenced proceedings in the Consumer Trader and Tenancy Tribunal alleging the existence of defects in the building work and breach of the statutory warranties implied in the building contract under section 18B of the HBA. Two years later, the proceedings were transferred to the District Court; the proceedings were again transferred, to the Supreme Court, in May 2016.

It was common ground that:

- the seven-year warranty period provided for under section 18E of the HBA had expired on 10 April 2013 (7 years after the final Occupation Certificate).
- the 10 year long-stop period under section 109ZK of the EPAA had expired on 10 April 2016 (10 years after the final occupation certificate).

On 7 March 2016, the OC raised a new water ingress defect (by way of an affidavit sworn by the OC's solicitor), with evidence of the new defect not being served until mid-May 2016. By this time the long-stop period under section 109ZK of the EPA had expired. At around the same time, the OC transferred the proceedings to the Supreme Court and subsequently applied for leave to amend its claim to include the new water ingress defect, as well as other new defects.

Decision

Ceerose opposed the application to amend so far as it concerned the addition of the water ingress defect and another category of defects, the 'fire and BCA defects'.

Ability to add new defects after the seven-year warranty period

The builder submitted that the water ingress defect was 'wholly new' and should be rejected. This was on the basis that:

- it arose out of a cause of action which had expired at the end of the seven year period under section 18E of the HBA.
- it did not arise from the same or substantially the same facts as those giving rise to an existing pleaded cause of action – which would have provided a basis for allowing it under section 65 of the *Civil Procedure Act 2005* (NSW).

Justice Stevenson rejected this submission. His Honour observed that:

- the appropriate question was whether the introduction of the new water ingress defect would amount to the introduction of a new cause of action.
- the OC's claim was in contract (albeit relying on the implied statutory warranties under the HBA).

- cases considering res judicata, and specifically cases where a party to a building contract had sued a builder to judgment, and then sought to bring further proceedings arising from later discovered defects, could be applied to the limitation context, and held:

  > It seems to me that if there is "but one cause of action for breach of contract" ... for the purposes of the doctrine of res judicata, the same must be true for the purposes of the law of limitation. That is because both are concerned with whether a right to bring a cause of action has been extinguished.

- it was at least arguable that the addition of the water ingress defect to the OC's claim did not introduce a new cause of action.

Accordingly, his Honour observed that he would not have refused the application for leave to introduce the water ingress defect on a limitation basis.

Ability to add new defects after the 10 year long-stop period

However, it was especially significant that the 10 year long-stop had also expired.

The builder submitted that the amendment to introduce the water ingress defect should be disallowed in any event because of the 'obvious and significant' prejudice it would cause to the builder as a result of the expiry of the 'long-stop' period.

The builder was able to identify several parties, including subcontractors, as potential cross-defendants. As the long-stop period had expired the builder could no longer bring a 'building action' against any of those parties.

The Court held that if the builder could show that it had 'viable and realistic' as opposed to 'fanciful and theoretical' claims, then to allow the amendments would be prejudicial. The court rejected the OC's argument that the builder did not have a 'viable and realistic' claim because any contract claims against those parties had expired. The court also rejected the submission that there would not be a tort claim available and emphasised that concurrent liability in contract and tort is well recognised.

The Court held that with the expiry of the long-stop, the builder 'lost an opportunity to prosecute viable and realistic cross-claims and that it would thereby suffer obvious and significant prejudice if the proposed amendment was allowed.'

The Court also considered the builder's objection to the 'fire and BCA' defects claim.

The OC had included Fire and BCA defects in a list of defect particulars annexed to the statement of claim dated 19 August 2014. It was not out of time. The Court, however, noted that no figure was ascribed to the defect until 7 March 2016 when a letter affixed to an affidavit stated the amount claimed was $336,000.

Justice Stevenson held that it was reasonable for the builder to await service of expert reports before making a decision about pursuing cross claims in relation to these defects. The Court also accepted evidence from the builder that it had decided to defer investigation of potential cross claims unless and until a single claim in the order of $300,000 emerged.

Justice Stevenson held that he was satisfied that had the OC served its evidence before the expiry of the long-stop, and had the OC complied with the Court-ordered dates of March and August 2015 for serving this evidence, the builder would have taken a different approach, and taken steps concerning cross claims.

Accordingly, because the long-stop expired before service of the OC's evidence, the Court held that the builder could no longer bring a claim against the certifier and had suffered similar prejudice to the prejudice it had suffered in relation to the water ingress defect.

However, the Court observed that in December 2014 it was prepared to take a risk up to a particular quantum. Accordingly, the Court allowed the claim up to $195,000.

What this means for you

In the circumstances of this case, the Court was prepared to permit an OC to expand its claim to include new defects arising from alleged breach of the implied warranties under the HBA even though the 7 year warranty period under the HBA had expired. This suggests that, where proceedings have been commenced within the warranty period, the subsequent expiry of the warranty period may not be effective to prevent the OC from enlarging its claim to include new defects.

If, however, the 10 year long-stop period has expired, the decision illustrates that leave may be denied if the defendant can show it has, by reason of the expiry, lost the ability to pursue 'viable and realistic' claims against other parties, such as subcontractors.

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EVOLUTION, NOT REVOLUTION – THE FIRST RAFT OF REFORMS TO THE *CONSTRUCTION CONTRACTS ACT 2004* (WA) PASSED BY PARLIAMENT

On 22 November 2016, the WA Parliament passed the *Construction Contracts Amendment Amending Bill 2016* (WA), taking effect as the *Construction Contracts Amendment Act 2016* (WA) (**Amending Act**). The Amending Act received Royal Assent on 29 November 2016.

The Amending Act makes changes to the *Construction Contracts Act 2004* (WA) (**CCA**), as part of some initial measures outlined in the Government's response to Professor Philip Evans' Report on the Operation and Effectiveness of the CCA (**Response**), to improve the operation of the CCA and the rapid adjudication process. A 'second raft of reforms' will be introduced at a later time.

The amended CCA will be complemented by, among other things, a Code of Conduct for contractors, the establishment of a compliance unit within the Department of Commerce and an increased role of the Small Business Commissioner.[1]

The Code of Conduct was announced on 5 December 2016, to take effect on and from 1 January 2017 to 'major State contracts worth more than $10 million'. In part, the Code is intended to 'promote timely payment of subcontractors'.[2]

Amendments to the CCA

The following amendments, contained in the Amending Act, are reflective of the proposed changes identified in the Response:

- significantly increasing the time in which adjudications applications can be made, from 28 days to 90 business days;
- reducing maximum payment terms permitted in construction contracts from 50 calendar days to 42 calendar days, from 3 April 2017;
- altering the time periods from calendar days to business days and excluding the dates 25 December to 7 January inclusive;
- permitting recycled claims; and
- removing the obligation to dismiss applications for technical deficiencies, leaving this at the discretion of the adjudicator.

Notably, the Amending Act does not contain any amendments in relation to the following changes proposed in the Response:

- additional and ongoing registration and renewal process for adjudicators; and
- penalties for failure to comply with prohibited terms.

Additional amendments

(a) The 'mining exclusion'

Although its operation is unclear, the Amending Act contains an amendment to section 4(3)(c) that appears, consistent with the tenor of Professor Evans' Report, to restrict the reach of the 'mining exclusion' (i.e. 'constructing plant' for the purposes of extracting or processing resources will now potentially be caught by the CCA).

(b) When a 'payment dispute' arises

Somewhat unexpectedly, and perhaps coincidentally with the Court of Appeal decision in *Laing O'Rourke Australia Construction Pty Ltd v Samsung C&T Corporation* [2016] WASCA 130 delivered on 21 July 2016, the Amending Act contains an amendment to clarify when a payment dispute arises and clear up the confusion identified in several recent decisions.[3]

(c) Enforcement of determinations

The Response indicated that the Government would consider a change to facilitate speedy registration of adjudication determinations by court order. The Amending Act identifies the method for doing so.

The amendment removes the requirement for the leave of the court to be obtained in order for a party to enforce a determination. The party entitled to payment may obtain an order from the Court and, accordingly, enforce the order by simply filing at court:

- a certified (by the Building Commissioner) copy of the determination; and
- an affidavit of the unpaid amount under the determination.

Conclusion

The amendments are aimed at addressing industry issues such as unscrupulous and insolvent contractors, and assisting smaller and exposed subcontractors.

The provisions of the Amending Act will come into effect on 15 December 2016, with the exception of:

- amendments to section 10 (provisions requiring payment to be made after 42 days); and
- the insertion of a new section 60 (payment periods),

which will come into effect on 3 April 2017.

ENDNOTES

1. Media Statement – Construction Contracts Act amendments introduced, Thursday 22 September 2016 (Hon Sean L'Estrange MLA Minister for Mines and Petroleum; Finance; Small Business and Hon Michael Mischin MLC Attorney General; Minister for Commerce) https://www.mediastatements.wa.gov.au/Pages/Barnett/2016/09/Construction-Contracts-Act-amendments-introduced.aspx.
2. Media Statement – New code of conduct for WA's building industry, Monday 5 December 2016 (Hon Sean L'Estrange MLA Minister for Mines and Petroleum; Finance; Small Business, Hon Michael Mischin MLC Attorney General; Minister for Commerce and Hon Mike Nahan MLA Treasurer; Minister for Energy; Citizenship and Multicultural Interests) https://www.mediastatements.wa.gov.au/Pages/Barnett/2016/12/New-code-of-conduct-for-WAs-building-industry.aspx.
3. *Blackadder Scaffolding Services (Aust) Pty Ltd and Mirvac Homes (WA) Pty Ltd* [2009] WASAT 133; *Fuel Tank & Pipe Pty Ltd and Decmil Australia Pty Ltd* [2010] WASAT 165; *Northern Territory v Urban and Rural Contracting Pty Ltd* [2012] NTSC 22; *Cape Range Electrical Contractors Pty Ltd v Austral Construction Pty Ltd* [2012] WASC 304; *Alliance Contracting Pty Ltd v James* [2014] WASC 212; *Field Deployment Solutions Pty Ltd v SC Projects Australia Pty Ltd* [2015] WASC 60; *Laing O'Rourke Australia Construction Pty Ltd v Samsung C&T Corporation* [2015] WASC 237; *Laing O'Rourke Australia Construction Pty Ltd v Samsung C&T Corporation* [2016] WASCA 130.

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CAN A FAILURE TO MEET CONTRACTUAL PROMISES IN A CONSTRUCTION CONTRACT GIVE RISE TO MISLEADING AND DECEPTIVE CONDUCT?

The Victorian Supreme Court in *WTE Co-Generation v RCR (No 3)* [2016] VSC 674 recently refused to summarily dismiss a claim which relied on the terms of a construction contract as representations capable of giving rise to misleading or deceptive conduct under section 52 of the *Trade Practice Act 1974* (Cth) (the **TPA**) and section 18 of the *Australian Consumer Law* (the **ACL**).

Background

The proceedings relate to a dispute arising from the construction of a cogeneration plant in the Melbourne suburb of Coolaroo.

In October 2008, Visy Paper contracted with RCR Energy to design, construct and commission the plant. The rights and obligations of Visy Paper under the contract were later novated to WTE.

The plaintiffs (WTE and Visy Energy) alleged that the defendants (RCR Energy and RCR Tomlinson, together called RCR) engaged in misleading or deceptive conduct in contravention of section 52 of the TPA or section 18 of the ACL.

The representations relied on by the plaintiffs were terms of the contract regarding:

- the plant's future performance capacity;
- RCR Energy's qualification and experience; and
- the suitability of RCR Energy's proposal for the works under the contract (to ensure the works would achieve the performance guarantees).

These terms are of the kind commonly found in an EPC contract.

The plaintiffs alleged that the representations were false in that, among other things, the plant was not capable of reaching the performance capacity specified in the contract, and was not complete by practical completion.

It is these terms which the plaintiffs alleged gave rise to an actionable misrepresentation, because, for instance, they alleged that the plant could never reach the level of output specified in the contractual warranties.

The defendants sought summary judgment to strike-out the TPA/ACL claim under section 62 and 63 of the *Civil Procedure Act 2010* (Vic) on the basis that the claim had no real prospects of success.

Among other things, the defendants submitted that the making of contractual warranties could not amount to a misrepresentation which is actionable under the TPA/ACL.

The plaintiffs rejected this and further submitted the representations were representations as to future matters within the meaning of section 51A of the TPA and section 4 of the ACL. As a consequence, they reasoned that if the defendants did not adduce evidence to the contrary, the representations would be considered to be made without reasonable grounds and taken to be misleading.

Decision

Justice Vickery dismissed the summary judgment application on the basis that the defendant had failed to show the cause of action had 'no real prospect of success'.

His Honour acknowledged the reservations evident in previous authorities considering whether contractual terms could be relied on as representations grounding a TPA/ACL claim.

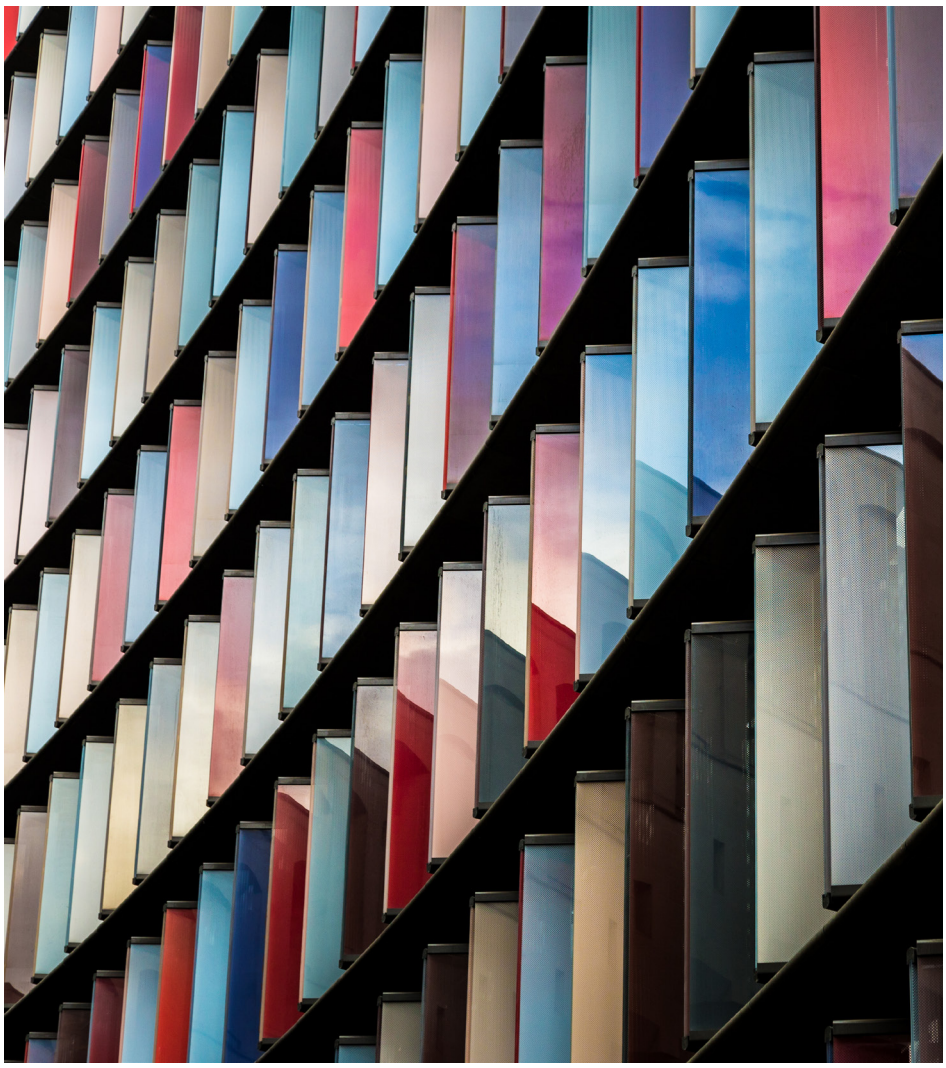
His Honour also recognised that there were unique elements to this case. His Honour observed that there was no direct authority relating to a situation where the alleged misleading or deceptive conduct comprised a representation made in a contractual promise, and where that promise was alleged to have been false on the basis that it was not fulfilled. His Honour also noted that this is a case where the contractual promises relied on relate to performance standards which comprise terms of a construction and engineering contract.

However, his Honour pointed to a substantial body of authority supporting the position that contractual provisions may constitute conduct in contravention of the TPA/ACL. His Honour held:

> Here we have a situation where statutory rights are sought to be superimposed on the rights created by terms of the agreement negotiated by the parties. Proof of the breach of the contract will need to be established by the Plaintiffs if they are to succeed in the contractual cause of action. The fact that the same body of facts may also be deployed to establish contravention of legislative provisions, at first glance, does not preclude the statutes from being engaged. In principle, and subject to further analysis and argument, there would appear to be no impediment in law to proceeding in this way, as the authorities presently stand. However, this will be a matter for the trial.

Ultimately, the Court emphasised earlier authority that whether particular conduct is misleading or deceptive is a question of fact to be determined in the context of the evidence to be adduced at trial, including the relevant surrounding facts and circumstances.

His Honour noted some of the factors that may well be relevant in determining the claim at trial, including the contractual context and the fact that 'construction is a risky business'. Indeed, his Honour observed that 'it may be, for example, that the representations conveyed an intention to perform to the performance standards, but qualified by the usual risks of non-performance for projects of this type undertaken in the context of the Contract.'



What this means for you

The Court has refused to rule out the possibility that making contractual promises can constitute actionable representations for the purposes of the ACL/TPA.

Assuming the matter proceeds to trial, the Court's decision in the substantive proceedings will be awaited with interest. The possibility of making and failing to meet contractual promises in a construction contract giving rise to claims for misleading and deceptive conduct has significant implications given the possibility of longer limitation periods for an ACL/TPA claim (given the timing of accrual of the cause of action) and the potential application of insurances that may well provide cover for ACL/TPA claims, but exclude cover for breach of the type of contractual promises underpinning the claim.

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