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COMBUSTIBLE CLADDING

UPDATE 2020

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INTRODUCTION: COMBUSTIBLE CLADDING

Innovation in building design and materials has led to combustible cladding being used on the external walls of many Australian medium and high rise buildings. However, fires in buildings in Melbourne's Lacrosse building (November 2014), London's Grenfell Tower in June 2017 and the Neo fire in Melbourne (February 2019) have revealed the latent fire risks associated with combustible cladding and consequent risk to public safety.

Across Australia various state governments have introduced a series of measures to address community concerns about public safety and to identify the extent of the issues posed by combustible cladding.

The wider picture presents a number of challenges. The issues raised by Opal Tower in Sydney and combustible cladding overlap and expose systemic issues involving compromised design and broader building defects. The Building Ministers' Forum has sought to introduce some broader national approach while still giving state governments' regulatory powers. Nevertheless, the approach taken at National and State levels is fragmented and sanction based, instead of offering a uniform approach aimed at creating incentives for compliance. This is hardly comforting to industry participants and consumers, the ultimate end user.

This e-book highlights the following:

- Recent developments in Victoria, NSW & Q'ld;
- Challenges for consumers, the building industry and professional participants;
- Implications for insurance cover.

VICTORIA
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LACROSSE APPEAL: MID 2020

In March 2019 the Lacrosse VCAT decision served as a warning to building industry professionals including design consultants, engineers and certifiers about their potential liability arising from the selection, approval and installation of non - cladding on previous projects.

The Lacrosse decision found that the builder LU Simon had breached the statutory warranties of suitability of materials compliance with law of fitness for purpose implied into the design and construct contract. The decision also apportioned liability between various building professionals including the designer, surveyor, fire engineer, architect and superintendent.

Three of the respondents to the VCAT hearing, the building surveyor Gardner Group, fire engineer Thomas Nicolas and architect, Elenberg Fraser lodged an appeal with the Victorian Court of Appeal. They are arguing that the builder's liability should be increased saying the builder largely escaped its statutory obligations under the state's Building Act and should be regarded as a "concurrent wrongdoer". The appeal is expected to be heard in/around mid 2020.

FUND FOR RECTIFICATION WORKS ESTABLISHED

On 16 July 2019 Victoria announced a \$600 million package to fund building rectification works on 500 high risk buildings and the establishment of a dedicated fire cladding agency, Cladding Agency Victoria. The funds will be applied towards project management, professional design services, building surveying, building materials, building rectification works and approvals.

A state wide cladding audit inspected over 2200 buildings of which 500 of those were deemed high risk.

CLADDING RECTIFICATION GUIDELINES

On 19 December 2019, the Victorian Government issued funding guidelines (<https://www.vic.gov.au/cladding-rectification-funding-guidelines>) for the combustible cladding 'rescue package'. Cladding Safety Victoria may provide funding for the rectification of external wall combustible cladding of some higher risk residential apartment buildings, as assessed by the Victorian State-wide Cladding Audit led by the VBA.

Funding for eligible buildings may be provided to owners corporations to design and implement cladding rectification solutions which comply with the relevant Victorian building regulations and meet the VBA's Cladding Guidelines for Building Surveyors.

To be eligible for funding an owners corporation must be responsible for a residential building that has been:

- assessed as having combustible cladding through the Statewide Cladding Audit, and deemed to be of higher risk;
- subject to a Building Notice or Order related to combustible external wall cladding;
- referred to Cladding Safety Victoria by either the VBA or a local council; and
- prioritised for rectification by Cladding Safety Victoria.

Cladding Safety Victoria will only fund works associated with cladding rectification. Any additional works will need to be financed by the building's owners. The Guidelines provide funding at various stages including:

- Design Stage – pre-works commencement: focuses on developing a rectification solution to establish compliance with building Notices or Orders related to cladding.
- Rectification Works Stage: may provide funding for construction and materials for rectification, in line with the rectification solution, including appropriate disposal of waste material.
- Design and Construct Stage: applies for funding for design, construction and materials may also be provided by Cladding Safety Victoria where a building practitioner is retained to undertake a direct design and construct standard approach to fully remove and replace the combustible cladding from the building.

The Guidelines do not provide funding for any legal expenses incurred by the owners corporation. However, funding is available which is related to cladding works to reduce fire risk and directly related to cladding rectification to address fire safety risks. The costs charged must be reasonable and the solution proposed is cost-effective. In determining what costs are reasonable, Cladding Safety Victoria may consider factors including:

- the complexity of the design and construction of the rectification solution;
- the time and skill involved in the design and construction process;
- any scale of costs that might be applicable to the process; and
- reasonable costs incurred in obtaining quotes for approved rectification work (full removal or Building Appeals Board (BAB) approved solution only), that is, the cost of quoted work for both full and BAB approved solutions.



CLADDING RECTIFICATION LEVY

Effective from 1 January 2020 the Victorian State Government has introduced a proposed Cladding Rectification Levy (applicable to new buildings) to raise funds to assist in rectifying affected buildings in Victoria.

Provisions for the levy were included in amendments to the Building Act 1993 in the Building Amendment (Cladding Rectification) Act 2019 (<https://www.vba.vic.gov.au/news/news/2019/cladding-rectification-levy-to-commence-on-1-january-2020>)."

The levy applies to:

- Building work in metropolitan areas (as defined in section 18(8) of the First Home Owner Grant Act 2000)
- With a cost of at least \$800,000, and
- a classification of class 2 to 8 under the National Construction Code

The levy was established following its proposal in 2019 to generate an additional \$300 million over five years to support the Victorian Government's Cladding Rectification Scheme.

The levy "does not apply to stand-alone houses or other class 1 buildings (ie a boarding house, guest house, hostel, lodging house or backpackers accommodation).

NSW
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NSW

DESIGN AND BUILDING PRACTITIONERS BILL 2019

In October 2019 the NSW Government released a draft of the Design and Building Practitioners Bill 2019 for public consultation. The draft Bill introduces a suite of new reforms to improve the quality and compliance of design documentation and to strengthen accountability across the design, building and construction sector.

The reforms are part of the commitment made by the Government in February 2019 in Response to the Building Confidence Report, authored by Professor Shergold AC and Ms Weir in February 2018 (**Shergold Weir Report**).¹ It is intended that when the Act and Regulation eventually come into force, the reforms will apply to multi-unit and multi-storey residential apartment buildings and certain categories of designs, which will be set out in the regulation. No draft Regulation has been developed as yet.



The draft Bill proposes the following key reforms, including:

- practitioners who prepare regulated designs issue a compliance declaration must declare that the designs comply with the Building Code of Australia (**BCA**).
- Requiring that building practitioners obtain, rely upon and build in accordance with declared designs, and issue a compliance declaration to declare they have complied with the BCA.
- Requiring that any variations to declared designs are prepared and declared by a design practitioner if they are in a building element or performance solution, or in any other case, documented by the building practitioner.
- The draft Bill requires any design, principal design or building practitioner who intends on making a compliance declaration to be registered under a new registration scheme set out under the proposed Bill.
- Clarifying the common law to ensure that a duty of care is owed for construction work to certain categories of 'owner' including owners' corporations and subsequent titleholders. There can be no contracting out of this duty of care. This means that homeowners will have a right to pursue compensation when they suffer damage because of a building practitioner's negligence.

It is mandatory for all design, principal design and building practitioners to have adequate insurance.

The NSW Government has indicated that it proposes to develop and consult upon draft regulations in 2020. The draft Bill once enacted will not apply to existing work or arrangements but only to new works or arrangements entered into after the commencement of the proposed Act.



BUILDING MINISTERS' FORUM

On 18 December 2019 the Building Ministers' Forum the Building Ministers' Forum issued a communique (<https://aib.org.au/building-ministers-forum-131219/>) to progress a national approach to the implementation of the Shergold Weir *Building Confidence* report.

The Forum introduced discussion points on a number of initiatives on building infrastructure including cladding and a providing a coordinated response to professional indemnity insurance. Standards Australia is developing a technical specification proposed for inclusion in the National Construction Code amendment for labelling aluminium composite panels. An Australian Standard for labelling these products will now be developed drawing on the work done to deliver the technical specification.

A meeting of the Building Ministers is scheduled in February 2020 with the Insurance Council of Australia to discuss measures to reduce the cost and improve the availability of professional indemnity insurance premiums for building industry practitioners. The meeting will also be convened with building surveyor and certifier industry associations to discuss implementing plans for establishing a Professional Standards Scheme and raising standards within the industry.

States and territories agreed to achieve greater national consistency with regards to licensing requirements for professional indemnity insurance.

QUEENSLAND
QUEENSLAND
QUEENSLAND

On 3 July 2019 the Government introduced a 3 part compliance process following a meeting of the Ministerial Construction Council:

- Part 1; Buildings to be registered and building owners to complete a cladding checklist by 29 March 2019;
- Part 2: Building industry professional statement completed by 31 July 2019;
- Part 3a: engage fire engineers and register by 31 October 2019;
- Part 3B: complete the building fire safety risk assessment, the fire engineer statement and cladding checklist by 3 May 2021.

The Qld framework provides a considerably longer time frame, compared to NSW and Victoria for the completion of a series of measures to promote fire safety risk assessment and cladding checklist.

In contrast to the Victorian model of a Government sponsored fund and levy, on the other hand, QLD has forged a different path. It requires building owners (and their insurers) to be responsible to rectify their buildings.

PRACTICAL IMPLICATIONS FOR BUILDING OWNERS AND PURCHASERS

The cladding crisis has already have and will continue to affect building owners and purchasers and they face compliance obligations and potential issues with financing cladding remedial work.

TIGHTENING LENDING CRITERIA

It has now become commonplace for there to be a request for the purchaser of a property who wishes to purchase off the plan to produce a certificate or letter to the effect that the building does not use any prohibited materials within the meaning of the *Building Projects (Safety) Act 2017* and that it complies with the cladding requirements.

This is to ensure that the security property over which a mortgage is granted by the prospective purchaser is not at any significant risk of being engulfed in flames. For some lenders, this is a criteria required as precondition to the loan approval. For some buyers it may be seen as an impediment to obtaining a loan approval.

Where building owners were required to register their buildings by 22 February 2019, Qld owners were given an extension until 31 July 2019. Those looking to purchase or refinance buildings in Australia will be impacted by the increasing reluctance of lenders to be involved with properties suspected of containing combustible cladding.

Suggestions for purchasers – include cladding audits in to their due diligence process and review warranties given by vendors to ensure they address combustible cladding risks and that any warranty claim period in a sale and purchase agreement is adequate and a retention agreement for the remediation of non-compliant cladding.

These issues are also likely to have an impact on off the plan purchases of apartments.

PROPERTY OWNERS

In buildings fund to be affected by non - cladding property owners may be claimants seeking to recover their losses from third party professionals service providers or defendants exposed to claims by lessees or visitors.

In addition to undertaking the steps require under legislation, depending on the risk of harm and the cost of taking remedial action, prop owners may owe a duty of care to occupiers and entrants to take reasonable precautions to eliminate or mitigate the risk of identified non conforming cladding products.

Property owners will be required to undertake a risk assessment of their building to determine the level of rectification or precautionary steps required to discharge their duty of care. They may be required to disclose to their insurers any non -compliant cladding, and if so, the steps they have taken to protect against such risk.

A further challenge is that where a fire or damage occurs as a result of non-compliant cladding, the typical insurance cover may offer no cover for rectification costs which can be claimed from professional service providers or others in the cladding industry.



PROFESSIONAL SERVICE PROVIDERS

Following Lacrosse, construction professionals are seeing their PI insurers apply imposing cladding exclusions re comb cladding and seeking to increase premiums to a point where the cost of insurance is prohibitive. This may cause professionals to breach statutory licensing requirements or contractual provisions requiring insurance to be held. Vic and Qld have announced that it will relax statutory requirements to permit certifiers to remain licensed, despite PI cladding related exclusions. Similarly NSW has amended the Building Industry Professionals Regulation 2017 to allow for exclusions to PI insurance. While these steps avoid the construction industry grinding to a halt, professionals potentially remain exposed to legal liabilities that may arise re past projects.

The Building Ministers Forum at its meeting in December 2019 discussed the difficulties faced by industry professionals to obtain cover. Its meeting planned in February 2020 with the Insurance Council of Australia is seeking to improve the availability of premium across Australia. These issues are central to qualified industry professionals obtaining cover for their professional services. Without cover these professionals will exit the industry.

STEPS TO SEEK TO MAXIMISE INSURANCE COVER

Building owners who want to maximise the prospect that the builders and building industry professionals including certifiers, have insurance cover for recovery claims, should immediately place on notice all potential defendants so that those parties can notify their insurers before the insurers apply the exclusions for cladding claims.

The issue with non-compliant cladding is already starting to impact of whether PI insurers offer cover and remain in the market in Australia. Fears have been expressed about whether professional such as building surveyors and certifiers cannot obtain cover free of cladding exclusions.²

CONCLUSION

The changed regulatory landscape has introduced challenges for a number of parties, namely industry professionals, consumers and intending purchasers. The response by the Federal and State governments reflects fragmented versus a uniform approach and sanction versus incentivising compliance.

Cladding task forces have been established in a number of states. However, much remains to be done. The NSW Cladding Taskforce has audited 185,000 building records. At the present time (<https://www.customerservice.nsw.gov.au/programs-and-initiatives/fire-safety-and-external-wall-cladding>) it has inspected 4,127 buildings.

While it has set out a road map for reform including target time frames, it has highlighted different approaches between the States. For example, it remains to be seen whether other States adopt the Victorian model of introducing a compulsory levy to fund cladding remedial work, or allow the market time to address cladding on a self-funded basis.

Certainty and the involvement of qualified construction professionals at all levels is key for all industry players and consumers. It is also vital for the insurance market looking for a coordinated approach at a political level, as a basis to continue providing a safety net via cover for practicing industry professionals and consumers.

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21 January 2020



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