BUILDERS BEWARE OF EXPANDED RISK AND RIGMAROLE

The New South Wales parliament has introduced a new legislative regime that seeks to regulate the construction industry in an effort to promote public confidence in the construction of apartment buildings following a plethora of defects encountered over recent decades.

The new regime comprises the Design and Building Practitioners Act 2020 (Act) and the Design and Building Practitioners Regulation 2021 (Regulations).

On 11 June 2020 the Act took effect. On 1 July 2021 the Regulations commenced and the operational provisions of the Act came into force.

The purpose of the Act is to impose greater regulation on the building and construction industry in an effort to reduce the prevalence of design and build defects in apartment complexes. The Act adopts a multi-faceted approach in an effort to achieve its purpose and imposes a range of requirements. Most notably the Act:

- Requires design and building practitioners to register and be named on a publically accessible register of practitioners;
- Imposes mandatory insurance obligations;
- Requires designers and builders to submit "compliance declarations" which state whether a design or building work complies with the requirements of the *Building Code of Australia* (BCA); and
- Establishes a statutory duty of care regime.

In this article we seek to address the practical impact of the "compliance declarations" and "duty of care" provisions of the Act.

If you have any queries regarding the provisions of the Act please do not hesitate to contact the authors of this article.

New Regulation of Design and Build

Compliance Declarations

The Act provides that:

- A registered design practitioner must provide a "design compliance declaration" if the practitioner provides a "regulated design"[1] to be used in connection with "building work"[2];
- A registered principal designer must ensure that a design compliance declaration has been submitted and the designer is registered in accordance with the Act[3]; and
- A registered building practitioner must provide a "building compliance declaration" (and other documents) for building work.[4]

Design declarations must be submitted before building work commences. If the design is varied before or after the building work is commenced, design practitioners must submit a further declaration within 1 day of commencing the varied work.

Only registered building and design practitioners can provide these compliance declarations.

Building declarations must be submitted before an application is made for an "occupancy certificate" (OC).

The Act and Regulations prescribe the form and content of three types of compliance declarations:

- **Design compliance declarations –** must include a declaration as to:
  - whether or not a regulated design complies with the requirements of the BCA;
  - whether other standards, codes or requirements have been applied;
  - whether specialist advice has been sought in respect of the designs; and
  - whether or not the design complies with other applicable requirements prescribed by the regulations.
- **Principal compliance declaration –** must include a declaration as to:

1 "Regulated designs" is broadly defined to include any design prepared for "building work" (section 5).

2 "Building Work" is broadly defined to include, amongst other things, work involved in the construction, alteration, repair or renovation of a class 2 building (residential apartments) (Section 4).

3 Section 12, the Act.

4 Section 17, the Act.

> **"The Act adopts a multi-faceted approach in an effort to achieve its purpose and imposes a range of requirements."**

  - whether or not a design compliance declaration has been provided in accordance with the Act for each regulated design;
  - whether the design practitioner is authorised to give the declaration; and
  - any other matters prescribed by the regulations.
- **Building compliance declaration –** must include a declaration as to:
  - whether the building work complies with the requirements of the BCA and any requirements in the regulations;
  - whether the building work is compliant with the Act and if not, the steps required to ensure compliance;
  - whether the building work was carried out in accordance with the regulated designs; and
  - whether a registered design practitioner or a registered principal design practitioner was appointed, and the relevant compliance declarations were obtained.

The "as-built" design documents must also be submitted via the NSW planning portal within 90 days after the OC is issued.

Compliance declarations must be lodged via the "NSW planning portal". The forms can be accessed on the NSW Fair Trading Website.[5]

It is worth emphasising that monetary penalties apply for a breach of the provisions relating to compliance declarations. In some instances (for example, knowingly submitting a false or misleading declaration) a penalty of imprisonment also applies.

The Act and Regulations impose specific and in some instances cumbersome requirements. Care should be taken to ensure strict compliance by practitioners.

Professional Engineering Work

The Act applies to persons carrying out professional engineering work.

Professional engineering work includes the application of engineering principles and data to design and construction related to engineering. Some exceptions apply under the regulations.

Engineers that intend to provide services related to class 2 buildings must be registered in accordance with the Act. Presently the Act applies to civil, mechanical, geotechnical, electrical, fire and structural engineers.

Engineers that intend to issue design compliance declarations must also be registered as a design practitioner.

Specialist Work

The Act also contains a provision for "specialist work". This provision requires that all practitioners providing "specialist work" in relation to apartment complexes must be registered under the Act.

Specialist work applies to work that does not fall within one of the categories described above.

Extended Statutory Duty of Care

Prior to the Act

Previously, the High Court of Australia held that the builder and designer of components of residential strata-titled apartments, did not owe the owners corporation a duty to exercise reasonable care in the construction of the building to avoid causing the owners corporation to suffer economic loss resulting from latent defects in the common property *(Brookfield Multiplex Ltd v Owners Corp Strata Plan 61288* (2014) 254 CLR 185; 88 ALJR 911; *[2014] HCA 36).*

5 https://www.fairtrading.nsw.gov.au/trades-and-businesses/construction-and-trade-essentials/design-and-building-practitioners/forms.

As a result of a number of serious latent structural defects in high-rise strata titled buildings, causing residents of the building to evacuate, the Act was introduced on 3 June 2020 to not only address future latent structural defects in high-rise strata titled buildings, but to also have a retroactive effect.

Duty of Care Imposed by the Act

Section 37(1) of the Act states that "A person who carries out construction work has a duty to exercise reasonable care to avoid economic loss caused by defects:

- in or related to a building for which the work is done, and
- arising from the construction work."

"Construction work" is defined as:

- building work,
- the preparation of regulated designs and other designs for building work,
- the manufacture or supply of a building product used for building work,
- supervising, coordinating, project managing or otherwise having substantive control over the carrying out of any work referred to in paragraph (a), (b) or (c).[6]

Section 37, imposes an obligation on those who know, or ought to have known, of a latent defect in a building that if failed to be rectified, would cause the owner or a future owner economic loss. This risk of liability continues for 10 years after completion of the construction work (which extends beyond the six year limitation period for a breach resulting in major defects pursuant to section 18E of the *Home Building Act 1989)*.

It is important to note that section 37 only applies to construction, alterations, additions and repair of a building of a class or type prescribed by regulations[7] made under the section 4 of the Act.

Economic Loss

An:

- owners corporation is taken to have suffered economic loss:
  - when the owners corporation bears the cost of rectifying defects (including ancillary damage caused by defects) that are the subject of a breach of the duty of care imposed by Part 4 of the Act. However, it is only the cost of reparation of the latent defects that is the subject of the duty of care imposed by Pt 4 of the Act (section 38(1) of the Act);
- individual lot owner is taken to have suffered economic loss:
  - when the defects (including ancillary damage caused by defects), as well as the reparation of the defects, requires individual lot owners to seek alternate accommodation, or otherwise causes economic loss to the lot owner in the form of lost rent, or the loss of potential tenants. However, in calculating each lot owner's economic loss one must consider the owners corporation's economic loss to avoid "double dipping". In most instances, because the owners corporation will seek to recover economic loss for the benefit of individual lot owners, the lot owners will not seek to recover this same economic loss. This may result in one consolidated action as opposed to many actions.

Only economic loss that was foreseeable is recoverable. Generally, this means that if at the time of construction it was reasonably foreseeable (and not too remote) that the breach would cause the loss complained of, it may be argued that the economic loss was foreseeable and therefore recoverable.

Who can sue?

Section 37(2) of the Act provides, "The duty of care is owed to each owner of land in relation to which the construction work is carried out and each subsequent owner".

An owner of land, as defined under section 36 of the Act, can be any of the following:

- every person who jointly or severally or at law or in equity is entitled to the land for an estate of freehold;
- for a lot within a strata scheme, the owner of a lot within the meaning of the Strata Schemes Management Act 2015;
- for a development lot or neighbourhood lot within a community scheme, the proprietor in relation to the lot within the meaning of the Community Land Management Act 1989;
- every person who jointly or severally or at law or in equity is entitled to receive or receives, or if the land is let to a tenant would receive, the rents and profits of the land, whether as beneficial owner, trustee, mortgagee in possession or otherwise; and
- other persons prescribed by the regulations for the purposes of this definition.

Who can be sued?

All persons who carry out construction work owe the duty created by section 37(1) and can be sued. That includes those carrying out building work, preparing designs for building work, manufacturing and supplying building products used for building work and, supervising, coordinating, project managing or otherwise having substantive control over the carrying out of any of that work (section 36 of the Act).

Accordingly, and until we see the Act in action, there is risk that the relevant corporate entity and its employees will owe a separate actionable duty of care.

The Act is Retroactive

Importantly and a key feature of the Act is that section 37 does not only apply to design and construction work undertaken after the commencement of the Act.

It applies equally to construction work undertaken within the 10 years immediately before the commencement of the Act. It is important to note that only the duty of care provision set out in section 37 of the Act is retroactive.[8] This poses a significant risk to those persons described above who, by virtue of

6 Section 36 of the Design and Building Practitioners Act 2020 (NSW).

7 Sections 12 and 13 of the Design and Building Practitioners Regulation 2021 specify the prescribed classes or types of building/ building work that is captured under the Act, as well as certain work that is excluded from being building work (i.e. work that is carried out as exempt development; work that is waterproofing; work that is repair, renovation or protective treatment of a building but only if the work involves a mechanical, plumbing or electrical service etc.).

8 Section 5 of the Design and Building Practitioners Act 2020 (NSW).

the Act, owe a duty of care under the Act but may not have appropriate insurance in place for that period.

Reducing the Risk

Ultimately, you cannot contract out of the duties and obligations imposed by the Act.

Accordingly when defect claims are made, act on them. All time lost prevaricating and refusing to acknowledge the issue will inevitably involve an increased exposure for an economic loss claim, which in some instances might be more significant than the cost of rectifying the defect.

If you have a significant ongoing potential exposure, it is prudent to investigate whether you can obtain insurance against that exposure.

Insurance

Perhaps the most pressing question is: will insurance cover respond to retrospective claims made under the Act?

The answer is, maybe.

Retroactive cover is not uncommon. Many Directors and Officers and Professional Indemnity policies have retroactive dates and respond on a "claims made" basis.

In other words, if a policy was held at the time the works were carried out, a claim made years later will generally be covered. This is subject to the terms and conditions of the policy and whether the circumstances of the claim were known at the time (if so, the claim is likely excluded).

But will this cover automatically apply to claims made under the expanded duty of care?

Coverage will depend on the express wording of the policy, in particular the scope of the insuring, extension and exclusion provisions of a policy. If the insuring provisions are broad, this expanded liability may well be covered. However this will need to be assessed on a claim by claim basis.

But what if an individual or company did not have a suitable insurance policy at the time the works were undertaken?

In theory it is possible to purchase "claims made" cover with a retroactive date. In other words, cover for projects that have already been carried out. However it remains to be seen whether the insurance market will be amenable to such requests in light of the Act.

Alternatively, parties may be able to negotiate an extension of the policies held at the time, with their insurers.

The way in which insurance policies interact with the Act is yet to be seen in action and will ultimately depend on an insurer's response to any such claim. It is possible that adequate insurance cover becomes more difficult and more expensive to obtain noting the expanded duty of care and exposure to risk.

It is recommended that those owing a duty of care have a conversation with their construction insurance broker to determine how they are responding. Although, we expect that insurers and brokers will view this as an opportunity and on that basis, are already moving to get this covered.

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