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Building and Construction Update

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Welcome to …

… the April 2007 edition of the Building and Construction Update. This edition – by Justin Cotton - focuses on two recent cases heard in the Victorian Civil and Administrative Tribunal (VCAT) which raise complex issues for directors of building companies.

Justin Cotton joined our Building and Construction team in February this year. We welcome his expertise to the team and look forward to an opportunity of introducing him to you.

Please do not hesitate in contacting us if you have any queries regarding domestic building matters.

Andrew Whitelaw
Partner

Directors beware! Liability for Directors of building companies

A domestic building registration can only be held in the name of a natural person, not a company. A company engaged in domestic building must have at least one director who is a registered domestic builder. Regardless of whether a director is on site much of the time, they can be said to be a person who has "managed or arranged the carrying out of domestic building work", as contemplated by the *Domestic Building Contracts Act* 1995 ("**the DBCA**").

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To what extent is a director truly the directing mind and will of a defendant building company, and an appropriate party to legal action? Or is an aggrieved Owner taking a 'kick and hope' punt on making a viable claim against a company director?

It is always tempting to seek to draw a director into the litigation and liability loop, particularly when faced with small building companies with only one or two directors.

The two cases of *Lawley v Terrace Designs Pty Ltd [Domestic Building]* VCAT 1363 (11 July 2006) and *Baines v Terrace Designs Pty Ltd [Domestic Building]* VCAT 1363 (11 July 2006) examined a range of issues involving concurrent defendants to a claim for defective building works.

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Directors beware!
Liability for Directors of building companies continued

Various parties were joined to the VCAT proceedings, including the building company, the director of the building company, the architect, the building surveyor, and the soil engineer. Many pertinent legal issues were canvassed, including the meaning of apportionable claims under the *Wrongs Act* 1958 and the correct assessment of damages between concurrent wrongdoers. In addition, the possible liability of building company directors was analysed.

It appeared on the evidence that the director was involved with the works as follows:

(a) the director was the registered builder;

(b) the director performed some of the building work himself;

(c) the director personally supervised the construction of the houses including the construction of the footings;

(d) the director planted trees that led to problems with the works such as cracking;

(e) the director was intimately involved in the design of the houses;

(f) the director personally undertook rectification work on the light courts.

The Tribunal canvassed four diverging views each with judicial support as to the personal liability of a director for corporate torts. Those views indicate that the law is uncertain. They can be summarised as follows:

- A director will be liable when he or she has "procured or directed" the company to commit the tort;
- A director will be liable only if they have made the wrongful act their own as distinct from it being purely the company's act;
- A director will be liable if they have assumed responsibility for the company's acts;
- A director is not liable for procuring the company to infringe the rights of others (see for example *Said v Butt* [1920] 3 KB 497).

Other cases have drawn a distinction where the wronged party has deliberately chosen to enter into a contract with a company, and where no such election to contract with a company was made. In the former case, it can be argued that the Plaintiff has knowingly entered into a contract where the doctrine of 'limited liability' applies. In other scenarios, for example where a 'strict liability' or a tortious act may have occurred, no such election may have been made by the Plaintiff and a director will be less able to rely on 'limited liability'.

In *Baines and Lawley*, there were contractual claims against the builder including breaches of the statutory warranties in s8 of the DBCA. Senior Member Young found that the builder (i.e. the building company) was liable for these breaches. However, the natural person director was exonerated, because:

(a) there must be something more in the director's conduct than simply "organizing or even carrying out the work badly", so that a careless act by the director could not of itself attract personal liability, unless "the carelessness was so flagrant as to be outside normal bad building practice"; and

(b) the director's actions were not sufficiently careless to make him guilty in tort (for negligence), despite the fact it was a small building company where the director was personally involved in the defective works.

Senior Member Young decided that to create a liability for directors in a personal capacity there must be some conduct of the director which is more than simply carrying out company duties, even if such managing or arranging the carrying out of the works results in a breach of contract or a failure by the company to perform its obligations. To hold otherwise would be to deprive small companies, with only one or two directors, the limited liability protection afforded to corporations.

Although directors are often successfully joined to VCAT actions involving defective building works, there is an element of difficulty and novelty in the idea that such a claim against a director will eventually succeed. In all likelihood, a high degree of involvement in the building works, and carelessness in their performance, will need to be shown.

It should be borne in mind that a company structure can be used to protect a registered builder from personal liability.

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