On 25 November 2014, a fire broke out on an eighth floor balcony of the Melbourne Docklands' Lacrosse Apartments (Lacrosse Apartments). The fire spread from the eighth floor balcony up another 13 floors within a matter of minutes. Smoke detection systems, alarms and sprinklers all appear to have performed as intended, and all residents of the building were successfully evacuated, however the fire caused several million dollars worth of property damage.

It later emerged that aluminium composite panels (ACPs) had been used to clad the Lacrosse Apartments to provide a decorative finish. The Metropolitan Fire Brigade’s Post Incident Analysis concluded that the ACPs in question did not comply with the combustibility requirements for high-rise buildings specified by the Building Code of Australia and had contributed to the rapid spread of the fire.[1]

The Lacrosse Apartments was a relatively new complex and, in circumstances where such serious deficiencies had been identified, the immediate question was how many other high-rise buildings in Melbourne (and beyond) were clad with similar non-compliant ACPs?

A Federal Senate inquiry into the use of non-compliant ACPs followed, hearing from Metropolitan Fire Brigade fire safety director Adam Dalrymple that the use of cheap, non-compliant imported ACPs posed a serious risk to the public, that all state building regulators should undertake audits and that, whilst it had once been fair to assume that newer buildings are safer than older buildings “[f]rom a fire services perspective right now, I cannot guarantee that”. [2]

The Victorian Building Authority (VBA) subsequently undertook a comprehensive audit of around 170 high-rise and public buildings in the Melbourne CBD and surrounding suburbs, to determine the rates of cladding non-compliance.[3] The audit’s key findings, released in February of this year, make for grim reading:
of all the building permits audited, the incidence of non-compliant ACPs was found to be 51%;
101 incidences of non-compliant ACPs were published immediately on the VBA website, with the remainder being progressively published on the VBA website after input from building surveyors had been obtained; and
one other building in the Melbourne CBD, in addition to the Lacrosse Apartments, was found to require immediate emergency remediation.

That said, the VBA concluded that none of the other non-compliant buildings identified posed a safety issue requiring immediate action. [4]

As recently as 8 May 2016, ‘The Age’[5] reported that non-compliant ACPs had been identified at the Exo Apartments in Docklands and the Elm Apartments in South Melbourne. In addition, non-compliant ACPs have been located in some of Melbourne’s tallest buildings, including Melbourne’s fourth-tallest tower, the Prima Pearl, the Crown Metropol and Oaks on Lonsdale hotels and Melbourne’s tallest building, Eureka Tower.

Further afield, in February it was reported that occupancy permits had been refused for Iglu’s new student unit building in Mary Street, Brisbane, on the basis that non-compliant ACPs had been used in construction.

Costs of replacement
Replacing non-compliant ACPs on high-rise buildings is an extremely costly proposition and one that poses serious logistical problems. In the case of the Lacrosse Apartments, the cost of replacing non-compliant cladding has been estimated at in excess of $20 million. Who will ultimately foot that bill is far from clear.

The builder of the Lacrosse Apartments initially appears to have suggested that ‘behavioural changes’ could be implemented at the apartments to avoid the risk of fire and render replacement of ACPs unnecessary. Those behavioural changes are said to have included[6]:

- using drones to regulate the incidence of cigarette-smoking by residents and the build-up of clutter on balconies;
- limiting occupancy to two occupants per bedroom; and
- installing additional sprinklers.

These “work arounds” were rejected by the Melbourne City Council (the Council) which has now issued 312 apartment owners with building notices requiring the complex be bought into compliance with Australian building, safety and fire codes - i.e. that the building be entirely reclad.

The builder of the Lacrosse Apartments has rejected the Council’s demands that it replace the ACPs itself, while Melbourne’s municipal building surveyor admitted to apartment owners that he is powerless to order the builder to replace the ACPs.

The cost of replacing cladding on more substantial high-rise buildings will likely run into the many tens of millions.

The implications for the insurance industry
The sheer scale of the use of non-compliant ACPs in Melbourne, and no doubt beyond, suggests that a cluster of high value claims are ultimately likely to emerge as the full scale of
this problem becomes clear. In circumstances where the VBA audit concluded that "[n]o single category of practitioner involved in the design, approval or construction of the buildings audited was consistently responsible for the use of cladding components of external walls that did not comply with the BCA", [7] we would expect claims to be levelled at a broad range of professionals and entities all along the construction matrix - from developers, to architects, to builders and surveyors.

**Disciplinary Action**
The first actions to have already materialised are regulatory/disciplinary actions which flowed from the VBA investigation. Following the publication of its findings, the VBA referred the relevant building surveyor to the Building Practitioners' Board (BPB) on the grounds that he had failed to undertake his work in a competent manner or to a professional standard. The potential penalties, include a fine and/or the cancellation or suspension of the surveyor’s registration. Similarly, the VBA has referred the relevant architect to the Architects’ Registration Board of Victoria (ARBV) for potential disciplinary action. Neither the BPB or ARBV have completed their investigations.

**Inquiry costs**
Professional indemnity insurers providing inquiry costs cover can expect a range of similar disciplinary proceedings to emerge going forward, as the scale of the use of non-compliant ACPs becomes clearer. For Victorians, the VBA has indicated that future audits will include “a focus on the application of the technical advice published by the VBA”. [8] Going forward, developers, architects, builders and certifiers would be well advised to familiarise themselves with such advice published by the VBA. Insurers would also be well advised to confirm that their Insureds have read and understood such technical advice.

For the remainder of the insurance industry, disciplinary proceedings should likely be viewed as a precursor to significant claims for compensation.

**Claims against Builders, Developers, Architects, Surveyors**
In *Burbank Australia Pty Ltd v Owners Corp* [2015] VSC 160, the Victorian Supreme Court concluded that the consumer protection provisions in the *Domestic Building Contracts Act 1995* (Vic) extend to high rise apartments. That Act allows owners to bring claims against builders using materials that were not suitable for their intended purpose or failing to undertake work in accordance with the relevant building standards.

Similarly, owners may have claims against the relevant builder, developer, architect, building surveyor and others involved in the construction process on the basis that they have failed to take reasonable care to ensure that the cladding used on their building complied with the relevant building standards.

A class action has already been mooted on behalf of the owners of the Lacrosse Apartments, and plaintiff firms have been canvassing interest from owners potentially impacted by the use of non-compliant ACPs. Class actions are ultimately commenced on behalf of owners and/or owners’ corporations, the value of such claims will be considerable.

**Contract works claims**
In terms of contract works and project PI policies, there may be issues regarding whether the costs of replacing / rectifying non-compliant ACPs will be covered in circumstances where it may be argued there is no actual physical damage to the cladding itself, but rather it is simply non-compliant with building codes. We would also expect to see faulty products exclusions
coming into play, although some better policies are likely to write back in cover for resultant loss or damage. Finally, faulty design and workmanship exclusions will likely warrant attention.

**Property Claims**

Owners of buildings and apartments clad in non-compliant ACPs face a litany of issues, from depreciation in value, hefty bills for rectification works and potential implications for their property insurance.

Going forward, how owners manage (and notify) non-compliance issues may have a significant impact on their position. For starters, owners of buildings identified by the VBA as defective to date are likely to bear the brunt of increased insurance premiums. Furthermore, evidence that an insured building is not compliant with building codes has the potential to complicate the processing of future claims.

If policy holders become aware of information that materially alters the level of risk they face, they are obliged to notify their insurer. Owners will likely be placed in the position of determining whether to notify their insurers (and being the subject of increased premiums and potentially seeing a decrease in their property’s value) or fail to notify their insurer and face the inevitable consequences in the event of a claim.

**Valuers’ claims**

Another issue which we perceive emanating from the widespread use of non-compliant ACPs is the potential for claims to be levelled against property valuers (either by purchasers, lenders or their insurers) on the basis of negligent over-valuation.

Typically, property valuations of apartments such as the Lacrosse Apartments would be very unlikely to have considered whether or not compliant ACPs had been used in the premises. The presence of non-compliant ACPs is likely to have a significant impact on property values and, in order to ward against claims of professional negligence, going forward property valuers would be well advised to:

- consider whether a building or apartment being valued has previously been identified as having non-compliant ACPs (by way of a review of the VBA website for example); and
- where possible, obtain a materials certificate from the relevant builder to ensure that reputable and compliant materials have been used in construction.

**Conclusion**

The issue of non-compliant ACPs certainly has a long time to run yet, and it would seem to be only a matter of time before claims, and likely litigation, begins to follow.

While we are yet to see it in the market, we expect that underwriters will begin seeking to limit their potential exposure across a range of policies for claims arising out of non-compliant ACP type claims by expressly excluding such cover from policy wordings. Given the size of claims likely to emerge in the future, we would also expect insurers to seek to work closely with construction companies, developers and professionals in actively managing the inevitable rectification of buildings clad with non-compliant ACPs.

[1] LU Simon Builders’ Managing Director, Peter Devitt, told Fairfax that the ACPs “complied with Australian standard tests for ignitability, spread of flame, heat and smoke, but that it, like all other aluminium composite panels, did not pass the test for combustibility back in 2010 when the Building was commissioned” (http://www.architectureanddesign.com.au/news/non-compliant-cladding-fuelled-melbourne-25-MAY-2016)
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