

Building & Construction Law Update

Summer 2009

A timely reminder for developers

by James Christodoulakis and Andrew Barclay

In the current economic climate, effective risk management of construction projects by developers needs an even sharper focus than usual. One type of risk arises from the possibility of environmental contamination. The Victorian case of *Premier Building and Consulting Pty Ltd –v- Spotless Group Pty Ltd (2007)* is a reminder of the need for intending developers to pay close attention to environmental conditions.

The Facts

Premier was a property developer which purchased an industrial site in Melbourne in 1999. Between 1963 and 1989, Spotless had (through subsidiaries) operated dry cleaning and laundry businesses on land adjacent to the site. Before buying the site, Premier did not get its own certificate or statement of

environmental audit. It relied on a report obtained by the Vendor. The Vendor's report did not detect any contamination on the site.

Moreland City Council rezoned the land as residential in May 2000 with an environmental audit overlay. The overlay required a Certificate or Statement of Environmental Audit to be issued by a registered Environmental Auditor. This did not prevent the Council issuing a planning permit to Premier in 2001 or the issuing of a building permit and commencement of construction.

Premier developed the site into 49 residential units. The units were largely complete in 2002 with most of them sold "off the plan". However, investigations at this time found that the site was in fact contaminated

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with chemicals (white spirit and perchloroethylene) used in the cleaning businesses operated by Spotless on the adjacent property. Remediation of the site was required before the environmental audit could be completed. Until remediation the Council could not issue Certificates of Occupancy.

The consequences of the pollution were disastrous for Premier. The pre-sales were lost and Premier received clean up notices from the EPA. Premier was unable to complete the sales and went into administration. Premier had a right to legal action but (as the court case was to show) it was complicated, expensive and, as always, the outcome uncertain.

The Case

Premier made various claims against Spotless including for statutory compensation under the Victorian Environmental Protection Act 1970 and the Water Act 1989. Premier wanted compensation from Spotless for all its
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A timely reminder for developers

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losses (claimed to be more than \$30 million) – not just the cost of cleaning up the site. Premier also made claims against the vendor's environmental consultants for misleading and deceptive conduct, planning consultants for failure to provide proper advice, the council which had re-zoned the land and granted the planning permits and the owners of the Spotless land.

Although the Supreme Court was satisfied that Spotless contaminated the site, it did not award damages for most of Premier's losses. Of all the claims made by Premier, it was only successful under section 62A of the EPA which allowed recovery by Premier of remediation costs. The amount awarded by the Court to Premier for the clean-up was only about \$4 million.

What it means

There are many and varied considerations that need to be given to a construction project by developers. Environmental factors in particular must be properly investigated. Where industrial or mixed use land is involved, a certificate or statement of environmental audit should be obtained. An environmental report should only be sought from reputable specialist consultants - preferably, an EPA accredited environmental auditor.

If there is any doubt, legal advice about appropriate contract conditions should be obtained. When they are in a contract they need to be followed. In *Premier –v– Spotless*, Premier agreed to waive a requirement in the contract that the vendor obtain a certificate of environmental audit. The waiver was in return for a discount off the purchase price. This decision proved to be extremely costly.

The lesson for developers is to make sure that EPA requirements are understood and adhered to before making a binding contract or incurring large costs. Those costs and other losses may not be recoverable if the land falls short of the standards set by the EPA.

Thank you to Kate Jenkins for her contribution.

Industry Alerts

National interest

Looking for energy efficient buildings?

Both investors and tenants seeking commercial energy efficient premises stand to benefit from a scheme proposed by Federal Environment Minister Peter Garrett. Under the scheme it will be mandatory to obtain an energy efficiency rating and advisory report and disclose this document on the transfer or lease of commercial office space with an area of 2000 square metres or more. The Federal Government is consulting with the States and Territories to develop a national framework for the scheme. (18/12/08)

Support for the industry on climate change

The Australian Building Codes Board will benefit from a Federal Government allocation of \$161,000 to assist the industry in adapting to codes and products that counteract the effects of climate change. (6/11/08)

Construction downturn should turn around in early 2009

The Australian Industry Group – Housing Industry Association Performance of Construction Index reported the second steepest fall in construction activity during the month of November since the survey began in September 2005. BIS Shrapnel and others forecast a rise in residential activity in early 2009 as a result of the Federal Government's First Home Owner Boost Scheme which is forecasted to lead to the rise in demand for newly built detached housing. This will in turn ease pressures on rent payments. (5/12/08)

Master Builders response to decline

The Association has called for more action from the government after reporting a slump in dwelling unit approvals of 34.7% and housing of 27% in November 2008 compared to November 2007. (9/11/09)

Federal support for local government projects

The Federal Government has allocated \$300 million through the Regional and Local Government Infrastructure Program to assist in the economic development of communities across the nation. (18/11/08)

Review of 457 visas following claims of exploitation of migrant workers

Following publicity concerning the exploitation of skilled migrant workers the Federal Government's sponsored review recommends a major overhaul of the 457 Visa scheme. Recommendations include abolishing the minimum salary levels in favour of market rates for those on salaries of less than \$100,000. The Government is committed to the effective operation of the scheme and will take steps to ensure that labour shortages are addressed whilst protecting opportunities for Australians and the rights and entitlements of overseas workers. (14/11/08)

(source Thomson Reuters)

Poor documentation leads to a builder not being paid for work done

by Tony Mylne

The High Court case of *Lumbers –v– Cook Builders Pty Ltd (in liquidation) [2008] HCA27* resulted in an owner paying substantially less for a home than it cost to build.

Facts

In 1993, builders W Cook & Sons Pty Ltd (“Sons”) entered into a “cost plus” agreement with the owner of a block of land (the Lumbers) to construct a house at Northaven, near Adelaide. The Lumbers had a close relationship with a director of Sons (McAdam) and, although the house eventually cost more than \$1 million to build, the oral contract was made in a very informal way – “constituted by conversations” between McAdam and the Lumbers. However, it was never disputed that a contract between Sons and the Lumbers did exist.

Some time after the work commenced in about January 1994, Sons now did just joinery and carpentry and another entity, W Cook Builders Pty Ltd (“Builders”), was to be the builder. The reorganisation was just as informal as the contract with the Lumbers, but as far as the business managers were concerned the responsibility for building the house now lay with Builders. Unfortunately, nobody told the Lumbers. They still dealt with McAdam and the same people turned up to do the work. McAdam asked the

Lumbers for progress payments which were always made by cheque payable to Sons. Despite the “reorganisation”, externally nothing appeared to have changed. The house was completed in about May 1995.

In 1998 Builders went into liquidation and in 1999 the liquidators demanded payment of \$274,791 from the Lumbers as the difference between the costs incurred in doing the work and the amount paid by the Lumbers plus a 10% “supervision fee”.

Decision

Builders sued both the Lumbers and Sons. However, Builders failed to comply with an order to provide security for Sons’ costs and the proceeding against Sons was stopped. For that reason the main issue in the case was whether Builders was able to recover its entitlement (found by the Court to be \$261,715) directly from the Lumbers. The ordinary position is that a sub-contractor has no claim against the building owner. However, Builders argued that Sons had “assigned” to Builders all its rights under its contract with the Lumbers. As an alternative argument, Builders said it had a claim for “unjust enrichment” against the Lumbers because they had received a house without paying its full value. The trial judge found against Builders on both arguments. On appeal, the Full Court of the Supreme Court of South Australia (by a majority of 2 to 1) allowed the unjust enrichment claim. The High Court unanimously reinstated the original decision. Builders could not recover directly from the Lumbers.

What it means

The circumstances of the case (not all of which can be described in this short note) were unusual and the “lopsided” nature of the proceeding (Sons did not participate) and various gaps in the evidence (McAdam was not a witness)

give the impression that information possibly relevant to the outcome may have been missing. However, there are still some useful points coming from this decision:

- The undisputed existence of the original contract between the Lumbers and Sons was fatal to the unjust enrichment claim. The building contract’s high level of informality did not undermine its influence over the outcome in this case. The real barrier to Builders’ success was the informality of the business restructure. Even a letter to the Lumbers advising them that the building contract had been taken over by Builders could have made a difference to its position.
- Courts have a conservative approach to creating new rights in the context of commercial dealings. There is no substitute for properly documenting the contractual arrangements under which business is to be carried out.
- The Lumbers did not know that Builders was doing anything for them. They thought it was Sons. Builders argued that this didn’t matter because “confusion about which company in a group of companies is party to a contract is a common occurrence in modern corporate life”. It is true that many businesses are made up of groups of companies under a corporate “mother-ship” and individuals within the business may at different times be acting (or at least appear to be acting) for different legal entities. This did not change the outcome in this case, but in other circumstances it may be a critical factor particularly if an agreement has not been properly documented.

Generally this case illustrates what can happen when business dealings are not adequately committed to writing.



The importance of complying with extension of time procedures

by Guy Abel

This is a review of *Hervey Bay (JV) Pty Ltd –v– Civil Mining & Construction Pty Ltd & Ors (14 April 2008)* (Supreme Court of Queensland) which shows that entitlement to an extension may be lost if a contractor fails to comply with the procedures and time limits in the contract.

Background

Contractors are familiar with the importance of complying with procedures and time limits in order to gain an extension to the time for Practical Completion. Such procedures and time limits can be very specific – and very tough. Even the commonly used Australian Standards contracts (AS2124-1992 and its successor AS4000-1997) impose time limits and require the Superintendent to determine whether the contractor is “entitled” to an extension of time. But the standards also give the Superintendent a general discretion to grant an extension of time. AS2124-1992 says:

... notwithstanding that the Contractor is not entitled to an extension of time the Superintendent may at any time and from time to time before the issue of the Final Certificate by notice in writing to the Contractor extend the time for Practical Completion for any reason...

What is the effect of this discretion? In the well known case of *Peninsula Balmain –v– Abi Group Contractors Pty Ltd (2002)*, Abi Group wanted an extension of time. It was not allowed, a dispute arose and a referee was appointed. In his report the referee said that the relevant part of the contract (quoted above) gave the Superintendent complete discretion to grant an extension of time to a Contractor, so that the Superintendent was free to either allow or not allow any extension.



The Supreme Court of New South Wales agreed with the referee. However, the Court of Appeal said that the Superintendent was “... obliged to act honestly and impartially in deciding whether to exercise this power....” and in the circumstances of that case a Superintendent acting honestly and impartially would have given the extension. The Superintendent was therefore under an obligation to grant the extension of time.

The Hervey Bay Case

The more recent case of Hervey Bay also concerned AS2124-1992. However, as is often the case, important changes had been made to the relevant parts of the standard form. The part of the contract quoted above now had added on to the end the words;

“...in the Superintendent’s absolute discretion and without being under any obligation to do so.”

But there was more. A new provision said that:

“the Contractor shall not be entitled to an extension of time to the Date for Practical Completion or any other

Claim unless it has ... complied strictly with clause 35.5 (including without limitation) given all the notices required by clause 35.5 in the forms and within the time periods specified in clause 35.5.”

And another which said:

“...the Principal and Superintendent may exercise those discretions and rights given to them under the Contract in whatever way the Principal or Superintendent decide in their absolute discretion...”

The Contractor had claimed \$821,439 for extra costs due to delay. The right to get delay costs depended upon an extension of time for Practical Completion, but the Contractor had not given the notices required by the contract and did not have an extension of time. Following the Peninsula Balmain case, the adjudicator said that delay costs were payable because an honest and fair Superintendent would have exercised his general discretion to allow an extension of time. The adjudicator allowed most (\$767,700) of the amount claimed.

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The importance of complying with extension of time procedures confirmed

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But the Supreme Court of Queensland said this case was different because of the particular amendments to AS2124-1992 (which appeared to have been made with the Peninsula Balmain case in mind). The Court said that the express exclusion of an "entitlement" to an extension of time unless the contract procedures had been followed and the conferring of an "absolute discretion" on the Superintendent were inconsistent with the Contractor's arguments.

What it means

- It is not in a Contractor's interest to have in the contract provisions like those in the Hervey Bay case (just as it is in a Principal's interest for those provisions to be included). However if such provisions are included in the form of contract proposed by the Principal in the first place, the Contractor is unlikely to be successful in negotiating to have them removed. This reinforces the importance of having systems and training that focus on complying with procedures and time limits in an ongoing contract.
- Even if your contract is based on AS2124-1992 or AS4000-1997 amendments can open up the Superintendent's discretion – so that Peninsula Balmain does not apply.
- Despite best intentions, there will always be cases where contractual procedures and time limits for an extension of time will not be followed. If your contract is an Australian Standard form with amendments that are the same or similar to those in Hervey Bay, it seems likely that the Superintendent would be justified in taking the approach in that decision. However, in any particular case advice on the specific terms of the contract should be sought.

Setting out all the reasons in a payment schedule is necessary

by Chris Thompson and Andrew Barclay

A review of *Perform (NSW) Pty Ltd –v– Mev-Aus Pty Ltd t/as Novatec Construction Systems (19 August 2008) NSW Supreme Court*. Under the New South Wales *Building and Construction Industry Security of Payment Act 1999* can a respondent's payment schedule incorporate, by reference only, the reasons that were set out in an earlier payment schedule?

Facts

Formwork subcontractor Novatec Construction Systems issued a payment claim under the Act for work carried out at the Sydney Airport Car Park. Perform (NSW) Pty Ltd served its payment schedule giving reasons for valuing the payment claim at zero. Perform sought to incorporate within the payment schedule, by reference only, reasons contained in a payment schedule that Perform had served on Novatec two weeks earlier. The earlier payment schedule was not physically attached to the new payment schedule. In the resulting adjudication, Novatec's submissions did not deal with the issues raised by Perform in the earlier payment schedule.

Whether a respondent should be allowed to include in the payment schedule by reference only, reasons that are in another document is important because of section 20(2B) of the Act, which only allows the Respondent to include in its defence (the "adjudication response") reasons for withholding payment if "those reasons have already been included in the payment schedule provided to the claimant." If incorporation by reference is not allowed, the adjudicator cannot consider the reasons in the earlier payment schedule, even though they were part of the adjudication response.

The adjudicator decided that the Act does not allow the incorporation by reference materials that are not part of the payment schedule.

Decision

Perform took the matter to the Supreme Court. Perform argued that the adjudicator was wrong to ignore the reasons set out in the earlier payment schedule. However, the Court agreed with the adjudicator. The judge said that the Act requires reasons to be stated in the payment schedule with "some particularity". This is important to the "fast track" scheme of the legislation. The judge said that to allow inclusion by reference only "all manner of previous documents claimed to have passed between the parties", could lead to "mayhem" where time is of the essence to the critical steps to be taken by the parties under the Act.

It might be argued that prohibiting incorporation by reference would be unfair because it meant that Perform could not put its arguments to the adjudicator. However, the judge said that section 20(2B) of the Act underlined the importance of "setting out" reasons in the payment schedule.

Comment

The position in Victoria is quite different. In Victoria, unlike under section 20(2B), an adjudication response may include new reasons in which case the claimant must be given an opportunity to respond to them. This means that whether incorporation by reference is allowed in Victoria is hardly likely to matter because material left out of the payment schedule can be included in the adjudication response. The position in Queensland is the same as New South Wales.

Industry Alerts

New South Wales – new consumer protection measures for home builders

On 12 November 2008 the New South Wales Legislative Council passed changes to the Home Warranty Insurance Scheme giving more protection to consumers. The changes included increasing the cover from \$200,000 to \$300,000; speeding up processes for claims made where the builder has disappeared; and suspending the licenses of builders who fail to comply with a monetary order of a court within 28 days. (12/11/08)

Queensland – \$17 billion in capital works to proceed

The Queensland Treasurer has announced that the government will deliver in full its planned capital works program. As an estimated 119,000 workers will be engaged in projects such as the Gateway Bridge Duplication, the Eastern Busway, the Gold Coast Hospital and the Abbot

Point Coal Terminal the Treasurer stated that the Government is attempting to ease any effects of the economic downturn. (9/12/08)

Victoria – the Victorian government spends big on transport

The Victorian Government will exceed the recommendations of the Eddington Report on the State's future transport needs by spending \$38 billion. Priorities will be the \$6 billion road project linking freeways in north and east Melbourne and the acquisition of 72 trains and 53 trams. Upgrades to Avalon Airport, the \$80 million Dingley Bypass and extension of several rail services also feature in the spending plan. (8/12/08)

South Australia – Regulation for architects

The Architectural Practice Bill is the South Australian Government's first review of the legislation governing the profession since 1939. Proposed reforms include expanding the role of the Architects

Board by increasing the Board's membership and giving it the power to deal with misconduct by architects. The Bill also removes ownership restrictions on firms and companies, limits on remuneration and restrictions on advertising. (27/11/08)

(source Thomson Reuters)



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