IN THE HIGH COURT OF NEW ZEALAND
AUCKLAND REGISTRY

CIV-2012-404-005640
[2013] NZHC 2824

UNDER	the Weathertight Homes Resolution Services Act 2006
BETWEEN	CLEARWATER COVE APARTMENTS BODY CORPORATE NO 170989 First Appellant
AND	NICHOLAS VAN DIJK AND NORMAN PALMER AS TRUSTEES OF THE LIVI TRUST Second Appellant
AND	AUCKLAND COUNCIL First Respondent
AND	THE FLETCHER CONSTRUCTION COMPANY LIMITED Second Respondent

Hearing: 2 and 3 July 2013

Counsel E J L Werry for Appellants
S Thodey for First Respondent
G J Christie and M S C Harrison for Second Respondent

Judgment: 25 October 2013

JUDGMENT OF KATZ J

This judgment was delivered by me on 25 October 2013 at 4:30 pm
Pursuant to Rule 11.5 High Court Rules

Registrar/Deputy Registrar

Solicitors: Stephen McDonald, Auckland
Heaney & Co, Auckland
Simpson Grierson, Auckland

Counsel: E J L Werry, Auckland

Introduction

[1] This is an appeal from a costs determination of the Weathertight Homes Tribunal ("Tribunal"). Indemnity costs of over $1 million were awarded in favour of the respondents, Auckland Council ("Council") and Fletcher Construction Company Ltd ("Fletcher").

[2] The Body Corporate filed a claim under the Weathertight Homes Resolution Services Act 2006 ("WHRS Act") alleging that the Council and Fletcher were responsible for weathertightness defects in a complex of 16 residential apartments at West Harbour, Auckland, known as "Clearwater Cove". (Albeit only 12 of the 16 apartments remained in the claim by the time the matter went to adjudication.[1]) The claim was for approximately $1.5 million.

[3] Mr Brent Ivil had initiated and arranged the construction of the Clearwater Cove apartments by Fletcher. Further, all but one of the apartments involved in the proceedings are owned by an entity or person associated with Mr Ivil (for ease of reference, "the Ivil entities"). In particular:

(a) A family trust settled by Mr Ivil, the Livi Trust, owns three apartments.

(b) West Harbour Holdings Limited ("West Harbour") owns a further six apartments. Its director is Mr Ivil and its sole shareholder is the Livi Trust.

(c) Mr Ivil owns one apartment personally.

(d) Mr Palmer, a trustee of the Livi Trust, owns a further apartment personally.

[4] Accordingly, the Ivil entities have the controlling interest in the Body Corporate in respect of the apartments included in the claim (11 votes to one). The

[1] Claims in relation to three apartments were struck out unopposed after the respondents brought evidence that they had been purchased with knowledge of the alleged defects. The claim in relation to a fourth apartment was struck out for want of prosecution.

remaining apartment is owned by Petil Holdings Limited, an entity that appears to be unrelated to Mr Ivil.

[5] The Body Corporate's claims against Fletcher ultimately failed in their entirety. The claims against the Council also failed, save to a very limited extent, namely that there was a lack of clearance around the garage of the apartment owned by Petil Holdings Limited. The estimated costs of repairing that defect were $14,547.50 (incl GST). The Council was held to be 20% responsible ($2,909.50), with the Livi Trust being 80% responsible ($11,638.00) as it was the developer of the apartment complex.

[6] The Body Corporate appealed the Tribunal's substantive determination to this Court. That appeal was ultimately not pursued.

[7] Meanwhile, following the Tribunal's substantive decision, the respondents sought costs in the Tribunal. A full bench of the Tribunal (comprising the same members who had heard the substantive claim) found that the Body Corporate's claim lacked substantial merit and was also advanced in bad faith.[2] As a consequence the Tribunal awarded costs to the Council and Fletcher on an indemnity basis, totalling over $1 million. That decision now is before me on appeal. The key issues for determination are:

(i) Did the Body Corporate's claim in the Tribunal lack substantial merit?

(b) Was the claim in the Tribunal brought or pursued in bad faith?

(c) Did the Tribunal err in awarding costs on an indemnity (as opposed to District Court or High Court scale) basis?

(d) Did the Tribunal err in concluding that the level of solicitor-client costs incurred by the respondents was reasonable?

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2 *Clearwater Cove Apartments Body Corporate No 170989 v Auckland Council & Ors* [2012] NZWHT Auckland 35.

Appellate approach - two steps

[8] The Tribunal derives its power to award costs from section 91 of the Weathertight Homes Resolution Services Act 2006 ("WHRS Act"), which provides as follows:

> **91 Costs of adjudication proceedings**
>
> (1) The tribunal may determine that costs and expenses must be met by any of the parties to the adjudication (whether those parties are or are not, on the whole, successful in the adjudication) if it considers that the party has caused those costs and expenses to be *incurred unnecessarily* by-
>
> (a) *bad faith* on the part of that party; or
>
> (b) allegations or objections by that party that are *without substantial merit.*
>
> (2) If the tribunal does not make a determination under subsection (1) the parties to the adjudication must meet their own costs and expenses.
>
> (Emphasis added)

[9] Accordingly, the default position is that the parties bear their own costs in the Tribunal. Only if there has been bad faith on the part of one party, or aspects of the case (or defence) lacked substantial merit, does the Tribunal have jurisdiction to award costs, but only to the extent that the relevant costs and expenses have been incurred unnecessarily.

[10] Given this statutory context, the authorities have held that a costs appeal from the Tribunal should be approached in two stages:[3]

(a) Was the claim in the Tribunal "without substantial merit," or brought or pursued in bad faith?

(b) Did the Tribunal properly exercise its discretion to award costs?

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3 *Trustees Limited v Wellington City Council* HC Wellington CIV-2008-485-739, 16 December 2008, Simon France J; *Riveroaks Farm Limited v WB Holland* HC Tauranga CIV-2010-470-584, 16 February 2011, Allan J; *Coughlan v Abernethy* HC Auckland, CIV-2009-004-2374 20 October 2010, White J at [26] to [29]; see also Rule 20.18 of the High Court Rules.

[11] The first stage requires the Court to consider whether the jurisdictional foundation exists for an award of costs. This requires the issues of lack of substantial merit or bad faith to be considered afresh, by way of rehearing, in accordance with the well established principles set out by the Supreme Court in *Austin, Nichols & Co v Stichting Lodestar*.[4]

[12] The second stage will only arise if the appellate Court is satisfied that there is jurisdiction for a costs award (because the case lacked substantial merit or was pursued in bad faith). In that event it will be necessary to review the exercise of the Tribunal's discretion to award costs. The scope of appellate review of the exercise of a discretion is, however, much more limited. A Court will not interfere unless there has been an error of law or principle; the Tribunal has taken into account an irrelevant consideration or failed to take account of a relevant consideration; or the Tribunal has made a decision that is plainly wrong.

Factual Background

Information known at time of substantive Tribunal proceedings

[13] In the early 1990s the Waitakere City Council[5] owned a marina development at West Harbour. It included land that was leased to Westpark Marina Limited for a clubhouse. Significant construction work was undertaken. However, the clubhouse building was eventually abandoned in a partially completed state.

[14] In 1994 the Livi Trust acquired the site. It entered into an agreement whereby Fletcher agreed to design, build and fund the development of the site, on the basis it would be paid once the apartments were sold. The construction took place during 1995 and 1996, using the partially completed building developed by Westpark Marina Limited as a base.

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4 *Austin, Nichols & Co v Stichting Lodestar* [2008] 2 NZLR 141 (SC) at [16].
5 Whose successor is the Council.

[15] A final practical completion certificate was issued by the Waitakere City Council on 21 March 1996. On 2 April 1996 an interim code compliance certificate was issued, albeit certain work was still outstanding at the time. No final code compliance certificate was ever issued.

[16] By late 2002 the development was showing signs of “leaky building syndrome”. This was discussed at an annual general meeting of the Body Corporate in early August 2003. Subsequently, in March 2004, the Livi Trust raised its concerns with Fletcher that the development showed signs of being leaky. Mr Ivil’s evidence before the Tribunal was that Fletcher told him that the building was not a leaky building and he relied on this, although Fletcher did not comply with his request for a letter of confirmation.

[17] A year or so later, in July 2005, the Livi Trust wrote to Fletcher claiming that the development had “proven to be a leaky building”. It sent Fletcher a copy of a report identifying several areas of concern.

[18] In February 2006 a number of individual apartment owners made claims under the WHRS Act. An assessor’s report confirmed that the claim met the eligibility criteria under the WHRS Act. In May 2007, a Body Corporate multi-apartment application was filed with the Weathertight Homes Resolution Service. The assessor’s report in respect of that claim also confirmed that the claim met the eligibility criteria under the WHRS Act.

[19] The Ivil entities bought back a number of the apartments in the complex around or after the time the Livi Trust had first contacted Fletcher with its concerns that the complex was leaky, at heavily discounted prices. Indeed the Ivil entities continued to purchase apartments even after a claim was made to the Tribunal. The Ivil entities ultimately accepted that three apartments had been purchased with knowledge of the defects, as they were purchased after proceedings had been issued. As a result neither causation nor loss could be established and the claims in relation to those apartments were struck out unopposed.

[20] The hearing in the Tribunal took place over eight days during February and March 2011. West Harbour claimed that it had purchased its six apartments for market value and without knowledge of the defects. This was heavily contested by the respondents and appears to have been the focus of considerable evidence and submission at the hearing.

[21] A title search of the apartments prior to the hearing revealed that Waipareira Investments Limited ("Waipareira") held mortgages and caveats over some of the apartments. Mr Ivil was asked in cross-examination what interest Waipareira had in the apartments. He stated that Waipareira had assisted with refinancing and had taken mortgages by way of security. The Body Corporate denied that there was any intention to develop the apartments.

Further information discovered after the Tribunal had delivered its substantive decision, but prior to the Tribunal's costs decision.

[22] Following the Tribunal's substantive decision, the respondents became aware of separate proceedings between West Harbour and Waipareira. They searched the court file in those proceedings. From the statement of claim, statement of defence and affidavit of Mr Ivil in those proceedings the respondents learned that:

(a) In mid-2008 West Harbour and Waipareira had entered into a joint venture agreement to develop, construct and then operate (or licence the operation of) two stages of a hotel development at Clearwater Cove, utilising a joint venture company called Marina Resort Limited ("Marina Resort") in which they were each 50% shareholders.

(b) The Heads of Agreement was signed by Mr Van Dijk and Mr Palmer (the trustees of the Livi Trust), and Mr Ivil.

(c) The redevelopment included, as stage one, constructing a third storey on the apartments.

(d) Marina Resort agreed to purchase the 13 apartments owned by the Ivil entities for $7,810,000 (plus GST if any) with the deposit paid by discharge of an existing mortgage debt.

(e) West Harbour undertook to purchase the other three apartments in the complex (being the apartments owned by Mr Palmer personally, Petil Holdings Limited, and a Mr Garea).

(f) The joint venture parties agreed to delay registering formal transfers of title and, by an arrangement reached in November 2010, agreed to register the transfers of title on 30 June 2011, being after the Tribunal hearing set for March 2011. (The reason for this was that s 55 of the WHRS Act provides that a change in ownership terminates any claim by the former owner.)

(g) Waipareira registered caveats against some of the apartments to protect its "beneficial interest".

(h) Marina Resort allegedly agreed to vary the agreement and not to transfer title to itself in reliance on various oral representations made by Mr Ivil, including that West Harbour had a good claim against Fletcher and the Council and that the proceeds of recovery from the Tribunal proceedings would be utilised by the joint venture as working capital.

(i) The parties agreed not to undertake refinancing of the existing mortgages until the proceeds of the leaky home claims had been received by Marina Resort.

(j) In late 2008 Marina Resort Limited appointed a property manager, entered into tenancy agreements and began receiving the rents from the tenants of the 13 apartments owned by the Ivil entities. Further, the parties agreed that Marina Resort would fund any proceedings that were required to pursue the leaky home claims.

(k) Valuations had been undertaken in early 2008 and valuations continued to be obtained between then and the hearing.

[23] It was largely on the basis of this information, none of which had been disclosed prior to the substantive hearing, that indemnity costs were sought.

Did the Body Corporate's claim lack substantial merit?

Legal principles – what is "substantial merit"?

[24] In *Trustees Executors Ltd v Wellington City Council*[6] Simon France J considered what the Legislature intended by the phrase "without substantial merit" in s 91 of the WHRS Act. The issues he saw as important were whether the appellants should have known about the weakness of their case and whether they pursued litigation "in defiance of common sense".[7] Further, in determining the question of substantial merit it was impermissible to apply hindsight.[8]

[25] Subsequently, in *Riveroaks Farm Limited v W B Holland* Allan J endorsed those comments and observed further that:[9]

> The mere fact that an allegation or argument is not accepted or upheld by the Tribunal will not of itself expose the party concerned to liability for costs. In many cases a party will advance a claim or argument that requires careful consideration by the Tribunal, but which is ultimately rejected. Such claims may properly be characterised as of substance, as opposed to lacking substance. In other words they are "substantial". In my opinion, the Legislature has used the expression "substantial merit" in s 91(1)(b) in that sense, as denoting claims which do require serious consideration by the Tribunal.
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> Claims which have substantial merit, even if ultimately rejected, will not attract an order for costs ... Mr Lewis likens the proper approach to the "serious question" test commonly applied in respect of applications for interim injunctions. While in some cases the inquiry may be similar, it is preferable in my view to adopt the approach of Simon France J in *Trustees Executors* and to refrain from applying any gloss to the legislatively struck balance. The facts of individual cases will vary widely and the better course is simply to approach the necessary inquiry by reference to the language of the subsection.
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> (footnotes omitted)

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6 *Trustees Executors Ltd v Wellington City Council* HC Wellington CIV-2008-485-739, 16 December 2008.
7 At [52].
8 At [55].
9 *Riveroaks Farm Limited v W B Holland* HC Tauranga CIV-2010-470-584, 16 February 2011 at [9] – [10].

[26] I agree with those observations. Obviously the nature of litigation is that one party will generally be unsuccessful. It does not necessarily follow, however, that their claims (or defences) lacked substantial merit. A careful inquiry is necessary in order to determine whether a claim can properly be characterised as one that lacks substantial merit, viewed without the benefit of hindsight.

[27] However, as the Tribunal observed in *Phon v Modern Home Developments Ltd,*[10] the bar for establishing "substantial merit" should not be set too high. The Tribunal should have the ability to award costs against those making allegations which a party ought reasonably to have known they could not establish.

The Tribunal's findings on substantial merit

[28] The Tribunal found that the claim lacked substantial merit for the following reasons:

(a) The Council did not owe a duty of care to the Livi Trust because the Livi Trust was a developer.

(b) West Harbour knew of the defects before buying its apartments and bought them at a substantial discount reflecting the weathertightness issues. It should have been apparent to the Body Corporate from the time the Council's valuation evidence was filed that, in the absence of a plausible explanation for the (low) purchase price of the apartments owned by West Harbour, it could not prove loss. The claims arising from the seven units owned by West Harbour were therefore pursued in defiance of common sense.

(c) The Body Corporate's claim that the cladding installation was a major cause of damage and loss did not have a sound evidential basis and should not have been pursued. Further, there was no evidence of any causative link between the alleged cladding defects and the respondents.

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[10] *Phon v Modern Home Developments Ltd* [2011] NZWHT Auckland 24.

[29] I will consider each in turn.

Did the argument that the Council owed a duty of care to the Livi Trust lack substantial merit?

[30] The Livi Trust conceded at the substantive hearing that it was the developer and accordingly the Council did not owe it a duty of care.

[31] The Body Corporate argued that, notwithstanding this concession, the submission that the Livi Trust was not the developer had substantial merit as the contractual relationship between Fletcher and the Livi Trust was such that it was not absolutely clear which party was the developer.

[32] I do not accept that submission. Rather, I accept the respondents' submission that, unless there are exceptional circumstances, where an allegation is admitted by a party, the admission should be accepted as fact. As the respondents observed, this is consistent with a court being able to rely on facts which a party admits, to justify judgment being entered against that party.[11] It would be extremely unusual for a party to make an admission strongly against its own interests on an issue that had "substantial merit". In this case there was no benefit whatsoever to the Livi Trust in conceding the argument.

[33] As a result of the Livi Trust's concession there was no need for the issue to be fully traversed at the substantive hearing. It would be inappropriate, and prejudicial to the respondents, to attempt to embark upon that exercise now. The Livi Trust has admitted it was a developer. The Body Corporate did not dispute that admission at the hearing. The Tribunal clearly saw it as appropriate. Neither the Body Corporate nor the Livi Trust have appealed in relation to this issue.

[34] For all of these reasons I am satisfied that the argument that the Livi Trust was not the developer lacked substantial merit.

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[11] High Court Rules, r 15.15.

Did the Tribunal err in finding that the claims in relation to the apartments owned by West Harbour lacked substantial merit, because West Harbour knew of the defects before purchasing?

[35] The Tribunal, in its substantive determination, found that West Harbour knew of the weathertightness issues prior to purchasing its units. The Tribunal carefully weighed the competing evidence on this issue and found Mr Ivil's evidence in particular to be lacking in credibility. The Tribunal found that Mr Palmer and/or Mr Van Dijk and/or Mr Ivil had received documents that alerted them to the weathertightness issues in respect of the apartments before purchasing them. Further, the Council had adduced valuation evidence showing that West Harbour had bought its apartments at around land value. The Body Corporate did not produce any valuation evidence countering this. The Tribunal concluded there was no satisfactory explanation for the heavily discounted purchase prices, other than the weathertightness issues. An alternative explanation advanced by the real estate agent who brokered the sale was rejected.

[36] The Tribunal concluded that it should have been clear to the Body Corporate from the point at which the Council's valuation evidence was filed that the claim in relation to the apartments owned by West Harbour lacked substantial merit. The claimant could not prove loss in the absence of any opposing valuation evidence (which it did not bring). This finding also presumably applies to the apartment owned by Mr Ivil personally, because it was his knowledge that was imputed to West Harbour.

[37] I find no error in the Tribunal's analysis of this issue. The only reasonable inference from the evidence, considered as a whole, is that West Harbour must have known of the defects in the units at the time it purchased them and this was reflected in the purchase prices it paid. West Harbour's true state of knowledge would have been well known to the appellant and is not therefore an issue that needed "testing" at trial. Rather, the Body Corporate pursued recovery in circumstances where it knew or ought to have known that no loss had been suffered in relation to the units owned by West Harbour.

[38] Finally, I note that the Body Corporate also pursued unmeritorious claims in relation to the three other apartments from April 2008 until the end of 2009.[12] Those apartments had been purchased with knowledge of the defects, after the Tribunal application had been made. The respondents were unnecessarily put to the expense of applying to strike them out; an application that was ultimately not opposed by the Body Corporate.

Did the Body Corporate's claims relating to the cladding lack substantial merit?

[39] The Tribunal found that the Body Corporate's claim that the cladding had been wrongly installed over the entire building lacked substantial merit. The Tribunal observed that it should have been apparent to the Body Corporate prior to trial that its experts did not agree on the cause of the damage to the cladding. In addition, the Body Corporate provided no evidence of any causative link between the alleged cladding defects and the respondents' conduct. The Tribunal concluded that the claimant pursued its claim that the installation of the cladding was a major cause of damage and loss without a sound evidential basis: "This limb of the claim clearly lacked merit and should not have been brought".[13]

[40] The key difficulty with this aspect of the Body Corporate's claim appears to have been that one of its experts, Mr Earley, had relied on the wrong Harditex manual in his evidence, while its other expert, Mr Powell, had said that the cladding had cracked for reasons unrelated to Fletcher. Further, there was inadequate evidence linking any of the alleged defects to water ingress and damage. The Body Corporate submitted, however, that it was entitled to rely on the evidence of its experts and to test that evidence where it differed.

[41] Unlike the Tribunal I have not had the benefit of hearing the two experts give evidence. However, based on the record, I can see no basis for interfering with the Tribunal's conclusion that this aspect of the claim lacked substantial merit and should not have been brought. The suggestion that the Body Corporate should have been allowed to "test" its own expert evidence (which did not support its claim) at

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12 Referred to above at [19].
13 At [37].

trial is not convincing. The usual course is for a party to proceed to trial on the basis of evidence that supports their claim, then "test" their opponents' evidence.

Conclusion on extent to which the Body Corporate's claims lacked substantial merit

[42] As noted above, the fact that a claim is unsuccessful does not necessarily mean that it lacked substantial merit. Indeed in this case the findings of lack of substantial merit focussed on three specific issues. This is despite the fact that the claim failed on a number of other grounds, including limitation and the fact that there had already been a full and final settlement with Fletcher. The Tribunal presumably viewed those issues as being arguable and therefore having merit (viewed without the benefit of hindsight) despite the Body Corporate's arguments being ultimately unsuccessful.

[43] Nevertheless, the overall effect of the pursuit of the three arguments that lacked substantial merit was, as the Tribunal observed, that:[14]

> The claims in relation to the majority of units lacked substantial merit and should not have been pursued. As a result the Council and Fletcher have incurred costs and expenses unnecessarily.

[44] Although the claim in relation to Petil Holdings Limited's apartment succeeded to a limited extent, the Tribunal concluded that, when viewed as a whole, its findings were such that the entire claim should be considered to lack substantial merit.

[45] At this stage I part company with the Tribunal, albeit to a limited extent. The claim in relation to the unit owned by Petil Holdings Limited succeeded in the sum of $14,547.50 (incl GST). The Council was held to be 20% responsible for this claim, with the Livi Trust (which had been joined as a third respondent) being 80% responsible. Although in the context of the overall proceedings this amount is minimal, it cannot be said that the claim in relation to the unit owned by Petil Holdings was entirely without merit.

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[14] At [38].

[46] Further, of the three specific arguments that were found to lack substantial merit, only the third one (relating to the cladding) was relevant to the unit owned by Mr Palmer. The other two arguments were specific to the Livi Trust or West Harbour (and by implication Mr Ivil). Although ultimately the claim in relation to the unit owned by Mr Palmer was unsuccessful it is not clear to me that that claim lacked substantial merit from the outset. Accordingly I would err on the side of caution in relation to that particular unit also.

[47] The consequence of this is that it follows, in my view, that the claims in relation to 10 of the 12 units that remained in the claim at the time or trial lacked substantial merit.

Did the Tribunal err in finding that the Body Corporate acted in bad faith?

[48] As the Tribunal observed, the meaning of "bad faith" depends on the circumstances in which it is alleged to have occurred. The range of conduct constituting bad faith can range from dishonesty to a disregard of legislative intent. It is well established that a party alleging bad faith must discharge a heavy evidential burden, commensurate with the gravity of the allegations made.

[49] The Tribunal concluded that the Body Corporate acted in bad faith by failing to produce all relevant documents and failing to comply with specific orders by the Tribunal for discovery. The Tribunal observed that the fact that West Harbour was seeking to enforce the joint venture agreement in the High Court was inconsistent with the Body Corporate's denial in the Tribunal proceedings of any intention to develop the property.

[50] The Tribunal was, understandably, deeply troubled by the Body Corporate's failure to discover any documents relating to the existence and terms of the joint venture, the sale of the apartments to Marina Resort, valuations obtained for joint venture purposes and so on. This was despite both general and particular discovery having been ordered. In particular, given the unusual conduct of the Ivil entities in buying back a number of apartments, Fletcher had sought specific discovery regarding any repair and redevelopment plans for the complex. The Tribunal granted the application and ordered disclosure of:

> All documents including proposed remediation works, scope of works, concept plans, designs, quotations, reports, correspondence relating to the repair or remediation or redevelopment of the property.

[51] No documents relating to the joint venture were discovered pursuant to this order. Further, Mr Ivil did not disclose in cross-examination the existence of the joint venture, but simply stated that Waipareira had assisted with refinancing and had taken mortgages by way of security. Such an answer was extremely misleading. Mr Palmer also failed to disclose the existence of the joint venture in his evidence, despite having signed the joint venture heads of agreement. The Body Corporate denied that there was any intention to develop the complex.

[52] Due to the failure to discover the relevant documents, the Tribunal was deprived of the opportunity to make any factual findings regarding them in the substantive proceedings. Nor is it appropriate, or necessary, to make any definitive findings in the context of this costs appeal. However, it is clear that discovery of the documents would have been likely to significantly undermine key aspects of the Body Corporate's claim.

[53] The sale price of $7,810,000 for 13 apartments represents an average price of $600,769 per apartment. The evidence provided to the Tribunal was that West Harbour had purchased seven of the apartments for a total purchase price of $2,075,000. This is an average purchase price of $296,428. The respondents therefore submitted that the sale price of $7,810,000 reflects not only a sale at market value, without any deduction for any weathertightness issues, but also sale at a substantial profit.

[54] It was further submitted that the *Waipareira* documents establish that Marina Resort was for all purposes, other than the Tribunal claim, the owner of the apartments. It appointed the property manager, entered into the tenancy agreements and received the rent from tenants. The deferred settlement was simply a device to avoid the impact of s 55 of the WHRS Act, which would have terminated the Tribunal proceedings on transfer of the properties. Further, Marina Resort purchased the apartments with full knowledge of the condition of the apartments (the Heads of Agreement expressly acknowledged that issues exist).

[55] The Body Corporate submitted that such conduct did not amount to bad faith and that its failure to provide disclosure of the documents did not influence the outcome of the Tribunal's substantive decision (given that the Body Corporate's claims failed in any event). Further, the steps taken by the joint venture partners to defer settlement until after the Tribunal's determination made good commercial sense. In addition, West Harbour warranted in the joint venture agreement to make good any weathertightness issues, limited to the extent necessary in order for the third floor development to proceed.

[56] In my view, however, the Tribunal was correct to find that the appellant's conduct amounted to bad faith. Full disclosure in this case was critical, given that loss was a key issue and, associated with this, whether West Harbour bought its units with knowledge of the defects. Relevant documents were not discovered, in flagrant breach of a specific discovery order.

[57] The motivation for such conduct is, in my view, clear. Discovery of the documents would have been likely to seriously undermine the claims being made in the Tribunal. The documents strongly suggest that the apartments had been sold to Marina Resort at full market value, with no reduction in value for weathertightness issues. The documents also appear to significantly undermine West Harbour's claims of lack of knowledge of the defects. Further, the development plans would have impacted on the extent to which repairs were necessary. Indeed the documents suggest that the primary purpose of the Tribunal proceedings was not to obtain funds to repair the existing structure but rather to provide "working capital" for the joint venture's development plans for the complex. The documents were highly relevant to the issue of whether any loss had been suffered by the claimants.

[58] In my view there is no justification for overturning the Tribunal's conclusion that the Body Corporate's conduct amounted to bad faith. There was ample evidence before the Tribunal to support such a finding.

Did the Tribunal err in awarding costs on an indemnity basis?

[59] The jurisdiction to make a costs award under s 91 of the WHRS Act has been established, on both of the statutory grounds (lack of substantial merit and bad faith).

I therefore now turn to consider the second stage of the appeal, which is whether the Tribunal's decision to award costs on an indemnity basis was a proper exercise of its discretion. As noted at [12] above, there is a higher standard of appellate review where an appeal is from the exercise of a discretion.

[60] The Tribunal had three options as to costs: scale costs; increased costs; and indemnity costs. The Court of Appeal in *Bradbury v Westpac Banking Corporation*[15] gave the following guidance as to the circumstances in which it would be appropriate to award costs on each of these bases:

> (a) Standard scale applies by default where cause is not shown to depart from it.
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> (b) Increased costs may be ordered where there is failure by the paying party to act reasonably.
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> (c) Indemnity costs may be ordered where that party has behaved either badly or very unreasonably.

[61] The threshold to be met for an order for indemnity costs is a high one.[16] In deciding whether indemnity costs were appropriate in this case the Tribunal considered r 14.6(4) of the HCR (and cases decided under it) by way of analogy. That rule provides relevantly as follows:

> (4) The court may order a party to pay indemnity costs if—
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> (a) the party has acted vexatiously, frivolously, improperly, or unnecessarily in commencing, continuing, or defending a proceeding or a step in a proceeding; or
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> (b) the party has ignored or disobeyed an order or direction of the court or breached an undertaking given to the court or another party; or
>
> ...

[15] *Bradbury* v *Westpac Banking Corporation* [2009] NZCA 234; [2009] 3 NZLR 400 (CA).
[16] *Paper Reclaim v Aotearoa International Ltd* [2006] 3 NZLR 188 (CA).

(f) some other reason exists which justifies the court making an order for indemnity costs despite the principle that the determination of costs should be predictable and expeditious.

[62] In *Bradbury* the Court of Appeal, while noting that the categories in respect of which the discretion may be exercised are not closed, listed the following circumstances in which indemnity costs have been ordered:[17]

(a) the making of allegations of fraud knowing them to be false and the making of irrelevant allegations of fraud;

(b) particular misconduct that causes loss of time to the court and to other parties;

(c) commencing or continuing proceedings for some ulterior motive;

(d) doing so in wilful disregard of known facts or clearly established law;

(e) making allegations which ought never to have been made or unduly prolonging a case by groundless contentions.

[63] The Tribunal found that indemnity costs were justified in this case for the following reasons:[18]

> [69] We have no hesitation in concluding that in these proceedings Body Corporate 170989 engaged in misconduct causing loss of time to the Tribunal and other parties; wilfully disregarded known facts and clearly established law; and made allegations which ought never to have been made. We have not reached this conclusion lightly however we are not aware of another case where the conduct approaches the level of bad faith exhibited by this claimant. The fact that the claimant was legally represented from the outset of the proceedings reinforces our conclusion that the level of bad faith warrants an award of indemnity costs.

[64] It is therefore apparent that, in deciding to award indemnity costs, the Tribunal relied on both bad faith and the fact that the claims had lacked substantial merit.

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[17] At [29].
[18] At [69].

[65] The Body Corporate submitted that its conduct did not approach the flagrancy demonstrated in the *Bradbury* case and that it had not acted "badly or very unreasonably". The building did have water ingress issues, experts were retained by all parties who agreed on some, but not all, issues. As such it was reasonable in light of such disagreement to have the evidence tested at a hearing. Issues such as loss and whether West Harbour had prior knowledge of the defects needed to be tested at trial.

[66] I do not accept those submissions. For the reasons outlined at [30] – [47] above, the claims in relation to the apartments owned by West Harbour and the Livi Trust lacked substantial merit and should not have been pursued. Further, as a result of the Body Corporate's failure to comply with the Tribunal's specific discovery order, the eight day Tribunal hearing proceeded on the basis of incomplete and therefore misleading (by omission) information. Indeed I suspect that if full and complete discovery had been provided it is unlikely that the matter would have proceeded to a substantive hearing at all.

[67] In my view the lack of substantial merit, in itself, would probably not be sufficient to justify an award of indemnity costs on the facts of this particular case. However, when combined with the findings on bad faith, the necessary threshold is met. The Body Corporate has not persuaded me that the Tribunal was plainly wrong or made an error of principle in determining that costs should be awarded on an indemnity basis. The Tribunal was cautious in its approach, acknowledging that this was the first and only occasion on which it has awarded indemnity costs. Further, the two Tribunal members who determined the costs issues had presided over the claim since its inception. They therefore had detailed knowledge of the way the claim had progressed and been run by each party. They concluded that the bad faith demonstrated in this case was at a level never before seen in the Tribunal.

[68] Nevertheless, s 91 of the WRHS Act provides that only the costs "incurred unnecessarily" as a consequence of a party advancing arguments that lack substantial merit, or acting bad faith, are to be recovered. As I have noted above, the claims in relation to two of the units (that owned by Petil Holdings and also that owned by Mr Palmer) did not lack substantial merit. Further, there is no evidence that Petil

Holdings was aware of the joint venture, or that discovery of the material relating to the joint venture would have undermined its claim. In such circumstances it is necessary, in my view, to adjust the award of indemnity costs to reflect the fact that it has not been established that the costs and expenses (or at least not all of them) associated with bringing the claims in relation to those two units were incurred unnecessarily. Irrespective of those aspects of the claim that lacked substantial merit, some expenses were inevitable. Of course, those expenses would have been relatively minimal compared to those actually expended.

[69] Quantifying such expenses is, however, challenging. Realistically it would not be practicable, or even possible, to attempt to separate out the specific legal costs associated with bringing claims in relation to the Petil Holdings and Palmer units. A pragmatic and robust assessment is accordingly required. The claim initially involved 15 apartments, but this had been reduced to 12 by the time of trial. The claims in relation to two of the apartments were not entirely unmeritorious. In such circumstances reducing the indemnity costs award from 100% to 85% of the respondents' total actual and reasonable costs would, in my view, appropriately compensate the respondents for the unnecessary costs they have incurred.

Quantum of costs

[70] The final issue is whether the actual costs claimed by the respondents were reasonable. Harrison J (the trial judge in *Bradbury*) provided a helpful analysis of the approach to be taken in assessing the reasonableness of actual costs incurred.[19] His Honour suggested that the appropriate course is to:[20]

(a) Determine whether a particular item of expenditure is reasonably incurred – for example preparation of a statement of defence.

(b) Fix what would be a reasonable allocation of actual costs measured by reference to an appropriate time taken and allowing for the significance and complexity of the category of work; and

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[19] *Bradbury v Westpac Corporation* (2008) 18 PRNZ 859 (HC) at [207] – [214].
[20] At [209].

(c) Quantify the costs by reference to a median hourly rate reasonably applicable to it.

[71] Harrison J was assisted by the bank's lawyers providing him with a table showing steps in the proceeding and the actual cost. His Honour could then assess the reasonableness of each step.[21] The award of indemnity costs against Mr Bradbury's firm was $1,057,691.25 which included solicitor costs and disbursements. Westpac had sought actual costs of $1.683 million, however, the Judge awarded the lesser sum as what he assessed was a reasonable figure for the bank's actual costs.

[72] In this case the Tribunal determined that all of the costs claimed by the respondents (totalling $1,063,746.05) were reasonably incurred. The Council had provided the Tribunal with a memorandum dated 5 June 2012 claiming $341,650.13 in legal expenses, together with expert fees of $105,889.69. The Tribunal accepted these figures as reasonable.

[73] I accept the Body Corporate's submission, however, that the memorandum provides little detail to objectively assess whether the costs were reasonably incurred, if the Court were to adopt the method suggested by Harrison J in *Bradbury.* The memorandum sets out only dates of invoices rendered and an amount. There is no other information provided.

[74] Fletcher also provided the Tribunal with a memorandum in which it sought indemnity costs of $433,022.46 for legal expenses and $153,183.77 for expert costs. That memorandum also provided little detail from which an objective assessment could be made as to the reasonableness of the claimed actual costs.

[75] In fairness to the Tribunal, I note that the suggestion that a more thorough assessment of the costs should be undertaken, in line with the approach set out by Harrison J in *Bradbury*, has apparently only been raised for the first time on appeal. It was incumbent on counsel to draw the relevant authorities to the Tribunal's

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21 See the table at [212] in Judgment of Harrison J.

attention, particularly given that this was apparently the first occasion on which the Tribunal has awarded indemnity costs.

[76] Nevertheless, I accept the Body Corporate's submission that the Tribunal erred by simply finding that the costs claimed were "reasonable" without undertaking a more thorough assessment of them, given the very significant quantum of costs claimed. Although I am reluctant to see any further delay in final resolution of the costs issues, I do not have sufficient information before me to undertake such an assessment. Further, the persons best placed to do so are the Tribunal members who presided over the claim since its inception. I therefore, with some reluctance, remit the matter back to the Tribunal to enable that exercise to be undertaken.

[77] It is now over two years since the Tribunal's substantive determination was delivered and over a year since its costs determination was delivered. Although the precise amount of costs owing by the Body Corporate to the respondents has yet to be finally quantified, it is in my view appropriate that a significant payment now be made "on account".

[78] The Tribunal awarded costs of $1,063,746.05, which was based on 100% of the actual costs incurred by the respondents. I have held that the costs award should be reduced to 85% of actual costs, which (subject to any reasonableness review) would amount to $904,184.10. I have concluded that approximately half of this amount should be payable forthwith, with the balance payable once the Tribunal has completed its review of the reasonableness of the quantum of costs claimed, in accordance with the approach set out in *Bradbury.*

Summary

[79] In conclusion, I have upheld the Tribunal's finding that the Body Corporate's claims in the Tribunal lacked substantial merit, on each of the three grounds identified by the Tribunal, namely that:

(a) the Council did not owe a duty of care to the Livi Trust, because it was the developer;

(b) West Harbour purchased its units at a substantially discounted price, with knowledge of the defects. It accordingly suffered no loss; and

(c) the Body Corporate's claim that the cladding installation was a major cause of damage and loss did not have a sound evidential basis and should not have been pursued. Further, there was no evidence of any causative link between the alleged cladding defects and the respondents.

[80] I differ from the Tribunal, however, as to whether the consequence of these findings is that the entire claim should be considered to lack substantial merit. Ultimately the claim only succeeded in relation to one unit, and even then only to a very limited extent. I have, however, concluded that the claims in relation to two of the 12 units, viewed without the benefit of hindsight, cannot be said to have lacked substantial merit in the sense of being pursued in defiance of common sense.

[81] I have also upheld the Tribunal's finding that the Body Corporate acted in bad faith in its deliberate failure to discover relevant documentation, despite an express discovery order requiring disclosure of such documents. Discovery of the relevant documents would have been likely to have significantly undermined the Body Corporate's claim.

[82] I have concluded that the Tribunal did not err in awarding costs on an indemnity (as opposed to District Court or High Court scale) basis. However, the claims in relation to two (out of 12) apartments did not lack substantial merit and would not necessarily have been impacted by discovery of the withheld documents. Accordingly it cannot be said that the entirety of the costs of the proceedings were incurred unnecessarily, in terms of s 91 of the WHRS Act. An award of 85% of the actual and reasonable costs incurred by the respondents would, in my view, appropriately compensate them for the unnecessary costs they have incurred.

[83] Finally, I have concluded that the Tribunal erred in concluding that the level of solicitor-client costs claimed by the respondents was reasonable, on the basis of the relatively limited information before it. Given the very significant quantum of

costs claimed the Tribunal should have undertaken a more detailed assessment of the reasonableness of the costs claimed. I have accordingly remitted this issue back to the Tribunal for further consideration. In the interim, however, it is appropriate that the Body Corporate now make a significant payment on account of the costs incurred by the respondents.

Result

[84] The appeal is allowed in part and the orders made in the Tribunal's costs determination of 22 August 2012 are accordingly set aside.

[85] Body Corporate 170989 is to pay 85% of the actual costs (legal and expert) and disbursements reasonably incurred by the respondents in the substantive Tribunal proceedings.

[86] I remit this matter to the Tribunal to undertake a more detailed assessment, in accordance with the guidance set out by Harrison J in *Bradbury v Westpac Corporation,* of whether the actual costs claimed by the respondents were reasonably incurred, and to fix a final costs figure.

[87] In the interim the Body Corporate 170989 is to pay:

(a) Auckland Council the sum of $200,00 immediately, as a contribution towards its actual legal costs and expert fees; and

(b) The Fletcher Construction Company Limited the sum of $250,000 immediately, as a contribution towards its actual legal costs and experts fees.

[88] Any balance owing is to be paid after completion of the Tribunal's review of the reasonableness of the costs claimed by the respondents, in accordance with any further orders made by the Tribunal.

[89] Leave is reserved to file memoranda in relation to the costs of this appeal. Any memorandum from the respondents is to be filed within 20 working days of this

judgment, with any response from the appellant to be filed within 10 working days after filing and service of the respondents' memoranda.

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Katz J