BUDDLE FINDLAY

All for one and one for all - the undisclosed body corporate 'underwrite'

Myles O'Brien

6 July 2021

For many first home buyers, purchasing a dwelling in a 'unit title' development may be the only realistic option to achieve that first rung on the housing ladder. But ownership of these sorts of dwellings requires a careful understanding of what it is you are buying into; it is more than just 'bricks and mortar'.

Unlike purchasing a standalone fee simple or cross lease property, a purchaser of a unit title also automatically becomes a member of the body corporate comprising the owners of each unit in that unit title development. This is essentially a small democracy that governs the operation and maintenance of the unit title dwellings and surrounds, and subject to the state of the building and the financial position of the other members of the body corporate, becoming a member of this democracy can have far reaching and unanticipated, financial consequences. This is not in and of itself problematic – but as with most things, having a clear understanding of the issues associated with unit title ownership will ensure a much happier investment outcome.

The 'leaky building' building issue is not new, and many body corporates are still grappling with it. Building industry experts have pointed out that it is not just a 'leaky building' crisis, but is better described as a 'defective building' crisis with structural issues, passive and active fire systems issues and now, earthquake strengthening issues for body corporates to resolve. Identifying the relevant building defects is one substantial challenge for a body corporate committee and then, once identified, putting in place the funding to complete the remedial works is another. Remediation levies can, on an individual owner basis, run into the hundreds of thousands of dollars.

Unless there has been a finally binding settlement with liable third parties which wholly covers the cost of any remediation, putting the funding in place to complete remedial works largely relies on each member of the body corporate being able to fund their share of the levy raised for the remedial works; this so that the body corporate has sufficient funds available to it in order to enable it to complete the whole job. Importantly, to the extent that any members of the body corporate are not able to fund their levy for the project to proceed, the requirement to fund the levy falls on those members of the body corporate who can. Only remediating those units of those owners who can afford to pay the remediation levy is almost never a viable option, especially where the building is an apartment block.

These considerations are not likely to be 'front of mind' for purchasers of property in unit title developments unless the building is already undergoing remediation. But as the cost of funding falls on those owners who can pay, these owners in effect 'underwrite' or assume the risk of financing those owners who cannot pay. Your traditional 'underwriter' or 'guarantor' is' usually aware of the risk they are assuming, however in these building remediation projects there is no guarantee to disclose and the risk is not appreciated until there is a remediation project and owners with unpaid levies.

Judicial comment has recognised this risk; "persons who purchase unit title properties and so become participants in bodies corporate must be taken to have assumed the risk that, from time to time, some owners will default in the payment of levies. The cost of funding the body corporate then falls on those proprietors who do pay levies." *Body Corporate 198072 v Bank of New Zealand [2011] 3 NZLR 249 at 42*.

Much like a guarantor who often has limited information about the debtor they are guaranteeing, an individual within a body corporate will have no realistic ability to obtain financial information about the other members of the body corporate they are joining. Accepting the risk of funding the usual operational levies of owners who cannot pay is one thing; but assuming the risk of a remediation levy of hundreds of thousands of dollars is an entirely different thing altogether.

So, any person looking to acquire a dwelling in a 'unit title development' should beware of the additional complexities of buying into an existing body corporate in particular, one of which could be underwriting your neighbours if the building does require remediation. Unfortunately, as the homeowners involved in the 'James Hardie' litigation now know, it can be very hard for a buyer to pick a defective building but scrutiny of the Body Corporate minutes to identify building condition issues and taking advice from a qualified building professional about the condition of the building will go a long way to assisting with any investment decision.

These issues are well known and there is a current legislative proposal to try to start fixing some of the issues we have identified. The Unit Titles (Strengthening Body Corporate Governance and Other Matters) Amendment Bill is currently in Select Committee. It seeks to fix a number of issues in the Act including what sort of information purchasers receive when they agree to buy a unit. It

also seeks to ensure that most body corporates must have long-term maintenance plans that address all defects in a building.

The disclosure requirements are proposed to be bolstered by requiring better information including:

- Financial statements and audits for the previous seven years
- Notices and minutes of AGM's for the last three years
- Amounts held in credit for long-term maintenance plans.

The long-term maintenance plan regime would be bolstered by requiring them to be peer reviewed by building surveyors, engineers, or other relevant professionals, if such plans are not required to be prepared by these professionals in the first instance.

These are worthy changes to make to the Act to ensure purchasers understand as much as possible about the true state of any unit and the development as a whole.

Auckland

188 Quay Street
Auckland 1010

PO Box 1433
Auckland 1140
New Zealand

P: +64 9 358 2555
F: +64 9 358 2055

Wellington

Aon Centre
1 Willis Street
Wellington 6011

PO Box 2694
Wellington 6140
New Zealand

P: +64 4 499 4242
F: +64 4 499 4141

Christchurch

83 Victoria Street
Christchurch 8013

PO Box 322
Christchurch 8140
New Zealand

P: +64 3 379 1747
F: +64 3 379 5659