

ARTICLE

Construction Law Update, 2013 in review

A paper delivered in the lecture given 20 November 2013. By Toby Shnookal S.C.

Introduction:

This paper was presented at the well attended Annual General Meeting and Dinner of the Building Disputes Practitioners Society in Melbourne on 20 November 2013. In this paper the author reviews the most significant developments in construction law over the last 12 months from a Victorian perspective.

The Building Commission replaced by Victorian Building Authority:

On 10 December 2012 the Victorian Ombudsman released a report detailing the corruption and financial incompetency of the Building Commission. \$200,000 had been spent on meals and entertainment. Over \$950,000 had been spent on sponsoring events and awards to bodies such as the Victorian branches of the MBA and HIA. Builders were almost never prosecuted for breaches of the building regulations and obtaining registration as a builder was too easy, according to the Ombudsman. The Commission lacked proper governance and had been involved in the questionable employment of staff.¹

The result was the Commission was replaced by the Victorian Building Authority. That Authority commenced operation on 1 July 2013. Senior Commission staff did not retain their positions. At the same time the Authority's role was expanded to include roles previously performed by the Plumbing Industry Commission and the Architect Registration Board.

Twelve months later the Attorney General announced some dramatic changes to the way domestic building disputes are to be dealt with in this state and the role the Authority is intended to have. I return to these changes at the end of this paper.

In terms of case law, there have been a number of significant cases this year.

Dura v Hue – Parties to a contract intend discretionary decisions of superintendents to be final and binding. They cannot be reviewed on their merits:

The first case I want to focus on is the recent decision of the Victorian Court of Appeal in *Dura (Australia) Constructions Pty Ltd v Hue Boutique Living Pty Ltd*,² (**Dura**) a decision of 26 July 2013. In this decision the Court of Appeal affirmed the decision of Dixon J and, in turn, his adoption of the reasoning of the WA Supreme Court in the judgment of Justice Ipp in *WMC Resources v Leighton Contractors Pty (WMC)*.³ Conversely, the Victorian Court of Appeal rejected the English approach on the same issue reflected in the House of Lords decision in *Beaufort Developments (NI) Ltd v Gilbert-Ash NI Ltd (Beaufort Developments)*.⁴

The main difference in the lines of authority is this: In the English line of cases, for a superintendent's determination under a building contract to have the effect that it is final, binding, and can not be reviewed on the merits, the parties have to expressly say that in their contract; similar to the way that standard form contracts in Australia often specify this in respect of the effect of a Final Certificate. However, in the Australian line of authority, which started in WA and has now spread to Victoria, a determination made within the contract by a Superintendent is considered to be non-reviewable on its merits by a court or an arbitrator if in making his or her determination the superintendent has been called on to make a discretionary determination.

It follows that *Dura* stands for the proposition that valid discretionary determinations of superintendents are non-reviewable by an arbitrator or a court on their merits. In my view, the significance of the decision is underscored by my perception that almost every determination by a superintendent under a building contract is discretionary.

I believe this is very significant and challenging decision. I have written a paper on it that is shortly to be published in the online journal, *Construction Law International* which is published by the International Bar Association.⁵ That paper will also be on the Melbourne TEC Chambers website.⁶ It is a significant decision and appears not to be as well known as it should be.

In England, in the case of *Beaufort Developments*, the leading judgment of Lord Hoffman set out the sound reasons why parties to a construction contract do not, in the absence of clear words to the contrary, intend certificates of superintendents to have final and binding effect.

He said:

“to make the certificate conclusive could easily cause injustice. It may have been given when the knowledge of the architect about the state of the work or the effect of external causes was incomplete. Furthermore, the architect is the agent of the employer. He is a professional man but can hardly be called independent. One would not readily assume that the contractor would submit himself to be bound by his decisions, subject only to a challenge on the grounds of bad faith or excess of power. It must be said that there are instances in the 19th century and the early part of this one in which contracts were construed as doing precisely this. There are also contracts which provided that in case of dispute, the architect was to be arbitrator. But the notion of what amounted to a conflict of interest was not then as well understood as it is now. And of course the inclusion of such clauses is a matter for negotiation between the parties or, in a standard form, the two sides of the industry,

1. [Ombudsman Finds Overspending and Corruption in Victorian Building Commission, Devenish and Barrance, 148 ACLN 50]

2. [2013] VSCA 179

3. (2000) 16 BCL 53

4. [1999] 1 AC 266.]

5. http://www.ibanet.org/Publications/publications_construction_law_international.aspx

6. <http://www.mtecc.com.au/>

so that what is acceptable will to some extent depend upon the bargaining strength of one side or the other. At all events, I think that today one should require very clear words before construing a contract as giving an architect such powers."

The recent Australian cases, now including our own Court of Appeal, do not follow that reasoning.

As referred to above, the Australian line of authority starts with the decision in the WA case of *WMC Resources v Leighton Contractors Pty*. In *WMC* the contract gave the power to the principal itself, WMC, to value variations performed by the contractor, Leighton, which the contract said was to be "in its sole discretion" although a schedule of rates was referenced as well.

Justice Ipp (with whom Justices Kennedy and White agreed) described the contractual role WMC had to perform, as including deciding whether or not the schedule of rates were relevant to any particular variation, as being 'essentially discretionary'.

His Honour then said that this finding was: "critical to the resolution of this appeal" and it followed that His Honour concluded that the parties had intended, by their contract, that the valuation of variations by WMC was to be final and binding, even though the contract did not expressly say that.

The result was that the Court of Appeal in WA held the arbitrator could not review WMC's assessments of Leighton's entitlements for variations on their merits under a broad arbitration clause in the contract.

Reduced to its most basic, the court considered that, because the parties had agreed the superintendent was to perform a discretionary valuation, neither the court nor the arbitrator had the power to replace the superintendent's assessment of the contractual entitlement with their own.

Adopting the reasoning in *WMC*, Dixon J, the judge at first instance in *Dura*, said:

"I am satisfied that the resultant certificate, involving discretionary judgment by the superintendent who, adopting [a quantity surveyor's] work, ascertained the costs as required by cl 44.6, followed the process contemplated by the contract and that process is not open to review for error. It is final and binding."

The Victorian Court of Appeal adopted the reasoning in *WMC* too. Maxwell P noted that "the most comprehensive analysis of the applicable principles is to be found in [*WMC*]" and he set out the principles as had been enunciated by Ipp J as follows⁷:

1. By the contract, the parties agree to be bound by a determination made in accordance with the terms of the contract. If the valuation complies, the parties are bound.
2. A court (or an arbitrator) will not set aside a determination merely on the ground that it is incorrect or that it reveals errors. The determination will only be interfered with if it is not made in terms of the contract.
3. There will ordinarily be implied terms of the contract that the process of making the determination will be conducted honestly, bona fide and reasonably.

4. Given that the parties have bound themselves to accept a determination which complies with the contract, a statement in the contract that the determination is 'final and binding' adds little.
5. No different approach is required where, in accordance with the contract, the determination is made by one of the parties to the contract or its representative.

The Western Australian *WMC* decision and the line of authority it represents has been the subject of some criticism by authors more learned than I, but I add my voice to those of the critics. For the reasons set out by Lord Hoffman, in the absence of express words, I find it difficult to accept contractors intend determinations of the superintendent or, as in *WMC*, the principal itself, to be final and binding whether they contain a discretionary element or not.

The decision has not been appealed to the High Court so it remains to be seen what the High Court thinks of this line of authority that holds valid superintendent's discretionary assessments are final and binding.

Proportionate Liability

Moving on to the area of proportionate liability, there has been a recent decision of the High Court that overrules the views of both the Victorian and the NSW's Courts of Appeal on when proportionate liability applies.

The proportionate liability regime was introduced into Australian states between 2004 and 2005 with every state adopting similar, but not uniform, legislation.

Under proportionate liability, the amount a defendant has to pay is limited to an amount that reflects that defendant's responsibility for the loss.

To enliven the proportionate liability protection, two things must be established. First, the claim must *arise from a failure to take care* [Section 24AF (1) (a), Wrongs Act 1958]. Second, the acts or omissions of one defendant must have *caused* the same loss or damage the subject of the claim against the other defendant [Section 24 AH (1)].

The Victorian Court of Appeal had considered the second of these tests in *St George Bank v Quinerts Pty Ltd (Quinert)*, a 2009 decision⁸. In that case St George had loaned money to a purchaser of a unit on the basis of a valuation by a professional valuer, Quinerts. The borrower defaulted and the Quinerts valuation was as over-valuation and did not completely secure the loan.

The Victorian Court of Appeal held Quinerts was not protected by the proportionate liability legislation because the loss St George had suffered as a result of the borrower not repaying the loan was, in law, a different loss to the loss suffered by St George because the sale price of the unit was not the valuation Quinerts had given. Justice Nettle, with whom Mandie and Beach JJ agreed, said:

"I do not consider that the borrower .. could be said to have caused or be liable for 'the same damage' as Quinerts. The loss or damage caused by the borrower .. was the failure to repay the loan. Nothing which Quinerts did or failed to do caused the borrower .. to fail to repay the loan".⁹

7. Ibid, at paragraph [18]

8. [2009] VSCA 245

The result of this technical differentiation of loss has been that it has always been at least arguable in building cases to assert that the proportionate liability legislation does not apply to particular claims. Sometimes the assertions have been successful. For example in the VCAT case of *TCM Builders Pty v Nikou & Kay*,¹⁰ SM Riegler held that the builder was not protected by the proportionate liability legislation even though claims to fix the same defects had been made against the supervising architect, the design engineer and others and they had all paid money to settle those claims. The decision is under appeal; but not on any ground that relates to the decision on proportionate liability. In my view, the judgement correctly applied the reasoning in *Quinert*. Indeed, in his judgment in *Quinert*, Justice Nettle had given one example of when proportionate liability would not apply as being where a claim was made by a principal against both an architect and a builder. In the reasoning Justice Nettle gave, the loss claimed against an architect for breach of its contract in giving a builder an extension of time (and thus precluding recovery from the builder for the cost of delay suffered by the principal) is different from a loss claimed against the builder for its breach of contract in the delayed performance of the building contract.

The High Court has swept away such a legal analysis by its decision in *Hunt & Hunt v Mitchell Morgan Nominee Pty Ltd*.¹¹ In my view the test of the requirement of the same loss having been suffered in the *Quinert* decision was too limited.

In *Hunt & Hunt*, handed down this year, a defrauded plaintiff, sued both the fraudsters and the plaintiff's solicitor who should have protected it from the fraud. The High Court looked at the causative effect of the solicitor's acts and omissions and concluded they had materially contributed to the plaintiff's loss. Based on causation, the High Court then came to the view the proportionate liability legislation did have operation and operated to limit the negligent solicitor's liability to the proportion of the loss that it had caused the plaintiff.

It is quite possible in considering this case, indeed in relation to the entire concept of proportionate liability, to have a lively discussion about the justice of the decision. Under proportionate liability legislation, part of a guilty defendant's loss is moved, in the first instance, onto the plaintiff who may not have done anything wrong and may not be able to recover that loss from another guilty defendant. In *Hunt & Hunt*, the solicitor had been engaged by the plaintiff to protect it from precisely the sort of fraud that had taken place, and yet it was the plaintiff that suffered the non recoverable loss apportioned to the fraudsters; not the solicitors it had engaged to protect it from a fraud. But, going back in time, that was the somewhat unholy purpose of introducing the proportionate liability legislation in the first place. It was to shift to the plaintiff part of the loss that otherwise the insurance companies of professionals would pay.

The result is that *Hunt and Hunt* has breathed new life into the proportionate liability legislation, and, from my view, the test of whether or not it applies in construction cases has been made clearer.

But there is still abundant uncertainty. Even tree roots have become entangled in the proportionate liability legislation. In the County Court decision in *Hiss v Galea* decided 21 December 2012,¹² Judge Anderson held that a nuisance claim for tree roots that caused damage was a claim that arose from a failure to take care even though that is not an element of a cause of action in nuisance and no allegation along that line was made. His Honour came to that conclusion because the neighbours who planted the trees had not installed a root barrier or carried out a more modest planting. That case is currently on appeal to the Court of Appeal.

Commercial Arbitration

In respect of proportionate liability at least in the area of Arbitration the law is now reasonably clear. Proportionate liability just doesn't apply. In the Western Australian case of *Curtin University of Technology v Woods Bagot Pty Ltd* the Court of Appeal held the proportionate liability legislation in that state¹³ did not apply to arbitral proceedings. In Victoria the Act specifically prohibits courts from having regard to the comparative responsibility of non-parties and it therefore follows that the arguments in *Curtin* that the proportionate liability legislation has no effect are even stronger here.

In Victoria, the new domestic Arbitration Act, the *Commercial Arbitration Act 2011*, came into operation on 17 November 2011 and there are two recent decisions on it. One of the differences between the new domestic arbitration Act and the one it replaced is that a court must stay court proceedings if there is a valid arbitration agreement. In *Subway Systems Australia Pty Ltd v Aaron Ireland*,¹⁴ a decision of Justice Croft handed down 18 October 2013, His Honour considered an appeal from a decision of VCAT's SM Reigler who had refused to stay VCAT proceedings where there was an arbitration agreement as part of a commercial lease. Justice Croft performed a broad review of the Act, concluded VCAT was not a court as referred to in the Act, and therefore concluded VCAT was not compelled to stay its own proceedings.

On the other hand, and perhaps more significantly, in *Lysaght Building Solutions Pty Ltd v Blanalko Pty Ltd*,¹⁵ a decision handed down 21 August 2013, Justice Vickery considered the arbitration clause in AS 4000 – 1995 and determined that under the new domestic arbitration Act, the Supreme Court was compelled to stay court proceedings of the substantive dispute where a Notice of Dispute had been served.¹⁶

In respect of the Commonwealth Arbitration Act, the High Court this year published its decision in *TCL Air Conditioner (Zhongshan) Co Ltd v Judges of the Federal Court of Australia*¹⁷ in which it found that the International Arbitration Act 1974 (Cth) is constitutionally valid.

Adjudication

There have been quite a number of significant decisions on adjudication across Australia in the last twelve months, but this paper will just focus just on the Victorian ones.

9. Ibid, at [76]

10. VCAT, 13 March 2012

11. [2013] HCA 10

12. [2012] VCC 2010

13. Part I F of the Civil Liability Act 2002 WA

14. [2013] VSC 550

15. [2013] VSC 435

16. Ibid at par [125] & [142]

17. [2013] HCA 5

The most significant of these, in my view, is the decision in *Sugar Australia Pty Ltd v Southern Ocean Pty Ltd*, a decision handed down 15 October 2013.¹⁸ In this case Justice Vickery declined to follow the considerable line of authority in Victoria, largely his own decisions, that had held that an adjudicator's determination of jurisdictional facts could not be reviewed by a court. (eg *Grocon Constructions v Planit Cocciardi Joint Venture (No 2)*, and followed recently by Justice McMillan in *Maxtra Constructions Pty Ltd v Active Crane Hire Pty*¹⁹). In *Sugar Australia* His Honour held that where an adjudicator's jurisdiction is challenged, the adjudicator should make a determination, but it falls to the court to conclusively determine the jurisdictional facts on which jurisdiction might depend. Importantly, in performing that review, His Honour held that the court could receive further evidence that had not been presented to the adjudicator.

In another decision concerning adjudication, in *Maxtra Constructions Pty Ltd v Gilbert*,²⁰ a decision handed down 10 May 2013, Justice Vickery decided claims for defects are not claims for damages and thus excluded amounts. Unsurprisingly, in my view, His Honour held the existence of defects in the works reduces the value of the construction work that had been carried out, which is the default way by which construction work is valued under section 11 (b) of the *Building and Construction Industry Security of Payment Act*. More interestingly, in my view, is that His Honour considered it was the default valuation provision that applied because he held the contract **did not** provide a means for valuing the entitlement. The valuation term of the contract provided that "the progress claim will be based on the subcontractor's tender breakdown and expressed in percentages against each component."²¹ His Honour held such a provision did no more than provide the "broad parameters within which a calculation might be calculated," and hence the contract did not provide for a method of valuing the progress claim.

In my view, following His Honour's reasoning, it will be rare for a contract to actually provide for a method of valuing a progress claim in the terms used by the Security of Payment Act.

Further, and as an aside, in my opinion the valuation provision in the contract Vickery J was considering, like just all valuation terms in similar contracts, provided the superintendent only broad parameters for the valuation. Essentially the valuation was *discretionary* in the same way the Court of Appeal considered the valuation clause in *Dura*. If that is right, then it should follow on the *final* determination of the rights of the parties, applying the rationale of *Dura*, the superintendent's determination should be unchallengeable. This creates an interesting legal round robin because in *Martinek Holdings Pty Ltd v Reed Constructions (Qld) Pty Ltd*²² it was held that an adjudicator's determination trumped a final certificate given by a superintendent.

Another Victorian Supreme Court decision on adjudication grappled with reference dates in adjudication. In *Jothan Property Holdings Pty Ltd v Cooperative Builders Pty Ltd*, a decision handed down 17 October 2013,²³ the vexed question of reference dates arose for determination in the context of a number of payment claims that had been served in respect of an entitlement to be paid on achieving stages of the work. The adjudicator had accepted later copy payment claims were validly served in relation to different

reference dates. Vickery J followed his decision in *Sugar* in terms of when jurisdictional facts should be reviewed by the court, and went on to review the adjudicator's determination of reference dates which was jurisdictional. His Honour held reference dates under the contract before him only occurred on completion of stages of work. That is, when a stage was completed, a reference date occurred and the claimant had one chance to serve a payment claim, and proceed to adjudication if dissatisfied. The determination of the adjudicator was without jurisdiction.

Injunctions under AS 4000

Justice Vickery has not only been active in adjudication. In the most recent decision mentioned in this paper, *Mainstream (Aust) Pty Ltd v Gilpip Projects Pty Ltd*, a decision of 13 November 2013,²⁴ Justice Vickery considered an application to injunct the cashing of a contractor's bank guarantee to pay the amount of the Superintendent's Final Certificate. The Contractor had served a Notice of Dispute challenging the validity of the Final Certificate. The contract was an AS 4000 – 1997 and in his decision His Honour considered the usual discretionary principles. Of prime importance, in my view, His Honour held that the terms of AS 4000 arguably comprised a contractual promise not to call upon a Bank Guarantee where a Notice of Dispute had been served. That is, in the terms usually used in discussion about bank guarantees, AS 4000 contains a contractual impediment to cashing a Bank Guarantee once a Notice of Dispute is served.

Agreement to negotiate not enforceable

In *WTE Co Generation v Visy Energy Pty Ltd*,²⁵ a decision handed down 21 June 2013, Justice Vickery held that the standard provisions contained in Standards Australia Contracts for parties to meet prior to issuing a Notice of Dispute was not an enforceable contractual requirement. Standards Australia promptly sent out what it called a "Standards Alert" advising users of AS 2124, AS 4000 and 20 other standard form contracts of the decision.²⁶

Watch this space

There are four areas of law I want to mention in the "watch this space" area.

Brookfield - Negligence, vulnerability and whether a Design & Construct (D&C) builder owes a duty of care to an owners corporation

*The Owners – Strata Plan No 61288 v Brookfield Australia Investments Ltd*²⁷ is a significant case, but I will only briefly mention it. In this case the New South Wales Court of Appeal unanimously held a design and construct builder owed an owners corporation a duty of care for latent defects in common property. It came to this conclusion on its analysis of when a duty of care arises, and in particular, vulnerability as explained by the High Court. The decision has been criticised and a Special Leave application to the High Court will be heard early in 2014. It is too big a topic for this small paper and we can expect the High Court to give a further explanation of what *vulnerability* means in the context of determining whether or not a duty of care arises for economic loss.

18. [2013] VSC 535

19. [2013] VSC 177

20. [2013] VSC 243

21. *Ibid* at [29]

22. [2009] QCA 329

23. [2013] VSC 552

24. [2013] VSC 610

25. [2013] VSC 314

26. Standards Alert, 29 August 2013

27. [2013] NSWCA 317

Penalties

*Andrews & Ors v ANZ Banking Group Limited*²⁸ is outside of the 12 months field of view of this paper, but its significance has yet to become clear. In that decision the High Court rejected the argument that the law of penalties is restricted to the situation of contract breach.

The decision has not been considered in any construction case yet, but one construction author has suggested that the decision might be used to strike down time bar clauses in building contracts. The argument goes that the effect of the time bar is wholly disproportionate to the loss suffered. The issue is raised because it is being pleaded as a defence to a time bar; so it is a watch this space issue.²⁹

Domestic Building Industry Reform Strategy

Third in my watch this space list are the radical reforms proposed in the Domestic Building Industry Reform Strategy mentioned earlier. Under this plan, as the BDPS heard from the Attorney General in September, the *Domestic Building Regulations* will be changed so domestic building insurance becomes a real insurance policy rather than merely a policy of last resort. Claimants will be able to claim directly on their insurance company like they used to be able to do against the HGF. More controversially, the Victorian Building Authority will provide inspectors who, for a fee, will inspect building work and issue Rectification Orders that compel builders to rectify work or direct owners to pay builders. If a Rectification Order is not complied with, it will be able to be enforced against the insurance policy unless challenged in VCAT. An unsuccessful challenge of a Rectification Order will carry with it adverse cost consequences. It will be brave new world and Authority inspectors will become the primary determiners of domestic building disputes.³⁰

Brirek Industries

The final "watch this space" area of law to mention is *Brirek Industries*, an appeal from a County Court decision.³¹ This long running case concerns whether the 10 year limitation period for the bringing of a building action under section 134 of the *Building Act*, which commences from the issue of the occupancy permit, either replaces and extends the 6 year period under the *Limitation of Action Act 1958* (from breach of contract or manifestation of defect in negligence) or just limits that period. The Court of Appeal has now heard the arguments, and as of the time of writing are considering their respective judgments.

I must admit I have some personal interest in this decision. In *Brooking on Building Contracts*, 4th Edition, I expressed my then view on the issue, and that view was later referred to with approval in Judge Shelton's judgment. Then, my co-author of *Brooking*, Michael Whitten, argued *against* that view in the Court of Appeal. No doubt he explained to the court his name on the cover didn't mean he agreed with what I had written.

Further, the case only fell to be determined by the Court of Appeal because of me.

You see, I had mediated the dispute.

28. [2012] HCA 20

29. A Possible End to Time-bar Clauses - Case Note; *Andrews v Australia and New Zealand Banking Group*, Philip Davenport, (2013) 51(2) LSJ 58

30. ACLN July/Aug 2013

31. [2011] VCC 294 Judge Shelton