



## THE CONSTRUCTION LANDSCAPE IN NEW ZEALAND

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*Over the past 12 months [various economic factors] have converged to create ideal conditions for New Zealand's property and construction sector ... but it seems that the activity has really only just begun.<sup>2</sup>*

*NZ Lawyer, June 2015*

### INTRODUCTION

1. It is now widely accepted that New Zealand is in the midst of the largest construction boom in 40 years. "Unprecedented growth" is already being seen in some regions and is forecast to continue over the next decade<sup>3</sup>. The boom presents both opportunities and challenges.
2. This paper, which considers the state of the construction industry from an economic and legal perspective, is divided into the following sections:
  - a. Economic landscape of New Zealand's construction sector;
  - b. Risks and challenges arising from the current boom; and
  - c. Key legal issues and responses – to date and in the pipeline.

### NEW ZEALAND'S CONSTRUCTION SECTOR

3. New Zealand's economy is comparatively small and isolated. Although consistently one of the larger sectors, construction activity has traditionally been sporadic and low by international standards.<sup>4</sup>
4. In 2010, prior to the current boom, construction activity contributed approximately 6.3% of GDP and employed around 7.6% of New Zealand's workforce (or over 170,000 people).<sup>5</sup> The sector is particularly prone to boom/bust cycles.
5. Since 2012/2013, New Zealand has entered a period of exceptional and extended demand for building products and services. That demand is expected to increase further and remain elevated over several years in what has been described as a "golden era for New Zealand's ... construction industry".<sup>6</sup>

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<sup>1</sup> With assistance from Richard Belcher, solicitor, Hesketh Henry.

<sup>2</sup> *A tale of two cities*, NZ Lawyer, Issue 7.2, June 2015 at 16.

<sup>3</sup> Steven Joyce, Minister for Business Innovation and Enterprise, Press Release, 20 November 2013.

<sup>4</sup> Construction is the fifth largest sector by value (MBIE, *Construction Sector Report* (2013)) and the third largest by business count (Statistics NZ, *A Statistical Overview of the Construction Industry from 2000 to 2008* (2009)).

<sup>5</sup> MBIE, *Construction Sector Report* (2013).

<sup>6</sup> Nick Smith, Minister Building and Housing, Press Release, 29 July 2015.

## What is driving the boom?

6. A convergence or co-incidence of factors is behind the current surge in demand. Those factors include:
  - a. The end of the GFC and relative performance of the economy. New Zealand weathered the financial crisis with less public debt and stronger macroeconomic fundamentals than most other OECD nations, although it is facing some short-to-medium “headwinds” with the recent fall in commodity prices and share market volatility;
  - b. A backlog of infrastructure/public sector projects following historic underinvestment;<sup>7</sup>
  - c. The \$40b Canterbury rebuild following the 2010/2011 earthquakes;<sup>8</sup>
  - d. Record net inward migration;<sup>9</sup>
  - e. A series of new commercial developments, especially in Auckland where there is a long-term shortfall in retail and office space;
  - f. The seismic upgrading of “earthquake prone” buildings;
  - g. Repairs to leaky buildings in the wake of the weathertightness crisis;
  - h. A chronic shortage of housing, particularly in Auckland and Christchurch; and
  - i. Business-as-usual building activity.

## How big will the boom be?

7. Starting in 2013, a National Construction Pipeline Report is now published annually.<sup>10</sup> This forecasts the nature and timing of future building work by type and region over the proceeding five years. It is intended to improve productivity and help moderate the industry’s boom/bust cycle by providing regular and reliable forecasting.
8. The latest Pipeline Report was released in July 2015.<sup>11</sup> While still only in its third year, previous forecasts have been largely accurate. For example:
  - a. The actual value of all construction activity in 2013 and 2014 was \$27b and \$30b – just 0.4% and 4.4% below forecast;
  - b. The 2014 forecast was marginally lower than predicted primarily because of an 8.1% over-estimate for non-residential building. This seems to be due to longer lead times than expected; and
  - c. A longer and smoother peak is now predicted compared with previous forecasts.
9. Looking ahead, the current pipeline report continues to forecast significant levels of activity.<sup>12</sup> For the industry as a whole:
  - a. Annual construction activity is forecast to peak at **\$36.4b in 2016/2017**. This will be around 30% higher than the last peak in 2007 (\$26b) and nearly 40% higher than in 2012 (\$22.3b);
  - b. The forecast aggregate spend on all construction for the three years to 2017 is **\$106b**, and **\$200b** for the six years to 2020;

<sup>7</sup> National Infrastructure Unit, New Zealand Treasury, *The Thirty Year New Zealand Infrastructure Plan* (2015).

<sup>8</sup> [www.treasury.govt.nz/budget/2013/speech/06.htm](http://www.treasury.govt.nz/budget/2013/speech/06.htm). Westpac, by contrast, estimates \$35b on the basis that construction cost increases will mean some planned projects are not viable (*Economic Overview*, February 2015 at 4).

<sup>9</sup> Statistics New Zealand, *International Travel and Migration: June 2015*. New Zealand’s population is currently growing at its fastest rate in more than a decade (Statistics New Zealand, [National Population Estimates: At 30 June 2015](#), Media Release).

<sup>10</sup> Commissioned by MBIE and jointly prepared by Pacificon (NZ) Ltd and BRANZ.

<sup>11</sup> National Construction Pipeline Report, July 2015.

<sup>12</sup> See also *Wall of Work*, Build Magazine, Issue 146, February/March 2015 at 42 and MBIE *Housing and Construction Quarterly*, June 2015.

- c. The value of all building activity has grown between 9% and 12% pa over each of the past three years. Further **growth of 12% pa** is forecast for the next two years. This should see construction activity increase by more than 10% pa for around 3½ years – 18 months longer than in previous booms;
  - d. **Residential** building shows strong growth and is the main area of activity, with a forecast peak value of \$19.5b pa in 2017. Approximately 67,000 new homes are expected to be built nationwide in the five years between 2015 and 2019; and
  - e. **Non-residential** building should have steadier but still significant growth, with a forecast peak of \$17.2b pa in 2016.
10. Added to this is the Government's Thirty Year Infrastructure Plan, which was released on 20 August 2015.<sup>13</sup> This stems from a wider policy initiative to give more long-term focus to New Zealand's infrastructure needs, particularly following years of underinvestment. The report estimates that approximately \$110b will be spent on infrastructure projects over the next ten years and provides a list of significant local and central government led infrastructure initiatives. These include several mega projects priced at in excess of \$1b each.<sup>14</sup> With some justification, the report has been criticised for lacking detail as to how and when these projects will be undertaken.<sup>15</sup> However, even if the eventual figure is lower than estimated, it seems unavoidable that New Zealand will have to undertake further infrastructure investment that will contribute to demand.
  11. The positive outlook should be tempered with a degree of caution. First, SCIRT and residential reconstruction in Canterbury is nearing its peak and there is likely to be a noticeable drop-off in that region in due course (see further below). Second, the recent difficulties and ongoing risks in the global and domestic economy may dampen momentum. This is more likely to affect projects that are still at the concept stage (especially in the commercial space), rather than those where insurance monies are involved or funds have already been committed (eg residential and infrastructure projects). Third, industry confidence declined in the first half of 2015<sup>16</sup>, although it seems to have rebounded somewhat.<sup>17</sup>
  12. Consenting data has been generally consistent with the forecasting. The number of new consents increased continuously between May 2011 and June 2014, before plateauing for approximately 9-12 months, albeit still at a level more than double the most recent low point of March 2011.<sup>18</sup> The flattening trend during that period reflected the fact that Canterbury residential projects were approaching their high point, with a lag between consenting and completing. In Q3 2015, the national trend for new dwelling consents began to increase again and has now reached its highest level since November 2004.<sup>19</sup> This growth is being driven by Auckland and its surrounding regions, with the trend for Canterbury stabilised, but still at a level that is twice as high as the long-term average prior to the 2010 earthquake. Meanwhile, the value of all building work consented during the year ended June 2015 increased \$1.7b (13%) to \$15b, which follows year-on-year rises since 2011.
  13. Auckland and Canterbury continue to drive the demand, with the former now starting to overtake the latter. Visually, Auckland's skyline is increasingly dotted with tower cranes, while Cantabrians have been surrounded by construction sites for some time now. If cranes are a proxy, Auckland experienced a 40% increase over the first six months of 2015 (to 29) to overtake Canterbury (down from 31 to 23), followed by Wellington (9), Otago (6) and Waikato/Bay of Plenty (5).<sup>20</sup>
  14. It is worthwhile considering the main regions in more detail.

#### Canterbury

15. In Canterbury it is a tale of further growth until about 2016/2017, and then a noticeable decline. The earthquake reconstruction is nearing its peak.
16. Total building activity is forecast to continue – increasing from \$4.3b in 2012 to \$8.2b in 2016 (a year later than

<sup>13</sup> Note 7.

<sup>14</sup> [www.nzherald.co.nz/bridging-the-infrastructure-deficit/news/article.cfm?c\\_id=1502837&objectid=11499216](http://www.nzherald.co.nz/bridging-the-infrastructure-deficit/news/article.cfm?c_id=1502837&objectid=11499216).

<sup>15</sup> [www.nzherald.co.nz/business/news/article.cfm?c\\_id=3&objectid=11500283](http://www.nzherald.co.nz/business/news/article.cfm?c_id=3&objectid=11500283).

<sup>16</sup> Aecom Sentiment Survey, New Zealand, 1<sup>st</sup> Half 2015.

<sup>17</sup> See, for example, ANZ's September 2015 Business Outlook survey.

<sup>18</sup> Statistics New Zealand, *Value of Building Work Put in Place: June 2015 Quarter*, released 30 July 2015. See also CDC Quarterly Economic Report, February 2015

<sup>19</sup> Statistics New Zealand, *Building Consents Issued: September 2015*, released 30 October 2015.

<sup>20</sup> Rider Levett Bucknall Crane Index, Q2 – 2015, Third Edition – New Zealand.

previously predicted), before dropping back to less than half this (\$3.6b) by 2020. Since Q1 2011 there has been nearly a three-fold increase in quarterly construction spending in Canterbury.<sup>21</sup>

17. Residential and civil engineering (principally horizontal infrastructure) has led the rebuild effort and these types of activity are estimated to be approximately 50% complete.<sup>22</sup> Residential building, in particular, is forecast to peak over the next two years at \$4.8b pa, before falling back to \$2.1b in 2020. Building consent data is already showing a 17% decline since August 2014, which foreshadows a corresponding drop in building works from about 2016.
18. Non-residential activity is forecast to peak later at \$3.3b in 2016 (although 2017/2018 seems more realistic), before steadily reducing to \$1.5b in 2020 – below Auckland, Wellington and Waikato/Bay of Plenty. Heavy and light commercial projects are estimated to be 21-33% complete. Approximately 1,100 commercial buildings were lost in Canterbury, but not all of these will be replaced. Meanwhile, various public sector projects are planned or underway: a list of these and their expected timeframes can be found on the [CERA website](#).<sup>23</sup>

#### Auckland

19. Auckland accounts for one third of New Zealand's construction activity, even with the Canterbury rebuild. The value of Auckland's construction activity is forecast to grow by 73% in the five years to 2018, peaking at \$16.3b in that year.
20. Residential building makes up a surprisingly significant portion of this trend. It is expected to more than double from \$4.2b pa in 2013 to \$9.6b pa in 2018 – an increase of 126%. This will represent almost 60% of all construction activity in the region in 2018. In terms of volume, 84,000 new dwelling consents are forecast for the seven years to 2020. This compares with 30,000 over the previous six years. A sub-trend is denser living with rapid growth in multi-unit dwellings (ie apartments and attached houses). Consents for multi-unit and detached homes are expected to be about the same by 2020.
21. Non-residential building has a comparatively steadier growth path in Auckland, with a projected increase of 30% by value from 2013 to 2020. A shortage of A-grade commercial office space in central Auckland and relatively old stock is helping to spark new developments alongside public-sector projects. More than \$10b is likely to be spent on infrastructure, education, transport, office, accommodation and retail initiatives during the next decade.<sup>24</sup>

#### Waikato/Bay of Plenty

22. Waikato/Bay of Plenty is experiencing steady growth. The combined value of all building activity in these regions in 2014 was \$2b, which was 32.5% above 2012 levels. This is forecast to peak at \$5.5b in 2018 and then decrease slowly in the following two years.<sup>25</sup> Over 50% of this is expected to be non-residential.
23. Hamilton, in particular, has several multi-million-dollar commercial developments in the planning stage, and across the region some significant infrastructure projects are planned or underway.<sup>26</sup> In 2014 construction was identified in a local authority report as one of three sectors leading that city's economic rebound.

#### Wellington

24. Wellington's prospects are currently more modest, with only 6% growth forecast between 2013 and 2020, peaking at \$2.9b pa in 2019 and declining slowly after that. Wellington already has a comparatively high proportion of high-density housing, which means there is less scope for residential development than in other main centres.
25. However, Wellington's predisposition to a major earthquake means much of its building stock (particularly older commercial buildings and converted apartment blocks) is "earthquake prone" and will need to be strengthened or demolished. The 2013 Seddon earthquakes caused relatively minor damage but highlighted the risks for affected property owners. Many regional centres face similar issues.

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<sup>21</sup> Richard Stone, MBIE, *Best Practice Procurement and Contracting in NZ Construction & Infrastructure*, NZSCL Annual Conference, 2015.

<sup>22</sup> Ibid.

<sup>23</sup> [cera.govt.nz/recovery-strategy/leadership-and-integration/public-sector-rebuild](http://cera.govt.nz/recovery-strategy/leadership-and-integration/public-sector-rebuild).

<sup>24</sup> [www.nzherald.co.nz/business/news/article.cfm?c\\_id=3&objectid=11435182](http://www.nzherald.co.nz/business/news/article.cfm?c_id=3&objectid=11435182).

<sup>25</sup> Note 11.

<sup>26</sup> See, for example, [www.stuff.co.nz/business/industries/67679569/waikato-building-boom-sparks-job-call.html](http://www.stuff.co.nz/business/industries/67679569/waikato-building-boom-sparks-job-call.html).

## Rest of New Zealand

26. The rest of New Zealand has less populated regions with only modest increases projected through to 2020. Growth of 11% and 24% is forecast for residential and non-residential construction activity between 2013 and 2016/2017.
27. Otago is by far the largest region in this catch-all category, with \$1.77b forecast for the year ending 2015. This is \$0.84b above the next highest region (Nelson/Marlborough) but well below Wellington. Nevertheless, the University of Otago has announced a \$650m works programme that will help drive demand in Dunedin for some time.<sup>27</sup>

## Significant projects and available information

28. To give a further flavour of the construction landscape, appended to this paper is a summary of some significant projects that are planned or already underway.
29. In addition, there is now a plethora of reports, statistics and other data available from government, industry and media sources to match the growth in construction activity. Anyone wanting to undertake research on the sector can access a wealth of resource.

## **OPPORTUNITIES, RISKS AND CHALLENGES**

30. Increased demand is obviously welcomed. It provides opportunities to make use of excess capacity, to drive efficiencies and innovation, and to generate increased revenue and profit. There are, however, a number of risks and challenges that arise from such a steep and extended demand curve.
31. By far the biggest overall concern is a lack of scale and capacity on the supply side.<sup>28</sup> New Zealand's construction sector comprises around 50,000 individual businesses.<sup>29</sup> Of these, approximately 87% employ less than ten workers and many are 'one-man-bands'.<sup>30</sup> These figures reflect a highly fragmented industry made up of a large number of small operators. In short, there may not be enough firms with the necessary scale and capacity to undertake the volume of work or to achieve the sort of efficiencies that might otherwise be possible in larger markets. Paradoxically, this is likely to result in more insolvency events as costs increase and firms grow too quickly, and already there are signs of this in Canterbury.<sup>31</sup>
32. The capacity constraints are especially acute with skills. In Canterbury alone, CERA has acknowledged there are not enough skilled workers and machinery to work on all recovery tasks at the same time.<sup>32</sup> To some extent the gap has been, and will continue to be, plugged by overseas workers and, to a lesser extent, foreign firms.<sup>33</sup> In the last few years the Government has also committed more funds to building and engineering training nationally, but there is a lag before students complete their training. As for overseas firms, anecdotal evidence suggests they have found it difficult to enter the New Zealand market due to unfamiliarity with local conditions and possibly some parochialism. Meanwhile, individual projects are often not large enough to attract some overseas players, and there seems to be a reluctance to bundle projects in order to mitigate this.
33. In 2013 the Government released its **Construction Sector Report**, which took an in-depth look at the state and direction of NZ's construction industry. This followed a **Residential Construction Sector Market Study Options paper**, which sought views on a range of proposals to reduce residential construction costs in NZ. These initiatives reflected frustration at a sector it regards as fragmented, risk-averse and suffering from a lack of competition.<sup>34</sup>
34. Concerns about anti-competitive features and practices have seen the Commerce Commission take an increasingly active interest in the construction industry. This includes an industry survey, the establishment of a dedicated website to improve awareness of competition and consumer laws,<sup>35</sup> and a recent investigation into the plasterboard market.<sup>36</sup>

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<sup>27</sup> [www.odt.co.nz/campus/university-otago/308321/uni-spark-building-boom](http://www.odt.co.nz/campus/university-otago/308321/uni-spark-building-boom).

<sup>28</sup> MBIE Construction Sector Report (2013) at 11.

<sup>29</sup> On a per capita basis, this equates to approximately 90pax/business, compared with approximately 70pax/business in Australia ([www.ausstats.abs.gov.au/ausstats/subscriber.nsf/0/BE7D4569A92E5CA6CA257DF9000E452A/\\$File/att4no0k.pdf](http://www.ausstats.abs.gov.au/ausstats/subscriber.nsf/0/BE7D4569A92E5CA6CA257DF9000E452A/$File/att4no0k.pdf)).

<sup>30</sup> Note 31 at 48.

<sup>31</sup> National Business Review, *Why are so many construction companies failing?*, 19 October 2015.

<sup>32</sup> [www.cera.govt.nz/recovery-strategy/overview/read-the-recovery-strategy/section-9-pace-of-recovery](http://www.cera.govt.nz/recovery-strategy/overview/read-the-recovery-strategy/section-9-pace-of-recovery). Aecom's Sentiment Survey (1<sup>st</sup> Half 2015) identified skills and materials shortages as the single biggest challenge.

<sup>33</sup> Since July 2011 c 5,500 work visas were issued for the Canterbury reconstruction, with the majority coming from Britain, Ireland and the Philippines (Georgina Stylianou, *Demand persists for Chch workers*, Radio New Zealand, 6 July 2015).

<sup>34</sup> Note 31 at 10-11.

<sup>35</sup> [www.construction.comcom.govt.nz](http://www.construction.comcom.govt.nz).

The Government has also temporarily removed duties and tariffs on certain building products in order to try to improve building affordability.

35. From a legal perspective, the widening of tort law in New Zealand in recent years has encouraged scatter-gun claims, most notably in leaky building disputes, and this could extend further following the recent *Carter Holt Harvey v Ministry of Education* decision.<sup>37</sup>
36. Construction is already prone to disputation. As New Zealand moves further into a period of significant building activity, the risk of claims is likely to rise.

## LEGAL DEVELOPMENTS AND RESPONSES

37. A number of practice areas should be affected by the current building boom, including property, insurance, insolvency, employment and immigration. Below is a summary of some of the legal developments or responses from a construction law perspective. In general, they are intended to prevent injury, generate efficiencies and reduce claims.

### Procurement / Contracting

38. New Zealand has started to embrace alternative procurement methods (including D&B, Alliancing and PPP) and use different standard form contracts (including NZS, NEC3 and FIDIC), which can be selected to suit particular projects.

#### Alliancing

39. There is, in particular, an emerging trend towards the use of alliancing to procure infrastructure projects. Alliancing is currently favoured by the New Zealand Transport Agency for its larger and more complex projects.
40. Alliancing was first developed for North Sea oil drilling and has been widely used by the public sector in Australia for several years. It aims to create a collaborative 'win together/lose together' project culture, which is a significant departure from the traditional contractual approach to procuring construction works. In general terms, an alliancing contract will typically provide that:
  - a. Uninsurable risk is shared between the participants in agreed portions. In its purest form, such risk would be shared equally regardless of fault.
  - b. Participants are paid on a pre-determined 'gain share/pain share' basis.
  - c. The project is governed by a project alliance board made up of representatives from each project participant, who are required to make decisions unanimously.
  - d. Participants will act in good faith and adopt a 'no blame culture'. This is reflected in a prohibition on commencing proceedings against one another except in limited circumstances (eg non-payment, wilful default, fraud, etc).
41. Alliancing requires a different mind-set and contractual framework to achieve the necessary ethos and outcomes. Principals are attracted to alliancing because, if it works properly, it should encourage collaboration and problem-solving (rather than blame attribution) and avoid claims. However, it is usually only suitable for larger, complex projects involving multiple parties.

#### New NZS contracts

42. It seems obvious, but having appropriate and carefully prepared contracts in place from the outset of a project goes a long way towards ensuring its success. Unfortunately, construction contracts are often ill-considered, poorly prepared and sometimes never concluded, which creates ambiguity and leaves the parties more prone to falling out.

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<sup>36</sup> [www.comcom.govt.nz/the-commission/media-centre/media-releases/detail/2014/commission-concludes-plasterboard-investigation](http://www.comcom.govt.nz/the-commission/media-centre/media-releases/detail/2014/commission-concludes-plasterboard-investigation).  
<sup>37</sup> 2015] NZCA 321.

43. Standard forms are commonplace in construction and, until recently, the most common of these in New Zealand was NZS 3910:2003. With good timing, NZS 3910:2003 has been revised and superseded by three new contracts:
  - a. NZS 3910:2013 (Construction);
  - b. NZS 3916:2013 (Design & Construct); and
  - c. NZS 3917:2013 (Fixed Term).
44. These provide more tailored provisions for the standard types of commercial construction contracts and draw on lessons learned from the old NZS 3910:2003. Standards New Zealand says the new contracts “reflect a fair risk allocation between the parties”, although in reality parties often still seek a large number of revisions.
45. The new standards are generally easier to follow, contain new guidelines (that no longer have contractual status), have a more comprehensive tick-box type table for the Special Conditions, and include additional standard form documents (to save parties developing their own).
46. Among the substantive changes, the payment system has been simplified and contains different time periods, the method of calculating the price in cost reimbursement contracts has been set out more clearly and there is greater certainty about responsibility for arranging insurance and paying the deductibles. The conditions are aligned with the Construction Contracts Act 2002 (as amended to date).<sup>38</sup>
47. NZS3910 remains the most common standard form construction contract in New Zealand. The 2013 versions are still taking time to become *de rigueur* as parties get used to the changes and update their Special Conditions. Click [here](#) for a more detailed note on these new contracts.<sup>39</sup>

### Regulatory Changes

48. There are a number of legislative changes that have occurred or which are in the pipeline that will affect construction and property practitioners in different ways. The following are some key examples.

#### Building Act 2004

49. Recent amendments to the Building Act 2004 and associated regulations designed to strengthen consumer protections under residential building contracts came into force on 1 January 2015. These include:
  - a. Where residential building work will cost \$30,000 or more (including GST), the building contractor (which may include builders, plumbers, electricians, or any other tradesperson, whether as a sole trader, partnership, or company) will be obliged to provide certain prescribed disclosure information prior to commencing work, and have a written contract with prescribed minimum content, otherwise default terms will apply; and
  - b. Enhanced remedies for breach of statutory warranties relating to the proper performance of the building contract.
50. The amendments apply only to residential building contracts between the building contractor and their client. They do not apply to subcontracts or design work.

#### Construction Contracts Act 2002

51. The Construction Contracts Amendment Act 2015 (**Amending Act**) was passed on 22 October 2015. The main changes to the Construction Contracts Act 2002 (**CCA**) that this introduces include:
  - a. Largely removing the existing distinction between residential and commercial construction contracts;

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<sup>38</sup> NZS3010:2013 does not take account of the Construction Contracts Amendment Act 2015 (see further below). Special conditions may be required once those amendments come into force.

<sup>39</sup> [www.heskethhenry.co.nz/Articles/x\\_post/new-nzs-construction-contracts-00081](http://www.heskethhenry.co.nz/Articles/x_post/new-nzs-construction-contracts-00081).

- b. Updating and clarifying the adjudication procedure (eg by including an express entitlement to a right of reply by claimants);
  - c. Extending and speeding up enforcement of adjudication decisions;
  - d. Extending the right of adjudication to design, engineering and quantity surveying work; and
  - e. Requiring retention monies to be held on trust.
52. The amendments to the CCA will come into force progressively:
- a. All amendments except those identified below – on 1 December 2015;
  - b. Bringing design, engineering and quantity surveying work within the CCA – on 1 September 2016; and
  - c. Retention monies to be held on trust – on 31 March 2017.
53. In the next twelve months, engineers, architects and quantity surveyors will need to get to grips with the effect of the CCA on their business, including reviewing their standard terms, updating their payment practices, and making suitable arrangements with their PI insurers in the event of claims in adjudication.
54. Arguably the most contentious change has been the requirement to keep retention monies on trust, which was announced as a policy initiative by the National Party during the 2014 election. In summary, the Amending Act:
- a. Provides that retentions (above a *de minimis* amount to be determined) for *commercial* contracts will be deemed to be held on trust, but with no obligation to maintain a separate account or to ring-fence retentions from other funds (although, in practice, this seems unavoidable). The related amendments will also:
    - i. Require proper accounting records to be kept of retention money held.
    - ii. Allow retentions to be invested in accordance with the Trustee Act 1956, with the payer free to retain any interest earned and responsible for meeting any shortfall.
    - iii. Award interest on late payment of retentions – at the rate agreed in the contract or otherwise prescribed by regulations (which are yet to be published).
    - iv. Prohibit retention money being used as working capital (ie paying debts) or being subject to any execution order or process by a creditor (eg in a liquidation).
  - b. Prevent parties contracting out of these provisions.

There are no CCA-specific statutory sanctions or remedies for non-compliance beyond what is already provided for generally in existing legislation (eg Trustee Act 1956). This means the receiving party may need to bring a civil claim to enforce compliance and any losses arising from the payer's breaches. However, if there was a serious breach of trust, directors could potentially face penalties and possibly even criminal sanctions.

55. There are a number of associated issues that will require thought and supporting regulations are still to be developed, which is why a long lead time has been given for this part of the Amending Act. Those issues include administration and record keeping arrangements, amending construction contracts to incorporate an express interest rate for late payment of retentions, whether retention monies must be drawn down from funders in advance and held on trust until paid out (thereby increasing funding costs),<sup>40</sup> and whether contractors must hold monies on trust for sub-contractors in circumstances where those funds have not been paid to the contractor and are retained in trust by the principal.
56. The proposed amendments should give some further protection to contractors and sub-contractors in relation to retentions. However, it will not stop principals and head contractors from seeking to avoid paying retention monies – typically by raising a claim, asserting set-off and offering the 'carrot' of future contracts.

<sup>40</sup> MBIE commentary suggests that is not the intention, but that may not reconcile with the wording used in the Amending Act.

### Earthquake prone building legislation

57. The Building (Earthquake Prone Buildings) Amendment Bill 2013 has passed its first reading and the Local Government and Environment Select Committee reported back on 2 September 2015.
58. The Bill aims to balance the protection of citizens from earthquake prone buildings with the cost of strengthening, upgrading or demolishing buildings, and the protection of heritage buildings. In practical terms, in its current form, the Bill should clarify the definition of "earthquake prone buildings", introduce a more co-ordinated approach to addressing at risk buildings, set new timelines for assessment and remedial work, and impose penalties for non-compliance.<sup>41</sup>
59. A building is "earthquake prone" if it is less than one third of the strength that a new building would need to be in the same location. The definition takes into account the different risk profiles in different parts of the country. For example, a new building in Auckland only needs to be one third as strong as an identical building in Wellington.
60. Under the Bill, territorial authorities will continue to be required to undertake seismic capacity assessments for existing non-residential buildings, multi-storey buildings and multi-unit residential buildings. Officials are now recommending that:
  - a. The period in which *assessments* must take place be extended from 5 years to 10 and 15 years respectively for medium and low seismic risk areas; and
  - b. Unless an exemption is obtained, remediation work to strengthen "earthquake prone" buildings be completed within 15, 25 and 35 years respectively for high, medium and low seismic risk areas.
61. However, the select committee has recommended that the time periods for assessments and strengthening be halved for "priority" buildings, which will include unreinforced masonry such as parapets and facades. It appears that this recommendation will be accepted by the Government.
62. As the definition threshold will not change, the Bill should not materially alter the position of owners who already face seismic strengthening or demolition. In addition, "earthquake prone" status often affects the availability/cost of insurance as well as saleability/leaseability. Where the building is already tenanted, "earthquake prone" status can create issues about the landlord's obligation under the lease to improve the seismic capacity, breach of quiet enjoyment and compensation during strengthening works, and possible termination. Leases typically now include provisions to address seismic issues, but many existing leases do not.

### Health and Safety reform

63. The Health and Safety at Work Act 2015 was passed on 4 September 2015 and will come into force on 4 April 2016. This aims to strengthen protections for workers, impose greater obligations on persons conducting a business or undertaking (PCBU) and officers of PCBUs, and increase offences and penalties for breaching those duties.
64. The range of persons owing duties is expanded from the current Health and Safety in Employment Act 1992, as is the scope of the duties owed, and the penalties for breaching the legislation. The penalties will increase to a maximum \$3m fine for corporate PCBUs and/or imprisonment of up to five years for officers or individuals who are PCBUs in their own right.
65. The reforms are not expected to result in significant practical changes for contractors who already comply with existing health and safety law, but it will bring in to sharper focus the importance of getting this right for directors and officers. There may also need to be greater liaison between contractors and subcontractors about health and safety on construction sites.

### Unfair contract terms

66. The Fair Trading Amendment Act 2013 came into effect on 17 March 2015, with the aim of modernising New Zealand consumer law and better aligning it with Australia.

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<sup>41</sup> For an economic/industry discussion, see Nick Helm, *The cost of earthquake resilience*, Build Magazine, Issues 146, December 2014/January 2015 at 68-70.

67. The effect of these amendments is that a person who is in trade (both “person” and “in trade” are broadly defined) must not include an unfair contract term in a standard form consumer contract, or apply, enforce or rely on an unfair contract term in a standard form consumer contract. A “standard form consumer contract” is a contract that is in a standard form (ie the terms have not been subject to effective negotiation) and is a consumer contract (ie the goods or services being supplied are of a household, domestic or personal kind).
68. A contractual term will be “unfair” if it: would create a significant imbalance in the parties’ rights and obligations; is not reasonably necessary to protect the legitimate interests of the party who would be advantaged by it; and would cause detriment if it were applied, enforced or relied on.
69. Enforcement is through the Commerce Commission, which may commence legal proceedings either on its own initiative or if it receives complaints from consumers. It is possible these amendments may impact upon standard terms and conditions in residential building contracts – ie a consumer or owner might complain about such terms to the Commerce Commission, which could then take a builder to court.

#### Resource Management Act 1991

70. If the Government manages to pass the RMA reforms, they are expected to reduce compliant costs/time for obtaining resource consent unlock some land supply, which ought to encourage development activity.
71. With the change in Parliament’s composition after the Northland by-election, the Government no longer has the majority required to pass its RMA reforms. Without the support of United Future and the Maori party, it has had to rethink RMA reform with new legislation expected before the House later this year.

#### Auckland’s Unitary Plan

72. The proposed Auckland Unitary Plan is designed to be a comprehensive framework for the built and natural environment within the region. It will determine what can be built and where.
73. A key focus is the intensification of housing density in central Auckland through the creation of new housing zones in response to the current and projected population growth. This will involve the adjustment of height restrictions and allow for the proliferation of terraced housing and apartment building. Overall, it should open up new sites for development by reducing consenting barriers.
74. The Unitary Plan process is currently going through hearings, with a report due to Auckland Council in mid 2016, before coming into effect some time after that.

#### **Disputes**

75. Disputes are one of the more significant risk areas associated with the current construction boom. Managing and resolving disputes effectively is important at both a macroeconomic and business level.
76. In Canterbury, the Courts responded with the creation of a dedicated Earthquake List within the Christchurch High Court Registry. All earthquake-related cases (including judicial review and summary judgment applications) are now referred to the Earthquake List with the intention that they be dealt with more swiftly. However, arguably the list has become a victim of its own success. Approximately 250 proceedings are currently in the list, which has put strain on the judicial resources.
77. The List is dominated by “first generation” claims about insurance cover and the scope of reinstatement works. However, “second generation” claims about defective repairs are beginning to emerge, as are insolvency issues among smaller contractors that have grown too quickly and/or are under resourced/skilled. Meanwhile, more traditional payment and defect claims may become more frequent as costs increase and demand begins to decline.<sup>42</sup>

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<sup>42</sup> For example, claims in relation to re-measurement, variations, delay and disruption.

### Potential dispute resolution options

78. The dispute resolution options that may be available to construction parties include:<sup>43</sup>
- a. Litigation;
  - b. Arbitration;
  - c. Adjudication;<sup>44</sup>
  - d. Expert determination;
  - e. Early Neutral Evaluation (ENE);
  - f. Mediation/conciliation; and
  - g. DRBs.
79. The merits of litigation and arbitration and their comparative advantages / disadvantages are well known. While they might be appropriate in the event of a “full-blown” dispute, they are expensive and lengthy processes, which are normally considered a final option.
80. Adjudication brought a sea change in the resolution of construction disputes by providing parties with access to what is essentially a short-form arbitration process.<sup>45</sup> Adjudication is believed to be the most commonly used dispute resolution method in New Zealand for construction claims.<sup>46</sup> However, not every issue is amenable to adjudication.<sup>47</sup>
81. Expert determination and ENE are a creature of contract with no statutory support:
- a. Expert determination involves the engagement of “a third party expert, with expertise in the particular subject-matter in issue, to give a determination upon that subject issue”.<sup>48</sup> It is usually reserved for technical issues where there are no complex issues of fact or law.
  - b. ENE is a preliminary, non-binding opinion by an independent person on particular issues in dispute, often to assist with negotiations.<sup>49</sup>
82. Mediation/conciliation have become popular in the last 10-15 years as alternative consensual processes. Conciliation is like mediation except that, if a settlement is not achieved, the mediator (or conciliator) gives a non-binding view on the merits. This usually works best with technical disputes (like construction), by helping to highlight risk and bridge negotiations.

### Dispute Resolution Boards

83. One dispute resolution method that remains uncommon in New Zealand, but which has an excellent track record overseas and is starting to gain further traction here, is Dispute Resolution Boards (or DRBs).<sup>50</sup>
84. DRBs are mostly used in high-value infrastructure projects. They involve a board of independent persons (usually there are three), which is formed at the outset to keep a “weather eye” on the project and resolve disputes during the

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<sup>43</sup> The availability of these will usually depend on the dispute resolution clause in the particular contract. For a more comprehensive discussion of dispute resolution clauses, see N Gillies and P Cogswell, *Dispute Resolution Clauses: Uses and Analysis*, ADLS, 30 July 2015.

<sup>44</sup> Subject to certain statutory limits, adjudication is available as of right under the Construction Contracts Act 2002.

<sup>45</sup> An adjudication decision can be available within 20 – 37 days.

<sup>46</sup> [www.buildingdisputestribunal.co.nz/ADJUDICATION.html](http://www.buildingdisputestribunal.co.nz/ADJUDICATION.html).

<sup>47</sup> This includes issues that are too small and/or too complex for adjudication.

<sup>48</sup> Robert Gaitskell QC, *Adjudication – Its effect on other forms of dispute resolution (the UK experience)* ACLN #105 November/December 2005 at 9.

<sup>49</sup> *Ibid* at 11.

<sup>50</sup> That is, the US-style model of a board of independent persons who are actively engaged throughout the project. This contrasts with the Dispute Adjudication Board (or DAB) model employed under FIDIC contracts, which involves a standing board that simply determines disputes that are referred to it.

course of the works.<sup>51</sup> The board visits site and meets with the parties on a regular basis in order to proactively identify and resolve issues before they escalate into disputes and, where necessary, to make formal determinations. They are particularly effective at preventing disputes, but require the parties to make a reasonably significant up-front cost commitment without knowing the extent to which the board will actually be needed. Standard form contracts and terms for the creation of a DRB are available, but need to be amended to comply with New Zealand law.

85. With the number of medium-to-large projects coming on stream, it is an appropriate time to give DRBs further consideration in New Zealand. For appropriate smaller-scale projects, single-person DRBs (rather than the usual three-person board) can be employed to keep costs down. For a detailed note on DRBs and their pros/cons, please click [here](#).<sup>52</sup>

## CONCLUSION

86. This paper provides a smorgasbord of high-level information about the state and future of New Zealand's construction sector and the key legal responses.
87. Overall, it is a generally positive picture, with high levels of demand for building activity, especially in Auckland and Christchurch. Allied to this are different demand drivers, which extend beyond the Canterbury reconstruction, and which include a mix of public, commercial and residential projects.
88. On the supply side, however, the sector faces a number of challenges, including capacity and scale constraints, skills shortages, fragmentation and possible competition issues, which give rise to economic, industry and legal considerations. For property and construction lawyers, there are new procurement and contracting trends, as well as a number of recent and expected regulatory changes. Meanwhile, construction disputes are likely to rise commensurate with the increase in building activity.
89. It remains to be seen how well the industry can maximise the opportunities and manage the risks that lie ahead.

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<sup>51</sup> *MI-Space (UK) Ltd v Lend Lease Construction (EMEA) Ltd* [2013] EWHC 2001 (TCC) per Akenhead J at 16.

<sup>52</sup> N Gillies, *Rebuilding New Zealand: A Case for Dispute Boards*, Arbitrators & Mediators Journal, 2014, Vol 33, No 2.

## **Appendix**

### **EXAMPLES OF SIGNIFICANT PROJECTS THAT ARE PLANNED OR UNDER CONSTRUCTION**

#### **City Rail Link (\$2.4b, 2019)**

The city rail link is to be built in two 3.4 kilometre long twin tunnels that are up to 42 metres below the city centre. This is an extension on the existing rail line, which stops at Britomart, to Albert, Vincent and Pitts streets and then beneath Karangahape Road and the central motorway junction to Symonds Street, before rising to join the western line at Eden Terrace. The three new stations will improve access to more parts of the city and double the number of people within 30 minutes train travel of a city station.

The project timeline runs from 2013 to 2024. The first stage is expected to start in late 2015 and be completed in 2018/2019. The entire project is estimated to cost \$2.4b.

#### **Auckland Airport (\$2.4b, 2044)**

Auckland Airport has announced a 30 year development plan that consists of four phases:

- (a) Phase 1 is due to be completed by 2022 and involves improvements to the domestic and international terminals, the first stage of a new terminal road network, bus and public transport access, a terminal plaza, and improved parking facilities.
- (b) Phase 2, which is to be completed by 2030, will see a new northern runway operational around 2025 and an extension of the terminal forecourt.
- (c) Phase 3 is due to be completed by 2044 and involves the expansion of the international and domestic spheres within the terminal. This will see a largely increased number of aeroplanes that may be stored at the terminal.
- (d) Phase 4 is to be completed after 2044 and involves an extension of the northern runway to its full length as well as further development of the roading network outside the terminal precinct.

This four phase plan recognises the rapid growth projections in annual passenger movements over the next 30 years. In 2013, 14m passengers passed through Auckland Airport. In 2044, this figure is estimated to increase to over 40m.

The whole project is expected to cost approximately \$2.b.

#### **Waikato Expressway (\$2.1b, 2019)**

The Waikato Expressway project is designed to improve safety and reliability as well as reducing travel times and congestions on State Highway 1. The project will deliver a four lane highway from the Bombay Hills to the south of Cambridge. This project is split up into seven sections to be completed between January 2009 and December 2019. The project is expected to cost \$2.1b.

#### **Waterview Motorway Connection (\$1.4b, 2017)**

The Waterview connection in West Auckland involves a number of simultaneous construction projects. These projects range from the diversion and upgrading of motorway routes to the construction of new road tunnels. The project employs between 800 and 1,000 people on the five separate sites that cover a large area. In the south, the existing two lane motorway between Dominion Road and Maioro Street is being widened into three lanes in the northbound direction. This connects to State Highway 20, which has three lanes in each direction. The road then joins to two tunnels, each carrying three lanes of traffic between Owhiraka and Waterview.

The northern construction zone between the tunnels and the north western motorway includes ramps and trenches with four new ramps at Great North Road motorway interchange providing connections between the tunnels State Highway 16 to take the traffic to and from the tunnel portals.

The project agreement was signed in late 2011 and construction began in early 2012. The expected completion date is early 2017 with an estimated cost of \$1.4b.

### **Canterbury University Repairs/Expansion (\$1.1b, 2025)**

Canterbury University is currently executing its redevelopment plan to modernise its campus and infrastructure. The project is valued at \$1.1b, to be spent over the next ten years. 25% will be insurer funded, approximately half funded by the University, and the rest from Government support. The University has received \$268m in Government funds, contributing to "one of the largest building projects in New Zealand" and a major factor in the Canterbury recovery.

The investment is focused on recovery but also allows for redevelopment including new engineering and science facilities. The projects are expected to be completed in 2025.

### **Westgate Town Development (\$1b, 2016)**

The newly revamped Waterview connection will provide a swift route to the new Westgate Town development. The new development has elements of large format retail, business/office space, residential and public areas such as parks. The project consists of 56 hectares of new development including six hectares of public open space, playgrounds and skateboard parks, as well as large retail malls, large format and yard based retail, a library, community rooms and a Citizens Advice Bureau, an entertainment and lifestyle precinct, residential accommodation, and purpose built office space and commercial centre.

Westgate is one of three major urban developments currently underway in the North West of Auckland, alongside the creation of the Hobsonville corridor and the development of Hobsonville Point. Auckland Council estimates the first stage of the combined development will generate 20,000 new jobs and 5,000 new homes.

The Council is investing \$300m in infrastructure over the next 10 years in what is estimated to be a \$1b combined investment. The project is due to be completed in 2016.

### **Auckland University Works Programme (\$1b, 2024)**

Auckland University has launched a long-term investment programme. A significant part of this is aimed at improving its infrastructure and buildings. Projects include new student accommodation at the Carlaw Park Student Village, the Grafton Campus redevelopment, the Newmarket Campus, the Science Centre, and the Maths/Physics Building.

It is estimated that this programme will cost \$1b and be completed by 2024.

### **Lyttelton Port Repair/Expansion (\$1b, 2018-2035)**

Lyttelton Port will spend upwards of \$1b over the next 20 years to repair and upgrade its facilities. This will start with a \$465m earthquake reinstatement and development plan beginning in November 2015. The Port is also pressing ahead with controversial land reclamation on the Eastern side of its operation to allow the inner harbour to become more people friendly. The initial stages of the project are to be completed in 2018.

### **Transmission Gully (\$850m, 2020)**

Transmission Gully is an \$850m PPP project to build a 2km, four lane motorway, which will provide another route between Wellington and the Kapiti Coast. It is part of the wider Wellington Northern Corridor improvements that will assist in addressing capacity issues and remedying current safety and congestion concerns on the existing State Highway 1. Construction on Transmission Gully began in late 2014 and is due to finish in 2020.

### **Puhoi to Wellsford Motorway Extension (\$760m, 2025)**

The Puhoi to Wellsford Road of national significance is a 38 kilometre road through the Rodney area north of Auckland on State Highway 1. This project is designed to extend the northern motorway from the Johnstons Hill tunnels, just south of Puhoi, to a point north of Wellsford. The benefits are said to include future regional growth as well as improved safety and more reliable journey times.

The project is currently in its procurement stage, is expected to cost \$760m and be completed by 2025.

### **Ryman Health Care Growth Plan (\$710m, unknown)**

Ryman Health Care is reportedly planning to spend \$710m developing new aged care facilities after buying up land.

### **University of Otago Development Plans (\$650m, 2030)**

The University of Otago has approved a list of building developments with an approximate value of \$650m. The plan includes a new dental school, a major renovation of the science precinct, a new art building, a new biomedical research building, a new marine science building, a new music facility and other ancillary works.

This plan is part of the University's mission to remain a leading force in teaching, learning and research within New Zealand. The projects listed on the University's priority development plan will be evaluated for construction progressively over the next 15 years. The plan also includes a number of health and safety projects, which have high priority. These include improving access and safety in the commerce building, the completion of the refurbishment of the University of Otago, Wellington, facilities and some further seismic strengthening.

### **Christchurch Convention Centre (\$250-\$500m, 2018)**

The Christchurch Convention Centre precinct will accommodate up to 2,000 delegates. The centre will include hotel and residential accommodation, food and beverage outlets, retail, offices and car parking. It is expected to be completed at the end of 2018 with the total cost estimated to be between \$250m and \$500m.

### **Sky City International Convention Centre (\$430m, 2020)**

The New Zealand International Convention Centre will occupy a central Auckland site bound by Hobson, Nelson and Wellesley streets. It will feature a total of 3200m<sup>2</sup> of function area. Designed over three main levels, it will be able to host up to 2,850 delegates for convention and entertainment events.

Funded by Sky City, the \$430m building will be slightly smaller than originally planned but is expected to attract 33,000 visitors every year. The \$430m price tag excludes a new 300 room five star hotel, carpark and laneway, which will also be built and take the total spend on the development to approximately \$650m.

The centre is expected to take bookings from 2020.

### **NDG Tower (\$350m, 2020)**

Construction work on New Zealand's second tallest building is due to commence in 2016. At 209 metres, the tower off Albert Street is to be higher than all but the Sky Tower. Included in the design is space for shops, apartments, a cinema, restaurants, public swimming pool and a hotel (with the Ritz Carlton reportedly interested in the building).

The \$350m project is expected to be completed by 2020.

### **Justice and Emergency Services Precinct Christchurch (\$325m, 2017)**

A Justice and Emergency Services Precinct is currently under construction in Christchurch's CBD. This will comprise a justice building, an emergency services building and a parking building for operational vehicles. It will bring together all justice and emergency services in one purpose built, modern facility from mid-2017.<sup>53</sup> It is estimated that 2,000 people will occupy the 40,000m<sup>2</sup> precinct daily. Agencies are expected to move in by 2017, at a total cost of \$325m.

### **Metro Sports Facility Christchurch (\$300m, 2020)**

The Metro Sports facility in central Christchurch is a recreation centre, which will include netball, basketball, swimming and diving facilities. In the central feature will be a 79m reconfigurable competition swimming pool with a stadium seating 1,000 spectators. There will also be nine different courts, six for netball and basketball and three with retractable seating that can create a central show court.

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<sup>53</sup> This includes the Ministry of Justice, Police, Corrections, St Johns Ambulance Service, New Zealand Fire Service and Civil Defence and Emergency Management Functions for the Ministry of Civil Defence.

The project is expected to cost \$300m and be completed in late 2019 or 2020.

### **Precinct Downtown Development Project (\$300m, 2019)**

The Precinct Downtown development project is located at Auckland's CBD waterfront on approximately two hectares of land and buildings. It will provide new office and retail space, integrated with the existing HSBC House, Zurich House, PWC Tower and AMP Centre. The concept design is now complete and the consenting process is currently underway.

The project is estimated to cost \$300m and the expected completion date is 2019.

### **Wynyard Quarter Development (\$200m, 2017)**

In a joint project between Waterfront Auckland and Willis Bond, Wynyard Quarter is to become the site of a new intercity waterfront residential project. The partnership will see 500-600 new apartments, townhouses and duplexes built in the central area of Wynyard Quarter. It is expected to house over 1,100 people. All properties will be leasehold with a lease term of 125 years covered by an upfront payment.

Waterfront Auckland has expressed a vision for Wynyard Quarter to be the "leading location of sustainable urban transformation and the renewal in Auckland and across New Zealand".

The project is expected to finish 2017 and cost \$20m.

### **Christchurch Town Hall (\$127.5m, 2018)**

In June 2015 the Christchurch City Council agreed to restore the existing Town Hall. Before its closure following the February 2011 earthquake, the Town Hall had been the city's main venue for performances, civil and cultural events since 1972. The restoration is expected to be completed in 2018 at a cost of \$127m. This is partially funded by \$68.9m insurance monies, with rate payers contributing the balance of \$58.6.

### **State Highway 16 Causeway Upgrade (\$100m, 2017)**

The State Highway 16 upgrade is a 4.8km long project on Auckland's north western motorway between the Great North Road interchange and the Te Atatu interchange. The project is to raise the motorway 1.5m to prevent flooding and widen it to provide additional capacity and bus shoulder lanes in both directions. The cycleway along the motorway is also been raised, widened and upgraded as well.

The work is being completed in stages and is expected to be finally completed in 2017. The total cost of the upgrade is over \$100m.

### **Ngauranga Gorge to Aotea Quay Motorway Upgrade (\$100m, 2017)**

Work is now underway on the \$100m upgrade of Wellington's urban motorway between Ngauranga Gorge and Aotea Quay. The project includes adding another North bound lane, replacing the medium barrier, widening the State Highway to off ramp at Ngauranga, lengthening the existing sign gantries and adding a number of new ones, and finally building a new South bound on ramp for emergency services at Ngauranga. This 16 month project is expected to be operational by April 2016.

### **Pukete Wastewater Treatment Plant (\$24m, 2019)**

The Pukete Wastewater Treatment Plant, which is Hamilton's only treatment facility, is to be upgraded to meet the city's needs for the next 20+ years. The project has a budget of \$24m and a programme period of five years. It is expected to be completed in 2019.