

Legal alert - Property and Construction Strengthening consumer protection measures in the Building Act

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Building and Construction Minister Dr Nick Smith announced yesterday that, from 1 January 2015, building contractors will be required to have written contracts, provide information on their relevant skills, experience and qualifications, and disclose their insurance and warranty cover for residential building work valued at over \$30,000.

These new requirements are part of the wider consumer protection measures introduced in November last year by the Building Amendment Act 2013 (the Act), which will also come into force on 1 January 2015, and which strengthen the consumer protection measures currently contained in the Building Act 2004 (Building Act).

We consider that the consumer protection measures in the Act are a major evolution to consumers' rights in the residential construction industry. The government is aiming for these legislative changes to have a significant impact on the way the industry operates - a fundamental behavioural change on the part of both consumers and building contractors.

The purpose of the consumer protection measures in the Act is to move away from the heavy reliance on building consent authorities for building quality and incentivise building professionals and trades people to take responsibility for the quality of their work and to stand behind it.

The consumer protection measures provided for in the Act can be summarised as follows:

- Requiring certain information to be provided before a residential building contract is entered into
- Prescribing minimum requirements for residential building contracts over \$30,000
- Implying warranties into residential building contracts
- Providing remedies for breach of the implied warranties
- Requiring defective building work under a residential building contract to be notified and remedied within one year of completion
- Requiring certain information and documentation to be provided on completion of building work under a residential building contract.

Much of the detail relating to the consumer protection measures is still to be outlined in regulations.

We comment further on each protection measure below.

Pre-contract information

Before entering into a residential building contract, contractors will need to give the consumer:

- Certain information about the contractor (disclosure information)
- A checklist of the matters that the consumer should take into consideration when entering into a residential building contract (checklist).

Contractors will need to give the consumer the disclosure information and the checklist where the price of the building work is over \$30,000 or where the consumer asks for the information. We would expect that even modest renovations to a dwelling would be covered and certainly every contract for the construction of a new dwelling. Once consumers become aware of their rights, it is likely that consumers are more likely to request this information for the smallest of jobs (eg installing a dishwasher) or slightly bigger jobs (eg retrofitting double glazing). In addition, where contractors have been courting a consumer before the consumer protection measures have come into force (eg provided quotes or where builders have worked with the consumer to develop concept plans for renovations or a new build), the contractor would still need to provide the disclosure information and the

checklist before the consumer signs the building contract.

The disclosure information may include:

- The legal status of the contractor (eg whether the building contractor is an individual, a partnership, or a limited liability company)
- The dispute history of the contractor
- The skills, qualifications and licensing status of the building practitioners who will actually be doing the building work
- If the contractor is a limited liability company, the role of each director and the business history of each director.

The checklist may include:

- An explanation of the legal obligations of both the consumer and the contractor in relation to the work
- An outline of the risks associated with payment in advance for completion of the work
- A summary of dispute resolution options
- A list of sources for further advice and information.

The intention behind the disclosure information and the checklist is to assist consumers to distinguish between contractors who have a history of good business practice and good quality building work (and who use experienced, qualified and skilled practitioners) and those who do not.

Because it is difficult for consumers to distinguish between contractors on the basis of performance, many consumers choose contractors on the basis of price alone. The government considers that this allows well performing contractors to be undercut by poor performers and continue to remain in the market. As a result, this undermines building quality, increases the need for rework and repairs and reduces productivity.

We can see the benefit in contractors disclosing such information to consumers. A significant amount of information needs to be disclosed when unsophisticated investors invest in non-property related assets even when such investments are significantly less than the cost of (say) a new home. There is little publically available information that consumers can access about contractors.

Consumers can check the Licensed Building Practitioners register to see if the contractor has been suspended, or can check if the contractor is a member of a particular body (eg Plumbers, Gasfitters and Drainlayers Board) or registered as a Master Builder or certified by Certified Builders Association of New Zealand. However, there is little information about their history. Consumers have to rely on information that may be found on websites such as nocowboys.co.nz.

Contractors will need to manage how they provide the disclosure information to ensure that this information is provided in context.

Once contractors have developed this pre-contract information, it will be a matter of updating it overtime and ensuring that it is disclosed to consumers before the contract is entered into. This will involve some training to front line employees and a message to reinforce the importance of disclosure. A failure to provide the information pre-contract is an offence giving rise to liability to a fine of up to \$2,000.

Minimum requirements for a building contract

The Act goes further and provides that where a building contract is above \$30,000 it must be in writing, dated and contain certain provisions.

The provisions that are to be included in a residential building contract will be set out in regulations and may include:

- The parties
- Dispute resolution
- The process for varying the contract
- The timeframe for performing the contract
- The payment process.

If there is no written contract, the regulations may stipulate that specified clauses are taken to be included in the contract. If there is a written contract but it does not include the matters specified by the regulations, the regulations may stipulate that the prescribed clauses are taken to be included in the contract nonetheless. The contractor will be unable to alter the implied clauses.

As with the pre-contract information, once contractors have either prepared a form of contract or updated their existing contract, it will be a matter that (in respect of contracts that meet the threshold price) employees ensure that the contract is completed, signed

and dated before the work is carried out. This will involve some training to front line employees and a message to reinforce the importance of complying with this obligation. A failure to comply with the minimum obligations for contracts is an offence giving rise to liability to a fine of up to \$2,000

Implied warranties

The Act retains the existing warranties implied in building contracts (which are currently set out in section 397 of the Building Act). This maintains the Building Act layer for consumer protection in addition to that contained in the Consumer Guarantees Act 1993 for services provided by contractors.

As currently contained in the Building Act, subsequent owners of dwellings can bring proceedings for a breach of any of the implied warranties notwithstanding that they were not party to the contract in which the warranties were implied. Furthermore, contractors cannot contract out of or limit their liability for a breach of the warranties.

Remedies for breach of implied warranties

What is different from what is currently contained in the Building Act is that the Act sets out remedies for a breach of the implied warranties. These remedies are modelled on the Consumer Guarantees Act remedies. We are not convinced that this will impose any additional obligations on contractors since similar warranties and rights exist under the Consumer Guarantees Act. All that will likely result from these changes is to create an overlap of legal rights with little impact in practice.

Repair

Where the contractor breaches a warranty the consumer can require the contractor to remedy the breach (which includes repairing or replacing defective materials).

If the contractor does not succeed in remedying the defect or refuses or neglects to do so within a reasonable time, the consumer can have the breach remedied by someone else and recover the reasonable costs from the contractor.

In addition, the consumer can obtain from the contractor damages for any loss the consumer suffers as a result of the breach of the implied warranty provided such loss was reasonably foreseeable. This would not include a reduction in the value of the building work.

Cancellation

A consumer can cancel a building contract in three instances:

- Where the contractor does not remedy a breach which can be remedied; or
- Where the breach cannot be remedied; or
- Where the breach is substantial.

We do not think that the right to cancel a building contract will be overused. This remedy is a last resort. Consumers are more interested in having any defect remedied rather than spending time looking for another contractor to carry out the work. However, in some instances, it may be appropriate to exercise the right of cancellation where the relationship between the contractor and the consumer has deteriorated and is simply no longer workable.

Claim for reduction in value

Where the breach cannot be remedied or is substantial and the consumer does not cancel the contract, the consumer can sue for damages for compensation for any reduction in the value of the building work below the price paid or payable for that work.

Accordingly, where a breach can be remedied, to be able to claim for a reduction in value, the consumer will need to argue that a breach is substantial in nature.

A substantial breach

A breach of a warranty is substantial if one of the following circumstances exist:

- A reasonable consumer fully acquainted with the nature and extent of the breach would not have entered into the building contract; or
- The building work is unfit for the purpose stated in the building contract; or
- The building work is of such nature and quality that it cannot be expected to produce the desired result stated in the building contract; or

- The building work is unsafe.

There is no additional guidance in the Act about the "reasonable consumer" test as mentioned above (under the heading 'A substantial breach'). A similar test for a substantial breach is contained in the Consumer Guarantees Act. It is also unclear under that Act when a substantial breach occurs in that circumstance. However, commentary suggests that the enquiry as to whether a substantial breach has occurred in respect of services (at least) necessarily requires a comparison with other service providers in the same market, so that a consumer's dissatisfaction with a particular result may not amount to a breach of substantial character where comparable service providers might have achieved a similar result. It is difficult to know how this test will be applied in the context of building work. Would a consumer not engage a contractor if the consumer knew that the building work would have a remediable defect that has a stigma attached to it (eg any defects resulting in weather tightness issues)?

In Christchurch many factors affecting the building industry (eg shortage of labour) are causing delays to the completion of building contracts for new dwellings. There may be an opportunity for consumers to argue that they can cancel a contract where the completion of the building work had taken a significant amount of time and breached the implied warranty of completion within a reasonable time and the breach was substantial in nature.

Clearly what is a reasonable amount of time to complete the construction of a new dwelling will need to be considered in the context of the environment in which the building work has been carried out. So what is a reasonable time for carrying out building work in Christchurch might be different to what is reasonable in Invercargill. While a 26 week build time may be relatively standard in Christchurch it may not be in Invercargill. The question is whether, if the consumer knew that it was going to take [x] number of months to complete the construction of that consumer's new dwelling with that contractor, the consumer would have entered into the building contract with that contractor?

The most effective way of dealing with this issue is for contractors to provide consumers with realistic timeframes for completing construction projects and have this recorded in writing not as a hard date for completion but rather as an indication of the period of time (eg six to 12 months without agreeing to a fixed date) that it might take to complete the project. In a way, the contractor would be agreeing to a period of time which if the project is completed after this period could lead to a breach of the implied warranty. We note that new section 362(k) of the Building Act allows contractors to disclose to owners any breaches of the implied warranties that exist at the time the building contract was signed.

Remedy of defect within one year of completion

There will be an automatic 12 month defect repair period when contractors will have to fix any defects in the building work of which the consumer advises the contractor "no questions asked". This right is in addition to the implied warranties and the rights associated with a breach of those warranties. However, this right will not apply to work carried out before 1 January 2015 or work carried out under a building contract entered into before 1 January 2015.

The defect repair period will commence when the work is completed. In most cases, it will be obvious when the building work is completed but we would recommend that contractors advise consumers of this in writing so that it is obvious to both parties.

The contractor will have to remedy the defect within a reasonable time. It will be presumed that the defect is attributable to the contractor. In other words, the onus is on the contractor to show that the defect is not attributable to the contractor's work. The contractor will not be liable for defects if it is caused by:

- A cause independent of human control
- Any act or omission, including accidental damage, by a person who is none of the following:
 - the building contractor
 - a subcontractor to the building contractor
 - a person for whom the building contractor is responsible in law
- Failure to carry out normal maintenance, or
- Failure to carry out, or cause to be carried out, repairs as soon as practicable after the defect becomes apparent.

The right to require the building contractor to remedy defects within the first 12 months can be exercised by subsequent owners.

The Act does not include for this right to remedy to be included in the contract between the contractor and the subcontractor. It will be up to the contractor to include such an obligation on its subcontractors in its subcontract agreements.

In many instances, this right does not impose any obligations on contractors additional to those that are already imposed on them under the implied warranties and the guarantees under the Consumer Guarantees Act. However, there is a power to the 12 month period because it takes away the defence of time. Many contractors can dismiss consumer claims by pointing to their contractual warranty period (which is likely to be equal to or less than the 12 month "no questions asked" period), and intentionally or by

ignorance not mentioning the warranties under the Building Act or the guarantees under the Consumer Guarantees Act. At the very least, the contractor will have to inspect the defect to be able to argue that it is not liable for it. Depending on the defect, it may be just as simple to fix it as it is to argue the point.

Information to be provided on completion of a building contract

After the building work is completed the contractor will have to provide certain information (to be prescribed by regulations) to both the owner and the relevant consenting authority. The purpose of this obligation is to ensure that the consumer and future owners of the dwelling know who carried out the building work and can access information about the ongoing maintenance requirements of the building. This information may include:

- Who the contractor was
- Any guarantee or insurance obtained by the contractor for the building work
- Maintenance requirements for any products incorporated in the building.

Once contractors have established the practice of providing this information to consumers and the consenting authority it should not be an onerous obligation on contractors. This will involve some training to employees and a message to reinforce the importance of complying with this obligation. A failure to comply with this obligation is an offence giving rise to liability to a fine of up to \$2,000.

On-sellers

The Act introduces the concept of an on-seller of a dwelling. An on-seller means a person who does any of the following things in relation to a dwelling for the purpose of on-selling the dwelling:

- Builds the dwelling by himself or herself or with the assistance of others
- In trade arranges for the dwelling to be built or acquires the dwelling from a person who built it or arranged for it to be built, or
- Acquires the dwelling in a transaction that is intended to defeat the purpose and effect of being deemed to be an on-seller.

The provisions relating to the implied warranties as they apply to contractors apply equally to the sale of the dwelling by an on-seller. Therefore, a contract by or on behalf of an on-seller for the sale of a dwelling:

- Is taken to be a contract for the building work already carried out or still to be carried out in building the dwelling
- Is taken to incorporate as the obligations of the on-seller the obligations of the building contractor under a residential building contract.

The provisions relating to the remedying of defects within 12 months of completion of the building work also apply to on-sellers.

An on-seller commits an offence if the on-seller sells a house or allows the purchaser to enter into possession of the house before a code compliance certificate is issued. However, the on-seller and the purchaser can enter into a written agreement (to be prescribed by regulations) allowing the on-seller to sell the house or allow the purchaser to enter possession of the house before a code compliance certificate is issued.

Conclusion

While the consumer protection measures create new obligations for building contractors changing the way contractors do business, we think that the measures (other than the 12 months defect repair period) will not pose a significant burden on contractors.

Once contractors have developed the pre-contract information, prepared a form of contract or updated their existing contract, and established the processes for providing consumers and the relevant consenting authority with the post completion information, these obligations should not be too onerous on contractors. However, contractors will need to take care in how they present the pre-contract information to their consumers.

The implied warranties already exist in the Building Act and the remedies for a breach of them are similar to remedies contained in the Consumer Guarantees Act for a breach of the guarantees in that Act which already applies.

The 12 months "no questions asked" defect repair period will be a powerful tool for consumers. At the very least, it will force contractors to engage with consumers because contractors will have to inspect the defect to be able to argue that it is not liable for the defect and to avoid being in breach of this provision.

We will provide further updates once the regulations are released.

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