KR Hewlett & Co's
PROPERTY LAW NEWS and VIEWS –May 2011

Purchaser's relief in an off-the-plan

purchase: In a recent case regarding an off-the-plan purchase, the purchaser was successful in the litigation. The purchaser's solicitor ensured clauses were included in the contract confirming that the vendor would build the townhouse in question in a proper and workmanlike manner, in accordance with the terms and specifications approved by Council and that defects apparent and notified within 90 days of completion would be rectified by the vendor.

Departure from the plans: In construction of the townhouse, there had been departure by or on behalf of the vendor from the Council approved plans. The Judgment indicates that the toilet and laundry were in one room, rather than two, there was a smaller area for the kitchen bench, an exterior door was omitted and also designated trees were not provided.

The judge considered that these changes from the Council approved plans were substantial, rather than being merely nominal, and that that substantial departure from the plans entitled the purchaser to terminate the contract and to have their deposit returned.

The judge indicated, however, that the result may have been different if the vendor had sought an order from the court asking that the contract be performed (called specific performance). If specific performance had been sought, the judge indicates that the decision may have been to require the purchaser to complete, with the vendor giving some compensation to the purchaser.

Case lesson: The judicial interpretation in that case of "substantial" departure from the Council terms and specifications gave the purchaser a powerful right, and resulted in the purchaser succeeding. Purchasers and vendors in off-the-plan transactions, take note.

Another off-the-plan purchase dispute – a different result – the Wall:

An off the plan unit purchase for over $750,000. At the time of purchase, construction of the home unit complex of which the unit was to form part was yet to commence.

In that case, the contract allowed the purchaser to rescind if there was a *difference* between the draft strata plan in the contract and the final strata plan that detrimentally affected the property to an extent that was substantial.

The purchaser in the case claimed to pull out of the contract on a claimed such difference, arguing that a wall had been constructed that substantially obscured views from the property.

While the unit had 180 degree views to the north from the upper floor, as expected, those views had been obscured on the lower floor of the unit in question due to the presence of the wall.

To make matters worse the purchaser had been shown a scale model of the unit which did not show the wall. The purchaser did not, however, legally contract to purchase a unit that was substantially identical to the model examined (which the judge indicated the purchaser could have done if they were relying heavily on that model). The title strata plan (as strata plans do) did subtly show the presence of a wall, but only where its base would be, not any of its features such as height.

The court ruled that the purchaser did not have a legitimate right to rescind. The result could have been different if the contract referred to the model the purchaser relied upon.

Vendor Damages: The vendor claimed damages for the purchaser's breach of contract. The vendor substantially failed in its claim as it did not give the court evidence of the unit's value at the time of the court case. This was important as, if the value of the unit had dropped compared to the contract selling price, the drop (including incidental costs of any resale) would be a measure of damages.

The vendor tried to claim the additional interest paid on its loans as the mortgage was not discharged at the time of sale. This claim failed, it seems because the court found that those costs arose from the vendor's own decisions after the sale failed – such as the decision to keep the property and rent it out rather than immediately resell it.

In this case, the damages that the vendor was entitled to was considered to be negligible. As the vendor had held onto the property after the failed sale, they had gained over $50,000 in rent income while paying about $20,000 in strata levies, council rates and water rates. Accordingly, their damages were assessed to be Nil.

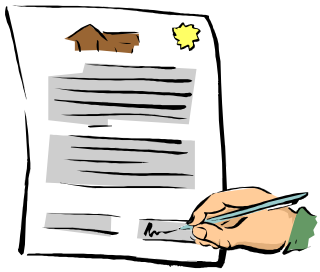
Refund of deposit: The court then considered the purchaser's rights again. It found that there was a promised represented availability, by the model (and an estate agent's comments), of 180 degree views, that the promise was a significant factor in the purchaser's decision to buy that particular unit for that particular price and that the building of a wall to in part obstructed 180 degree water views from the bottom storey of the unit was contrary to that representation.

The court therefore used its discretion to order return of the full deposit to the purchaser (less damages suffered by the vendor - but in this case those damages found to be nil).

Costs: Also, please take note. The court later ordered that the vendor pay just one sixth of the purchaser's costs. The court pointed out that both parties had lost their respective cases, except that the purchaser had succeeded on the return of deposit point. That point did not take up much time in evidence compared to other issues, and hence the purchaser was just awarded a small part of their costs.

Lessons: This case demonstrates a few important lessons. One hard lesson is that a purchaser, when a problem such as this obstructing wall occurs, should normally have their solicitor obtain Counsel's urgent advice before taking steps to terminate (or go ahead with) their contract following the discovery of the problem (no matter how upset the purchaser may then feel)..

UNFAIR CONTRACT TERMS



From 1 July 2010, new laws relating to unfair contract terms took effect. Those new laws, applying consistently Australia wide, will likely have significant benefits over time.

Background: Parliaments around Australia were concerned about unfair contract terms in "standard form contracts". Before the new laws were brought in, a Productivity Commission report that considered the matter indicated (from the Explanatory memorandum to the legislative Bill):-

> The PC (Productivity Commission) estimated that the implementation of a national consumer law could result in benefits to Australian consumers of between $1.5 billion and $4.5 billion a year.
>
> The PC assumed a 5 per cent reduction in detriment, stemming from its policy reform package, resulting in substantial gains.

In the Parliamentary second reading speeches about the legislation it was noted that "…similar laws … have been in place in Victoria since 2003. And laws tackling unfair contract terms exist in the United Kingdom, in the rest of the European Union, in Japan and in South Africa. Laws which allow for the examination of the fairness of contracts and contract terms also exist in jurisdictions in Canada and the United States."

The new laws: Are part of the Australian Consumer Law. The full Consumer Law is now contained in a Schedule of the Competition and Consumer Act (the new name for the Trade Practices Act).

When the new laws apply: As a general statement, the unfair contract terms law will apply to business to consumer transactions. In those transactions, the new law states that a term in a consumer contract is void (ie is basically of no effect) if the term is unfair and the contract is a standard form contract.

Importantly, a "consumer contract" includes not only a supply of goods or services, but also a sale or grant of an interest in land (ie property). Many contracts for sale of land or leases could be caught by the legislation.

To be a “consumer contract” however, also, the supply must be to an individual whose acquisition of the goods, services or interest is wholly or predominantly for personal, domestic or household use or consumption.

Therefore, while a contract for purchase of a principal place of residence property from a developer may be affected by the legislation, a contract for purchase of an investment property is unlikely to be affected. The purpose of the purchaser in question is important.

Standard form contracts: Of course, the legislation just applies to “standard form contracts”. There is a list, in the legislation, of factors that indicate there could be a standard form contract.

Very importantly, there is a “reversal of onus”. A consumer just has to allege that the contract is a standard form contract, then the onus will be on the supplier to prove that the contract is not a standard form contract. Suppliers may find that difficult.

Meaning of “unfair”: The legislation states that a term of a consumer contract is unfair if:

(a) *it would cause a “significant imbalance”* in the parties' rights and obligations arising under the contract; *and*

(b) *is “not reasonably necessary”* in order to protect the legitimate interests of the party who would be advantaged by the term; *and*

(c) *would cause “detriment”* (whether financial or otherwise) to a party if it were to be applied or relied on.

In relation to “*significant*” referred to in (a), this is likely in our view to be interpreted generously in favour of the consumer by the courts, although this is not yet certain.

In relation to “*not reasonably necessary*”, very importantly, the new laws again indicate that if a consumer alleges the term was not reasonably necessary, the onus again reverses onto the supplier to show that is incorrect. This may be difficult for the supplier.

Regarding “*detriment*” in (c) above, in her Second Reading Speech of 26 October 2009, Senator Penny Wong said:

‘In the context of the provisions, detriment includes both financial and non-financial detriment. ..in some cases...where a business abuses the terms of a contract by behaving unreasonably, causing irritation, inconvenience and distress to a customer, then this can — and should —be taken into account.”

Other factors to be taken into account: In determining whether a term of a consumer contract is unfair, a court may take into account such matters as it thinks relevant, but must take into account the extent to which the term is “transparent” and the contract as a whole.

“Transparent” is defined in the legislation to mean all of being expressed in reasonably plain language, legible, presented clearly and being readily available to any party affected by the term.

The ACCC draft guide about the new laws, in relation to “transparent” says –

“..the finding of Smith J in Office of Fair Trading v Abbey National plc21 may provide some guidance: “Regulation 6(2)…requires not only the actual wording of individual clauses or conditions be comprehensible to consumers, but that the typical consumer can understand how the term affects the rights and obligations that he and the seller or supplier have under the contract.””

Some examples of possibly unfair terms: The legislation indicates several types of terms that may be considered unfair including:-

- a term that permits, or has the effect of permitting, one party (but not another party) to terminate the contract;

- a term that permits, or has the effect of permitting, one party (but not another party) to vary the terms of the contract;

- a term that permits, or has the effect of permitting, one party unilaterally to determine whether the contract has been breached or to interpret its meaning;

- a term that limits, or has the effect of limiting, one party's right to sue another party;

A general comment: The ACCC draft guide notes that an apparently unfair term may be regarded in a better light when seen in the context of other counter-balancing terms. However, in Director of Consumer Affairs Victoria v AAPT22, Morris J said that even if a contract contains terms that favour the consumer, such favourable terms may not counterbalance an unfair term if the consumer is unaware of them. Examples include implied terms, or terms that are hidden in fine print, in a schedule or in another document, or are written in legalese. This may result in an information imbalance in favour of the supplier.

Exclusions to the new laws: As would be expected, contract terms that just define the subject matter of the contract or set (as a general statement) the main price of the good or service cannot be unfair under the legislation. So, if you just pay too much for a good or service, you could not normally use the legislation to complain about that.

Conclusion: This is a powerful new law that will affect many different contracts including mobile telephone, transportation and property sale contracts. It is hoped that it will lead to fairer standard form contracts. If a standard form contract affected by the legislation is unfair, consumers and regulators such as the ACCC will have powerful rights. The legislation in future might be extended to cover at least some business to business transactions. In her Second Reading Speech, Senator Wong said:-

> "There is a view that if something is disclosed then it is all right —no matter how unclearly or obscurely that information is presented. This reflects the view – put about by some – that all standard-form contracts reflect a 'bargain' reached by the parties, which is well understood by them and should not be subject to any scrutiny or challenge once a signature is on the page.
>
> In complex markets, with ever-increasing rates of innovation and change, the notion that a customer is always perfectly informed and able to act in his or her own best interests represents a view which is simply not sustainable, and does not reflect the reality of modern business or contract law…"

The current ACCC unfair contracts terms guide can be downloaded at the webpage address
http://www.accc.gov.au/content/index.phtml/itemId/937060

Strata Legislation Reform

You will recall that our last property newsletter reported that there were several important changes made to NSW strata and related legislation. We firstly report further briefly about those changes.

Several of the changes related to the powers of "developers" during the "initial period" of a strata scheme.

The "initial period" is the period before one third of the unit entitlements of the unit development are sold (and sales settled) by the developer. The first annual general meeting of the strata is held at the end of the initial period. Until that first annual general meeting, the developer would normally make any Owners Corporation decisions necessary (such as to take out strata common property and public liability insurance).

Pursuant to the changed laws, during that initial period - in regard to parking - by laws authorising an owner to park a vehicle on common property now cannot be made. The intention is that this will prevent developers making by-laws that grant unreasonable parking rights over common property during the initial period.

Caretakers: Changes were made relating to caretakers. A concern was that people were doing the work of caretakers, but not being called caretakers, perhaps so as to avoid having to comply with the legal obligations on caretakers under the strata legislation.

The legislation now states that "…a person is taken to be a caretaker for a strata scheme if the person meets the description of a caretaker set out…, regardless of whether the title given to the person's position is caretaker, building manager, resident manager or any other title."

Proxies: Another concern was that contracts for sale in new unit complexes sometimes required a purchaser to give a "proxy" to the developer in owners corporation voting. The new laws indicate that any such clause in a contract for sale or ancillary arrangement is now unenforceable.

Voting: Also, the new laws make clear that the original owner, or a person "connected" with the original owner, may not cast a vote at a strata general meeting pursuant to a proxy in a sale contract or ancillary arrangement. While there may be ways developers may try to have purchasers to vote in

accordance with the developer's wishes, it is no longer likely to be a general proxy, but relate to pre-disclosed specific issues.

Since these new laws came in, we have seen at least one contract where there seemed to be very brief disclosure of many issues, then an attempt made to effectively require purchasers to vote in accordance with the developer's wishes in relation to all those issues. Whether this type of arrangement will be enforceable, if it is challenged, remains to be seen.

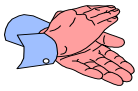
Executive Committee: Further, under the reforms, a person who is "connected" with the original owner or caretaker of the strata scheme is not eligible to be elected as a member of an executive committee for the scheme unless that person discloses their connection with the original owner or caretaker at the relevant meeting and before the election is held.

Of course, this will mean that it will be very important for owners to listen carefully for such disclosures at any meeting where executive committee members are being elected.

If, after being elected, a person on the executive committee becomes connected to the original owner or caretaker, they must properly disclose the connection as soon as possible. In addition, the owner corporation may by special resolution vacate the office of that executive committee member. In any vote about any such vacation, the number of votes of the original owner may be limited.

Developer duties: A recent court decision has made it clearer that a developer/promoter of a strata scheme owes a fiduciary (special) duty to subsequent owners in a strata or community scheme.

In the recent decision, it appears that the developer/promoter was paid (what the court described as) a premium, of about $190,000, by a company, to secure management rights in the future for the owners corporation. This was agreed to before the first annual general meeting of the owners corporation.



The court held that the developer/promoter had breached fiduciary duties not to place itself in a position of conflict or to profit from contracts entered into between the Community Association and the management company, without proper disclosure and also not to act to the detriment of the association.

The case is an important precedent. Where a breach of fiduciary duty can be established, there are often powerful legal remedies.

Termination of long term strata contracts: Finally, in this topic, it is noted that an Owners Corporation who wishes to terminate an unfortunate long term management or caretaker agreement before its end may only be able to do so if there are proper legal grounds and the termination is carried out in a proper manner. Court decisions confirm our view that it can be done, but it should be done very carefully, and only after obtaining good legal advice early in the process.

STRATA TITLE IN THE COURTS

Maintenance and Repair: Of interest are decisions coming through in recent years relating to the Owners Corporation's obligation to "maintain and repair" common property pursuant to section 62 of the relevant laws. Section 62 of the Strata Schemes Management Act 1996 (NSW) provides:-

"(1) An owners corporation must properly maintain and keep in a state of good and serviceable repair the common property and any personal property vested in the owners corporation."

In a recent Supreme Court case, Acting Justice Bryson states:-

"It is well established…. that s 62 creates the duty owed to each lot owner, breach of which gives rise to a private cause of action for damages for breach of statutory duty… A duty of that kind is also enforceable, in an appropriate case, by a mandatory injunction requiring compliance with s 62…. A mandatory injunction is not granted as of course…"

Damages: Individual lot owners may be able to more readily claim damages suffered, such as loss of rent, where it is established that the loss is caused by the Owners Corporation's failure to comply with their section 62 obligation to maintain and repair.

In 2 cases, individual lot owners were able to obtain judgements for damages of about $234,000 and $55,000 respectively against their owners corporations.

Recent case law seems to be indicating that the maintenance and repair obligation of an owners corporations is a strict one. This means that where the obligation is established, and where the Owners Corporation have been unable to carry out the maintenance or repair even though they have taken reasonable steps to do some work, the Owners Corporation may still be held liable.

For example, Justice Ward stated in a different recent case that:-

> ".. the fact that the Owners Corporation may have taken reasonable steps to effect those works (but has been incapable for whatever reason of so doing) does not mean that there is no breach of the statutory duty."

Examples: In one of the recent cases, construction of the unit complex in question was completed probably in 2001, there were problems almost immediately and the subsequent victim purchased the problem unit in 2002, apparently not aware of concerns. The purchaser victim moved in immediately after purchase, but had to move out late 2004 due to the severe water leak problems. A tenant was put in, but rent had to be reduced and the tenant later moved out too. In the meantime, the owner presumably had to make their mortgage repayments. The unit was uninhabitable and empty for more than 3 years, up to early 2010, when the court case was decided. A valuer estimated that the water leak problems had reduced the value of the unit from $810,000 to $130,000.

As well as awarding damages of over $250,000, the court required by injunction order that rectification works be completed within 9 months.

In another case, it was noted that it took over 7 years from the time of initial complaint by an owner, of water penetration problems, before the problem was finally fixed by contractors engaged by the owners corporation. Damages of about $55,000 were awarded, including loss of rent of $40,000.

Pre purchase reports: The cases also show how important it is to obtain both a strata owners corporation records search, and also a builder's report, when purchasing a unit. Clients of ours have incorrectly been advised by others, on many occasions, that one or both of these reports do not need to be obtained when purchasing a strata unit. Even if the unit is new, both reports should be obtained, as shown by the first case example above.

Conclusions: For individual lot owners whose Owners Corporation are not inclined to rectify a common property defect that affects their lot, the case law confirmation of strong rights of common property maintenance or repair of such lot owners will be welcome. For Owners Corporations in general, such cases will legally mean that it will be more important than ever to ensure that reasonable sinking fund plans are not only put in place, but also followed. Of course, in so doing, this may lead to increases in strata levies.

With best regards to all, and I hope I'll see you soon somewhere….

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