IN THE HIGH COURT OF NEW ZEALAND
AUCKLAND REGISTRY

I TE KŌTI MATUA O AOTEAROA
TĀMAKI MAKAURAU ROHE

CIV-2021-404-605
[2022] NZHC 503

BETWEEN	BODY CORPORATE 392418 Applicant
AND	HOK FAI CHAN AND DEXIN MA & ORS First Respondents
	ANZ BANK NEW ZEALAND LIMITED Second Respondent

Continued over page

Hearing:	16 September 2021
Appearances:	A Hough and M Samountry for the applicant J Haig and D MacKenzie for the respondent
Judgment:	18 March 2022

JUDGMENT OF ROBINSON J

This judgment was delivered by me on 18 March 2022 at 2.30pm
pursuant to Rule 11.5 of the High Court Rules

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Registrar/Deputy Registrar

Solicitors:
Grimshaw & Co
Counsel:
J Haig, Barrister, Auckland
D MacKenzie, Barrister, Auckland

ASB BANK LIMITED
Third Respondent

BANK OF NEW ZEALAND
Fourth Respondent

LLOYDS BANK PLC
Fifth Respondent

MORTGAGE HOLDING TRUST COMPAY LIMITED
Sixth Respondent

WESTPAC NEW ZEALAND LIMITED
Seventh Respondent

CHUBB INSURANCE NEW ZEALAND LIMITED
Eighth Respondent

Introduction

[1] Body Corporate 392418 (Body Corporate) applies for an order to settle a scheme under section 74 of the Unit Titles Act 2010 (Act). The application applies to the unit title development at 132 Stancombe Road, Flat Bush, Auckland (132 Stancombe). HWD NZ Investment Co Limited (HWD) opposes the Body Corporate's application.

[2] The unit title development at 132 Stancombe consists of three blocks with a total of 47 units. HWD developed two of the three blocks and owns nine of the 47 units.

[3] The proposed scheme relates to repair and remediation works the Body Corporate has determined is required to be carried out at 132 Stancombe. The Body Corporate (and others) have issued separate proceedings against HWD (and others) alleging (amongst other things) that HWD was negligent in the course of developing two of the three blocks that comprise 132 Stancombe (negligence proceeding).[1]

[4] HWD's opposition to the current application to settle the scheme is two-fold. First, it says that 132 Stancombe is insufficiently damaged for section 74 of the Act to apply. Secondly, and in any event, HWD says that it is premature for the Court to approve the proposed scheme before the negligence proceeding has been determined.

[5] The application has been served on all unit holders at 132 Stancombe and also their mortgagees. Only HWD opposes the application.

Background

Damage and defects at 132 Stancombe

[6] The Body Corporate says there are two broad categories of defects at 132 Stancombe:

(a) Building/weathertightness defects; and

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1 *Body Corporate 392418 v Auckland Council & Ors* HC Auckland CIV-2016-404-2904.

(b) Fire defects.

Building/weathertightness defects

[7] The building defects are summarised in an affidavit of Andrew Gray, a Registered Building Surveyor and a director of GBC Group Limited. Mr Gray concludes that 132 Stancombe suffers from several building defects that require extensive repairs to both common and unit property. In summary, Mr Gray says that:

(a) *Perimeter walls*: The perimeter walls do not prevent the penetration of water and fail to meet the requirements of the New Zealand Building Code (NZBC). He says this has allowed leaks to the basement causing water ingress, widespread efflorescence and dampness, water staining to the walls and membrane detaching from the tanking walls.

(b) *Podium and walkway areas*: The podium and walkway areas do not prevent surface water from damaging the property/entering buildings. Mr Gray says the balustrade and balustrade fixings are susceptible to early corrosion; and do not sufficiently protect against loss of amenity through degradation and accidental falls. He says that this has caused water ingress to the basement, efflorescence, corrosion of steel and the development of mould.

(c) *Decks*: Mr Gray says that the balustrade and balustrade fixings do not sufficiently protect against loss of amenity through degradation and/or reducing the likelihood of an accidental fall. He says they do not meet the requirements of the NZBC. He says the surface coatings of the balustrades to the decks and their fixings do not resist corrosion and have corroded prematurely.

(d) *Roofs*: Mr Gray says the membrane gutters do not shed moisture or prevent the penetration of water and fail to prevent water ingress. He says the roofs do not comply with the NZBC. He says the inadequate construction of the roofs has resulted in water damage, water staining and premature deterioration of cladding.

[8] Mr Gray says these defects have caused damage requiring repair and remediation works including:

(a) *Perimeter walls*: Removing and reinstating all handrails, concrete stairs and timber decking; preparing blockwork walls to accept a new waterproof membrane; and installing new tanking including waterproofing above ground to the face of the masonry walls.

(b) *Podium and walkway areas*: Removing and disposing of membrane to podium; removing and reinstating downpipes, handrails, balustrades, access entry doors; repairing cracks in the top of the podium concrete; and undertaking repairs to masonry walls.

(c) *Balustrades*: Removing balustrades, deck membranes and adjacent cladding and installing new membranes and cladding and modified balustrades.

(d) *Roofs*: Remove cladding to wing walls and roof cladding sheet to vertical stepped roof walls; replacing gutter membranes; installing new cladding; and remediating wall to roof junctions.

Fire defects

[9] Fire defects are explained in an affidavit sworn by Ronald Green, a Passive Fire Consultant and director of Fire Group Consulting Limited (Fire Group).

[10] Mr Green carried out investigations into the passive fire defects at 123 Stancombe. He did so with a colleague from Fire Group and a fire engineer, Michael James. Mr Green says he found fire defects which can be divided into the following categories:

(a) The external walls were constructed in such a way that they do not adequately resist the spread of smoke.

(b) Interior walls and floors were constructed such that they do not adequately resist the spread of smoke and fire; and

(c) The stairs were constructed in such a way they do not adequately resist the spread of smoke and fire. In particular, no ventilation system or smoke lobby was installed.

[11] Mr Green says these defects amount to breaches of the NZBC. Importantly, he says that in the event of a fire significant avoidable damage will be caused to the building due to its compromised ability to resist the spread of fire and smoke.

[12] In order to rectify the fire defects, and to ensure that 132 Stancombe complies with the NZBC, Mr Green says it will be necessary to undertake (at least) the following repairs:

(a) Remove horizontal weatherboard and fibre cement sheet backing;

(b) Reinstate new compliant cladding and fire rated envelope system;

(c) Remove the electrical room and reconstruct to meet fire rating requirements;

(d) Remove and reinstate ceilings to access penetrations;

(e) Remove non-compliant penetrations as necessary and provide/install compliant fire rating to penetration;

(f) For the fire doors, remove the architraves, pack excessive gaps with fire stopping sealant and re-install fire doors; and

(g) Install a fire sprinkler system to the area where no ventilation system or smoke lobby was installed.

[13] On the other hand, in support of its opposition, HWD filed an affidavit from Kenneth Crawford, a fire engineer. Mr Crawford disputes Mr Green's evidence that

"*in the event of a fire, significant avoidable damage will be caused to the building due to its compromised ability to resist the spread of fire and smoke*". Mr Crawford points out that Mr Green's statement is predicated on a fire actually occurring. He says that has not happened and may never happen. Mr Crawford disagrees with Mr Green's statement that a fire would cause "significant avoidable damage". He says no one can say with any certainty the extent to which 132 Stancombe would be damaged in the event of fire. He says that the vast majority of fires are small; usually start in the kitchen; and do not cause much damage. He says these small kitchen fires would not be affected by the alleged defects which Mr Green has identified.

[14] Mr Crawford had not inspected 132 Stancombe so he was otherwise unable to comment on the existence or extent of the fire defects identified by Mr Green. He reserved his position in that regard.

[15] In terms of Mr Green's proposed repair strategy, Mr Crawford says this goes further than section 112 of the Building Act 2004 requires. He says it would be difficult and expensive to install a fire sprinkler system. He expects there would be alternative strategies available to the Body Corporate.

[16] In reply to Mr Crawford the Body Corporate filed an affidavit from Michael James who inspected 132 Stancombe with Mr Green. Mr James considers the fire defects to be widespread and systemic in all three buildings at 132 Stancombe. He agrees with Mr Green that the passive fire defects contravene the NZBC and endorses Mr Green's proposed repair strategy.

[17] The Body Corporate also filed an affidavit of Patrick Hanlon who was a registered quantity surveyor and a director of BQH Limited (BQH). Mr Hanlon estimates the costs of works required to complete the repairs to be $13,365,690. Following a tendering process, a firm budget was set for $13,277,352.

Proposed scheme

[18] The Body Corporate's manager, Craig Leishman, has filed an affidavit explaining that due to the nature of the remedial work required it is not practical to design a remedial solution for only the parts of the building for which the Body

Corporate is responsible under s 138 of the Act. As such, all the remedial work needs to be carried out at the same time under a single construction contract so that the Body Corporate can meet its obligations and satisfy the requirements of the local authority for building consent under the Building Act 2004.

[19] An important incident of the proposed scheme is the way in which it apportions the cost of repairing the roof of each of the three blocks. Under the Body Corporate rules the roof of each block is the unit property of the adjacent units on the top floor. As such, only the owners of the top floor units would be liable for the cost of repairing the roofs. Under the proposed scheme, however, the cost of repairing each roof will be apportioned amongst the owners of all of the units of each block in proportion to their ownership interest. Mr Leishman says this is intended to result in a fairer allocation of costs, recognising that the roofs serve all units and all owners will benefit from their repair.

[20] The proposed scheme is otherwise on relatively standard terms. It provides that the Body Corporate is, subject to the provisions of scheme, to carry out the repairs irrespective of whether they are to common property or to principle units or accessory units. The Body Corporate is empowered to act as agent for the owners in respect of all matters relating to the repairs. In particular, the Body Corporate is empowered to identify defects; quantify the extent of repairs; instruct and engage experts; apply for and obtain consents, approvals and certificates of compliance; and contract with project managers, contractors and trade persons.

[21] The Body Corporate is empowered to levy and collect from the owners such funds as it considers necessary in order to undertake and complete the repair. As noted above, this would see the costs of repairing the roofs allocated between all unit owners, not just those on the top floor.

[22] The proposed scheme contains dispute resolution provisions. It also provides that the owners indemnify the Body Corporate and its committee members, but not in respect of fraud or wilful misconduct.

Approval

[23] The Body Corporate held an Extraordinary General Meeting (EGM) on 26 January 2021 at which it resolved to apply to the Court for orders settling the scheme. The minutes of EGM record that there were 15 unit owners present at the meeting in person, by proxy or postal votes all of whom voted in favour of the scheme. The vote in support of applying the scheme was carried unopposed.

[24] Each copy of these proceedings has been served on all unit owners. Only HWD opposes the application.

HWD's opposition

[25] HWD opposes the scheme on the following grounds:

(a) First, HWD says the alleged fire defects have not caused any physical damage to 132 Stancombe; and; the remaining weathertightness defects have not caused sufficient damage to qualify as "substantial damage" in relation to which a scheme can be approved under s 74 of the Act.

(b) Secondly, HWD says that it is inappropriate to approve the scheme while the negligence proceeding remains on foot because:

(i) the extent to which there has been damage requiring repairs, and the appropriateness of the Body Corporate's proposed remediation strategy, are contentious issues in dispute in the negligence proceeding; and

(ii) it is premature to approve the cost allocation sought under the proposed scheme because the outcome of the negligence proceeding (in particular any damages recovered) may affect the scope of the repairs the unit owners are prepared to undertake (and fund) at 132 Stancombe.

Legal principles

[26] Section 74 of the Act relevantly provides:

> **74 Scheme following destruction or damage**
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> (1) This section applies if any building or other improvement comprised in any unit or on the base land is damaged or destroyed, but the unit plan is not cancelled.
>
> (2) The High Court may, by order, settle a scheme on the application of –
>
> (a) the Body Corporate; or
>
> …
>
> (3) A scheme under sub section (2) may include provisions –
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> (a) for the reinstatement in whole or in part of the building or other improvement; or
>
> …
>
> (7) In the exercise of its powers under subsections (2) and (3), the High Court may make any orders that it considers expedient or necessary for giving effect to the scheme, including orders –
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> …
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> (b) directing payment of money by or to the Body Corporate or by or to any person; or
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> …
>
> (d) imposing any terms and conditions that it thinks fit.

[27] The leading authority is the Court of Appeal's decision in *Tisch v Body Corporate* 318596.[2] In *Tisch* the Court of Appeal identified a three step process which s 74 imposes on a Court considering an application to settle a scheme:

(a) Step 1: The Court must be satisfied that the building has been damaged or destroyed.

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[2] *Tisch v Body Corporate 318596* [2011] 3 NZLR 679. Tisch was decided under s 48 of the Unit Titles Act 1972 (UTA72) but s 74 of the Act is essentially the same as s 48 of the UTA72.

(b) Step 2: If so satisfied, the Court must decide whether to settle a scheme. That is, the Court must decide whether a scheme is appropriate in the circumstances.

(c) Step 3: If the Court decides a scheme is appropriate, it must then decide what the terms of the scheme should be.

[28] I deal with each of the three steps in turn.

Step one - has the building at 132 Stancombe been damaged?

Substantial damage?

[29] The Court may only settle the scheme if the buildings at 132 Stancombe are "damaged or destroyed, but the unit plan is not cancelled".[3] HWD submits this requires damage to a building to be *substantial* before a scheme may be settled to repair it. HWD submits the damage at 132 Stancombe does not reach that threshold because the passive fire defects have not caused damage and the weathertightness damage is insubstantial.

[30] As the Court of Appeal noted in *Tisch*, there is no guidance in s 74 as to the amount of damage necessary to trigger the section.[4] The Court of Appeal observed that:

> About all that can be said is that no-one is likely to apply [s 74] unless the damage is substantial. But if they do, the Court will probably not be minded to settle the scheme.

[31] HWD submits that realistically this requires damage to be substantial in order to engage s 74. Relying on the statutory interpretation principle noscitur a sociis counsel for HWD submits that the proper interpretation of "damaged" in s 74(1) should be coloured by the following words "or destroyed". Similarly, the heading of s 74 says that it concerns a "scheme following destruction or damage". HWD says that in this context "damage" means substantial damage, not just any damage.

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3 Unit Titles Act 2010, s 74(1).
4 *Tisch* at [36], with reference to s 48 of the Unit Titles Act 172.

[32] Counsel for HWD also points out that s 74 applies only in respect of unit plans that are not cancelled. Under s 188 of the Act the Court may only cancel a unit plan if it is satisfied that it would be "*just and equitable that the Body Corporate be dissolved and the plan cancelled*". Counsel submits that anything less than substantial damage would be unlikely to meet that threshold.[5]

[33] Counsel submits that a threshold requiring substantial damage is consistent with the potential consequences of schemes which may bind all owners and may require significant departures from Body Corporate rules. In support of this submission, counsel refers to various cases in which the Court has settled schemes in relation to buildings that were substantially damaged.[6]

[34] I do not consider that s 74(1) necessarily requires "substantial damage" in order to trigger s 74. Although the Court of Appeal predicted that a court would "probably not" be minded to settle a scheme unless the relevant damage is substantial, it deliberately did not set that threshold as a matter of principle. To state the obvious, Parliament could have easily incorporated a "substantial damage" threshold into s 74 but it did not. The subsequent cases in which schemes have been approved to repair buildings that were substantially damaged do not assist HWD. In those cases there was no dispute that the substantial damage had met the threshold. The Courts did not determine that the substantial or significant damage set the threshold.

[35] Having said that, the extent of damage will always be relevant. In my view a Court may consider that issue in the context of step 2 (whether a scheme is appropriate in the circumstances) and step 3 (what the terms of the scheme should be) of the three step process identified in *Tisch.*

Are the passive fire defects "damaged"

[36] HWD submits that fire defects alone are not damage within the scope of s 74. It says the fire defects have not caused any physical damage. It relies on Mr

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5 Counsel sights *O M Hardware Limited v Body Corporate 303662* (2015) 15 NZCPR 921 where the High Court cancelled a unit plan for a development in Christchurch that was destroyed in the Canterbury Earthquake.

6 *Body Corporate 312431 v Auckland Council* [2015] NZHC 951; *Body Corporate 371455 v ASB Bank Limited* [2019] NZHC 1606; *Body Corporate 208399 v Kim* [2015] NZHC 2548.

Crawford's evidence that there will be no physical damage to 132 Stancombe unless there is a fire in the future; and even then the damage may be insubstantial.

[37] In response the Body Corporate says that the Courts have previously accepted that passive fire defects can constitute damage when sanctioning a scheme. It relies on *Re Body Corporate 324371*[7] and *Body Corporate 182563 v Hadlow*[8]. HWD says those cases are distinguishable because in each there was also actual damage caused by significant building defects and weathertightness issues. HWD says there is no previous case in which alleged passive fire defects are the "driving feature" of alleged damage.

[38] I am satisfied that passive fire defects can amount to damage for the purposes of s 74(1). It should not be necessary for a Body Corporate or its members to wait for a fire to cause damage before a Court is able to settle an otherwise appropriate scheme to remediate a defective building. In *Tisch* the Court of Appeal held that s 48 did not require the proposed remedial work to be "essential", observing that "there may, for example be cases where early work will prevent or minimise imminent damage".[9] I make the same observation here. In my view defects giving rise to a risk of actual fire damage may themselves constitute "damage" for the purposes of s 74.

Weathertightness damage

[39] If I am wrong about that, I am in any event satisfied that Mr Gray's evidence demonstrates actual damage to 132 Stancombe. Amongst other things, water ingress to the basement has resulted in damage, including efflorescence, dampness, staining to masonry walls, membranes detaching from the tanking walls, corrosion of steel and the development of mould. Water ingress to the balustrades to the podium and walkway areas has caused the premature corrosion of those balustrades and their fixings. The balustrades to the decks have also prematurely corroded. Pooling water has damaged and stained the roofs and has caused the premature deterioration of the roof's fibre sheet cladding.

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7 *Re Body Corporate* 324371 [2021] NZHC 242 at [12].
8 *Body Corporate 182563 v Hadlow* [2021] NZHC 1358.
9 *Tisch* at [42].

[40] For these reasons I am satisfied that 132 Stancombe has been damaged.

Step 2 – is a scheme appropriate in the circumstances?

[41] The Body Corporate says that the practical issue here is the need to treat the roof areas at 132 Stancombe as common property notwithstanding that they are unit property owned by the owners of the top floor apartments. The Body Corporate says all units benefit from the roof, but a standard ownership interest levy would place a disproportionate burden on the top floor unit owners that own the roof area. The proposed scheme will apportion the costs of roof repairs to all unit owners in proportion to their ownership interests.

[42] HWD does not oppose the application directly on the basis that apportioning roof repair costs in this way is unfair or inappropriate.[10]

[43] HWD says the scheme is inappropriate while the negligence proceeding remains on foot. Contentious issues in that proceeding include: the extent of any damage; and the most appropriate method of remediating any passive fire defects. This will involve competing arguments about the proper application of s 112 of the Building Act 2004. HWD submits that by approving this application the Court may predetermine those issues and bind HWD to a remediation strategy that is based on the very claim in the negligence proceeding that HWD denies.

[44] I do not agree. Approving the scheme in no way determines whether HWD is liable to the Body Corporate; and if so what is required from HWD by way of remedy. This Court can approve the scheme without making any findings in that regard. No issue estoppel or res judicata will apply. The current application proceeds on the basis that the Body Corporate and unit owners (except HWD) have accepted the need to undertake the repair and remediation works recommended by their independent experts. The scheme sets out how the Body Corporate is to raise levies to cover the costs of those repairs and remediation works, and how it is to arrange for the works to

[10] The Body Corporate's evidence is that if it raises levies under the standard rules to fund the proposed repairs HWD will pay $217,415 more in repair costs then it will pay under the scheme in this respect in which case HWD will benefit from the scheme.

be carried out. Mr Leishman confirms that the unit owners have agreed to the arrangements regardless of the outcome of the negligence proceeding.

[45] It is also important to bear in mind that HWD is party to this application in its capacity as an owner of units at 132 Stancombe. It is party to the negligence proceeding in its capacity as a developer of 132 Stancombe. If HWD did not own units at 132 Stancombe it would not be a party to this application, or otherwise have standing to oppose it, purely in its capacity as a defendant in the negligence proceeding.

[46] This also deals with HWD's related submission that it is premature to approve the scheme before the parties know whether the Body Corporate will recover damages in the negligence proceeding. The proposed scheme is an arrangement between the Body Corporate and the unit holders, including as to the allocation of repair and remediation costs, that is independent of any claims the Body Corporate may have against HWD in its capacity as a developer.

[47] In this regard I also note clause 13 of the proposed scheme. This provides that the Body Corporate may issue credits to the owners to the extent of any compensation it receives in legal proceedings issued in relation to the defects. So, the scheme proposed in this application contemplates the recovery of damages in the negligence proceeding, but does not depend on any such recovery. The two proceedings, and the issues they raise, are entirely separate.

[48] In all the circumstances I am satisfied that settling a scheme is the best option for the unit holders as a whole. I accept the Body Corporate's submission that it is fair and just as between unit holders that they all contribute to the cost of repairing the roofs from which they will all benefit. I also agree that it is appropriate and beneficial for all repairs to be carried out at the same time, and under a single construction contract.

[49] In reaching this conclusion I note that paragraphs C and D of the background to the proposed scheme record that:

> C. [132 Stancombe] has building defects to common and unit property and resulting damage identified by the Body Corporate's building consultants and may contain further defects and damage identified during the course of further investigations and/or repairs ("**the Defects**").
>
> D. It is necessary to carry out remedial work to rectify the Defects and associated damage to the Property ("the Repairs"). For the avoidance of doubt, the repairs include all work the relevant authorities require be undertaken to ensure code compliance in the course of or in association with work to rectify the Defects.

[50] As noted above, the proposed scheme relates to repair and remediation works that the Body Corporate and the owners (except HWD) have accepted needs to be carried out regardless of the outcome of the negligence proceeding. I record that in approving the proposed scheme as between the Body Corporate and the unit owner I make no finding in relation to any of the matters in dispute between the Body Corporate (or any of the other plaintiffs) and HWD (or any of the other defendants) in the negligence proceeding.

Step 3 – what should the terms of the scheme be?

[51] This third step involves the Court settling the terms of the scheme. The Court has a discretion: s 74(7) provides: … "*the High Court may make any orders that it considers expedient or necessary for giving effect to the scheme*…". In *Tisch* the Court of Appeal identified five guiding principles, each of which I consider here.

[52] First, a proposed scheme with broad support is to be preferred. Here, the resolution approving the scheme was passed by all unit holders who attended the EGM. That was only 15 of the unit holders, but only HWD opposes this application. Importantly, HWD does not oppose the terms of the scheme per se. Its opposition relates more the timing of the scheme in relation to the negligence proceeding.

[53] Secondly, I am satisfied the proposed scheme is appropriately detailed. I have summarised the terms at paragraphs [19] – [22] above. This Court has approved similar schemes before.

[54] Thirdly, the scheme will apply retrospectively in relation to works already completed, including identifying the relevant defects and the scope of remediation works. I am satisfied This is appropriate in the circumstances.

[55] Fourthly, the scheme provides that the Body Corporate is to carry out the repairs irrespective of whether they are to common property or private units. The scheme will enable the works to be carried out at the same time and under a single contract. It provides that the Body Corporate must apply due care and attention, and undertake the repairs diligently and expeditiously.

[56] Fifthly, for reasons already traversed, I am satisfied that it is appropriate for the scheme to depart from the Body Corporate rules to provide that the costs of repair and remediation works to be met by all unit owners, not just those on the top floors as would be the case under the Body Corporate Rules.

[57] Overall, I am satisfied that the scheme does justice between all unit owners, including HWD.

Result

[58] The Court makes orders approving the scheme in accordance with paragraph 1 of the Body Corporate's Notice of Originating Application dated 8 April 2021.

[59] The Body Corporate is entitled to costs. My preliminary view is that these should be calculated on a 2B basis. In the event that the parties cannot agree, the Body Corporate is to file a memorandum within 10 working days of this Judgment. HWD is to file a memorandum with a further 5 working days. The memoranda are to be no more than five pages long. I will deal with the issue on the papers.

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Robinson J