Unravelling Risk

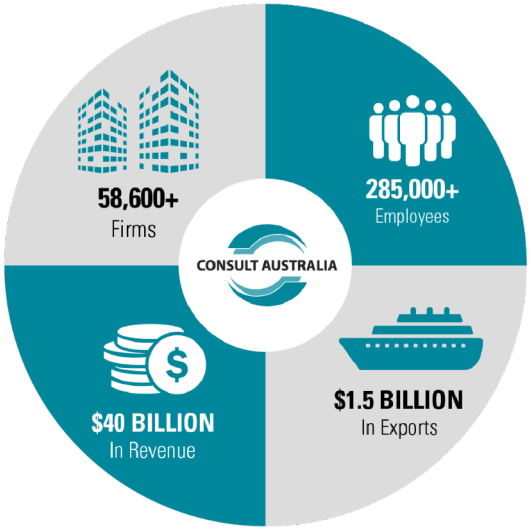
Reforming the design, construct & litigate cycle

CONSULT AUSTRALIA

About us

Consult Australia is the industry association representing consulting businesses in design, advisory and engineering.

For more than 70 years, we have championed this sector. Our members, ranging from Australia's most innovative small and medium sized firms to global corporations, deliver the solutions to the nation's most complex challenges helping shape, create and sustain our built and natural environment.



Our vision is for a thriving, competitive consulting industry that supports a prosperous economy and better outcomes for our members' clients including for governments and the communities they serve.

Consult Australia's advocacy is proudly member-led and this paper is no different. Sincere thanks to the many member representatives who had a hand in this paper and in the background claims data that propelled this paper forward. A full membership list is available on our website.

Centre for Contracting & Risk

This paper reflects Consult Australia's focus and depth of experience over 70 years on critical contracting and risk issues.

The Centre for Contracting & Risk brings together advocacy, education and empowering resources to help industry and government navigate the challenging interplay between contracts, risk and professional indemnity insurance.

INDUSTRY CONSULT AUSTRALIA CHAMPION

AECOM aurecon smec an SNC company

Jacobs GHD Stantec

COLLABORATIVE LEADERSHIP COMMITTED TO THE SUCCESS OF OUR INDUSTRY

We acknowledge the Traditional Custodians of the land on which we work and live which includes the lands of the Gadigal, Kaurna, Turrbal, Whadjuk and Wurundjeri people.

We pay our respect to Elders past and present.

About unravelling risk

This paper is for strategic leaders across government and the construction industry who want a productive industry underpinned by a collaborative culture where model client behaviours are the norm.

With projects growing more complex over time, the knotty issue of risk has become more important, but with no improvement in our management of risk. This is seen most starkly in design and construct contracting, which often results in a design, construct and litigate cycle.

Consult Australia proposes five reform threads to unravel the current situation, all underpinned by collaboration and transparency: scoping for success, valuing variations, transparent timing, refining the rules and resolution over disputation.

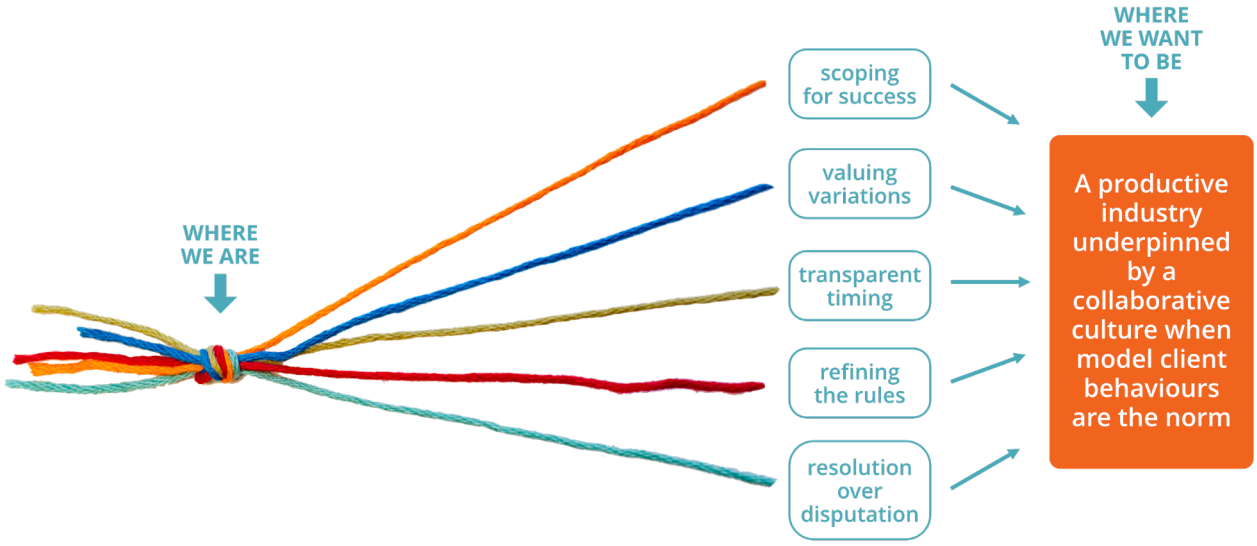


Figure 1 – Consult Australia recommends that unravelling the risk knot requires pulling on five reform threads to untangle the knot and get to where we want to be.

Every party has a role to play. As a solutions-focused voice for the consulting sector, Consult Australia is keen to work collaboratively with our colleagues in the broader construction industry and the government to realise the proposed reforms. We have demonstrated this commitment through both our thought leadership (from our Model Client Policy to this paper) and our submissions to government reviews and inquiries.

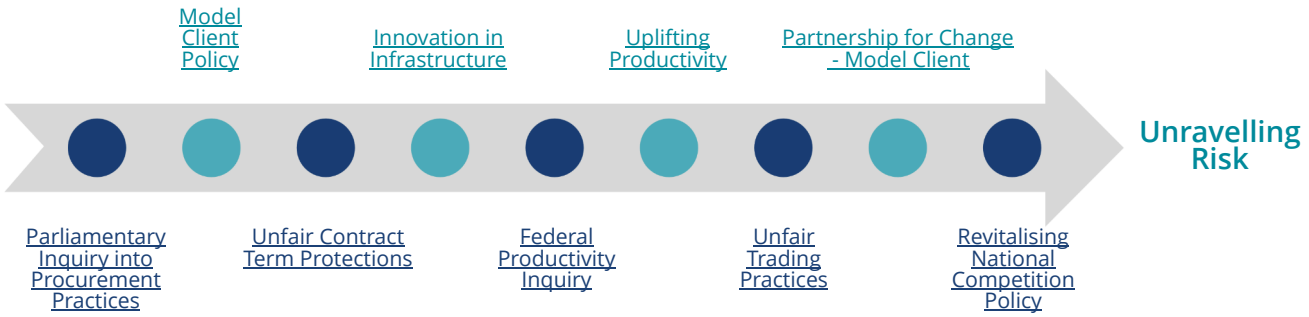


Figure 2 – Between 2018 and 2024, Consult Australia's solutions-focused advocacy on procurement and risk has been showcased in key thought leadership pieces (above the arrow) and in submissions to Commonwealth Government reviews and inquiries (below the arrow).

The knotty issue of risk

The culture of disputation in the Australian construction industry is becoming more entrenched – the talk of collaboration and risk-sharing is not translating into change. Is it just because projects are becoming more and more complex? Or are there so many issues tangled up, we don't even know what we mean by risk?

The push-pull of political pressure, inappropriate contractual and regulatory settings, unrealistic and inflexible budgets, the inappropriate pass-down of risks, capacity issues and the current spate of collapsed construction businesses are all symptoms of and contributors to an increasingly 'risky' environment for all parties.

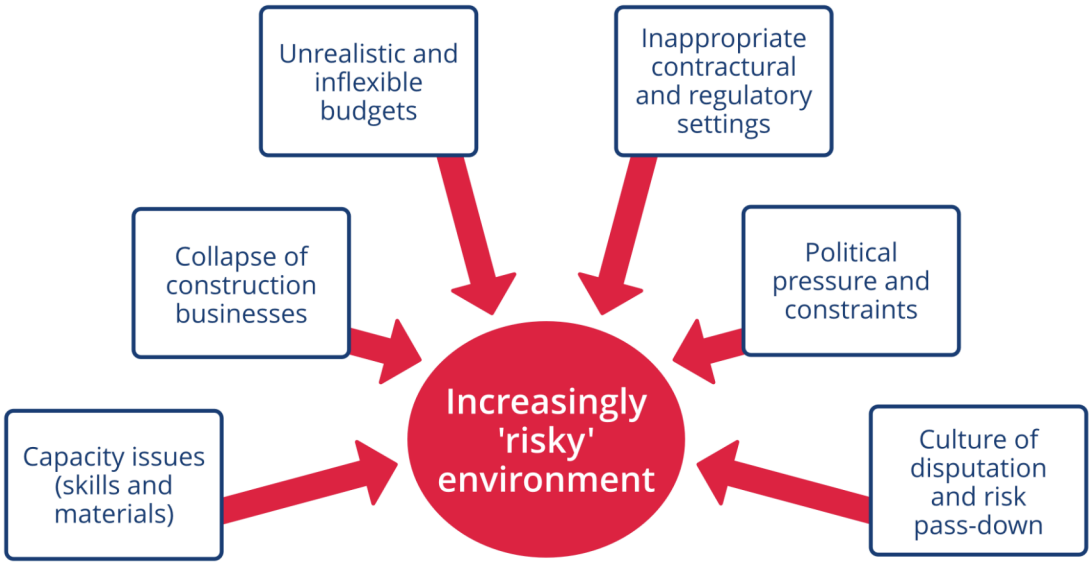


Figure 3 – There are a myriad of issues that lead to an increasingly 'risky' environment to deliver building and construction projects in Australia.

Risk underpins the current predicament – but what is risk?

The confluence of 'risks'

When we talk of a 'risky' environment what do we mean? Risk can be categorised in a myriad of ways; inherent vs residual risks, financial/environmental/legal/safety risks. Further, each party will be concerned about risks relevant to their situation. For example, government clients need to be aware of the risk to the public purse as well as political and reputational risk. For private sector businesses commercial risks and insurance risks need to be considered to keep the business viable.

The problem with the confluence of risks is that it becomes very easy to do 'performative risk management' – that is justifying an action as necessary because of the 'risk' of the project, even though the action doesn't impact any risk of the project.

Consult Australia often hears the cry of 'risk' as the justification for uninsurable and problematic contract clauses and unreasonable insurance requirements. Often the contract clause just increases the liability of one party but does nothing to manage a particular risk.

The conflation of liability and risk management likely happens because lawyers draft the contracts but are less involved in the project. It has been noted that while other professions, such as engineers, quantity surveyors and project managers have identification, assessment and management of risk as essential competencies, this is not the case for lawyers.[1]

What is performative risk management?

Performative risk management includes where a client conflates liability for a potential risk with an action that manages that risk.

Having unlimited liability in a professional services contract does nothing to manage the risk of a design error but it does tend to make the contract less commercial for the business supplying that service and make that business an insurance risk for their insurer.

Risk items

'Risk' is too often used as a collective and unspecified term. For example, industry's appetite for risk can be influenced by recent experience and market conditions - as explored in A National Study of Infrastructure Risk by Infrastructure Australia.

Parties need to be specific about which risk/s are relevant to the project and then how to balance the exposure of each party - including whether to manage the risk or transfer the risk. To assist in defining and specifying risks, let's talk about 'risk items'. Risk items can include:

- Aboriginal culture and heritage
- authority approvals
- escalation
- geotechnical
- heritage
- industrial disruption
- latent conditions / inground services
- stakeholder engagement
- supply constraints
- weather.

Each risk item will have a cost, time and likelihood component. What is needed is careful consideration by the parties of each risk item up front, with clients undertaking a cost/benefit analysis on minimising each risk item. For each risk item, the client should decide if it is worth continuing with a project with the current settings, or whether action should be taken to reduce the risk item/s with the highest cost/time/likelihood.

In practice, we see little attention to risk items and contractual settings that result in the supplier paying for the impacts of risk items arising without that risk being properly priced or even considered.

FOR EXAMPLE

A geotechnical risk item on a project is noted as having a potential cost impact of $20m, a significant impact on time and a high likelihood of arising.

It is recommended that the client undertake a cost/benefit analysis to determine if it should:

(a) take action to reduce the risk item – this might mean a delay to the project so that more investigations of the ground conditions can be done to lessen the cost/time/likelihood of a geotechnical risk item impacting the project. This is managing the risk item.

OR

(b) agree to carry the risk item – this means the client will pay for the impacts arising during the project because of the geotechnical risk item. It is noted that the risk item may not eventuate or might have a different cost impact than the estimated $20m. This is not managing the risk, but this is balancing the exposure of the parties to the risk item.

OR

(c) agree to pay the supplier $20m to carry the risk – this means the supplier will pay for the impacts arising during the project because of the geotechnical risk item. It is noted that the risk item may not eventuate or might have a different cost impact than the estimated $20m. This is not managing the risk, but this is balancing the exposure of the parties to the risk item.

Is engineering risky?

'Engineering is risky' is an easy throwaway line, too often used to justify clauses in contracts for engineering services that increase liability and commercial risks, but do not manage risks.

Risk is a critical part of engineering practice. Engineers are required to identify potential risks, assess the likelihood and impact of risks, and mitigate them to acceptable levels.

Engineering/design errors by qualified and experienced designers can occur for many reasons including incorrect assumptions or incomplete information and miscommunication of design intent. These reasons cannot be eliminated via contractual clauses that penalise the engineer. Instead, communication is the key. Designers need to know who to communicate with (owners, operators, contractors, and construction staff) to confirm assumptions and ensure complete information and design intent.

Insurance risks

Like any other business, insurers seek to avoid significant and continual losses. The willingness of an insurer to offer adequate and affordable insurance to a consultant is not only based on its claim history but also on the performance of that sector of the insurance market.

The 'indicative profitability threshold' for professional insurance (PI) insurers is a gross loss ratio of around 70% (as indicated by the blue line in the graph below). Where gross loss ratios are higher, insurers will need to modify their policies (through coverage limitations and policy exclusions) as well as refuse cover to certain businesses or disciplines/sectors.

The unprofitability of the general PI insurance pool has been of concern for many years, for engineering occupations we have seen unprofitability since around 2013, with the highest gross loss ratios seen around 2018 (at around 133%).[2] While there has been some improvement recently for some sectors, for engineering occupations the gross loss remains high.

Why PI insurance availability and affordability matters

Without PI insurance, consulting businesses cannot operate. Many professional registrations and licences require the consultant to hold PI insurance to provide services.

We see high-profile construction insolvencies covered in the media, but what is hidden is the increasing risk of consulting businesses unable to secure affordable PI insurance.

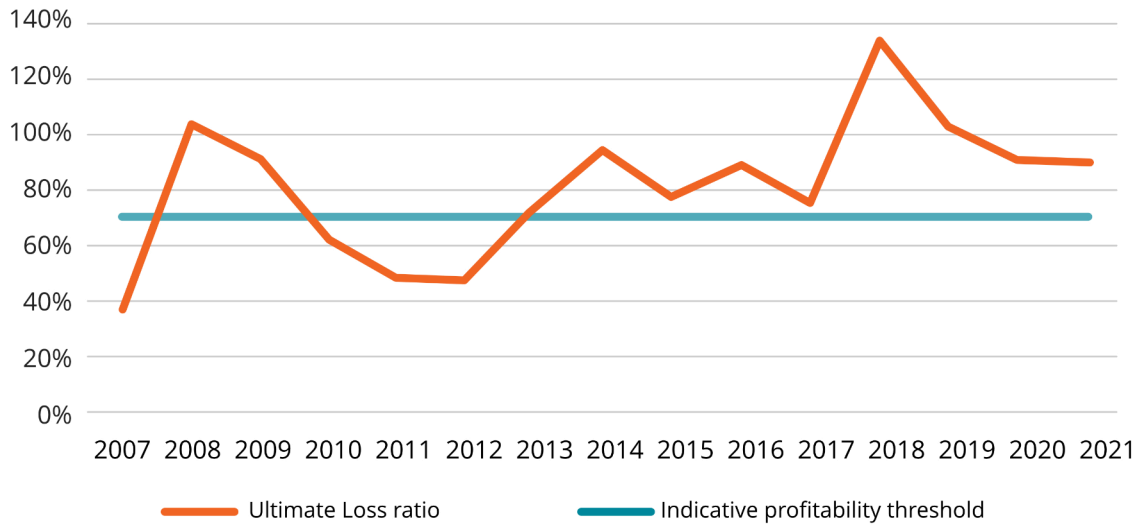


Figure 4 – Engineering Occupations Gross Loss Ratio for PI Insurance in Australia

More recent data shows a rapid expansion and return of capital for construction professionals generally.[3] There is increased appetite across a range of professions. Unfortunately, this appetite does not extend to diminish the concerns insurers have about activities and disciplines including complex infrastructure projects and design and construct projects.

The current buoyancy in the market will not be long-lived unless we tackle and reduce disputation.

Design, construct and litigate

Disputation in the Australian market falls heavily on consulting design, advisory and engineering businesses, which are paying the price of unfair and uncommercial risk allocation – especially in the design and construct context. When contracting directly with the government, consultants put significant trust in the fact that all governments are Model Litigants. Private sector clients are not under the same obligations, and it is in this environment Consult Australia members see the most egregious claims.

There is significant literature on poor risk allocation in Australia with industry and government agreeing that things need to change. This includes the 2022 Government Procurement: A Sovereign Security Imperative – the final report into the Inquiry on the Procurement Practices for Government-Funded Infrastructure. This report made recommendations aligned with Consult Australia's advocacy on procurement, risk and reform. Consult Australia was quoted heavily throughout the report, but we have seen limited action from any level of government to realise the inquiry recommendations.

Australia's construction industry has a reputation as being marred by adversarial, problematic and uncollaborative contracting arrangements. We see inappropriate and uncommercial risk allocation, especially within the design and construct (D&C) contracting model. This view is held not only by those within the industry but also by the international insurance markets which view operating in Australia as a high risk.

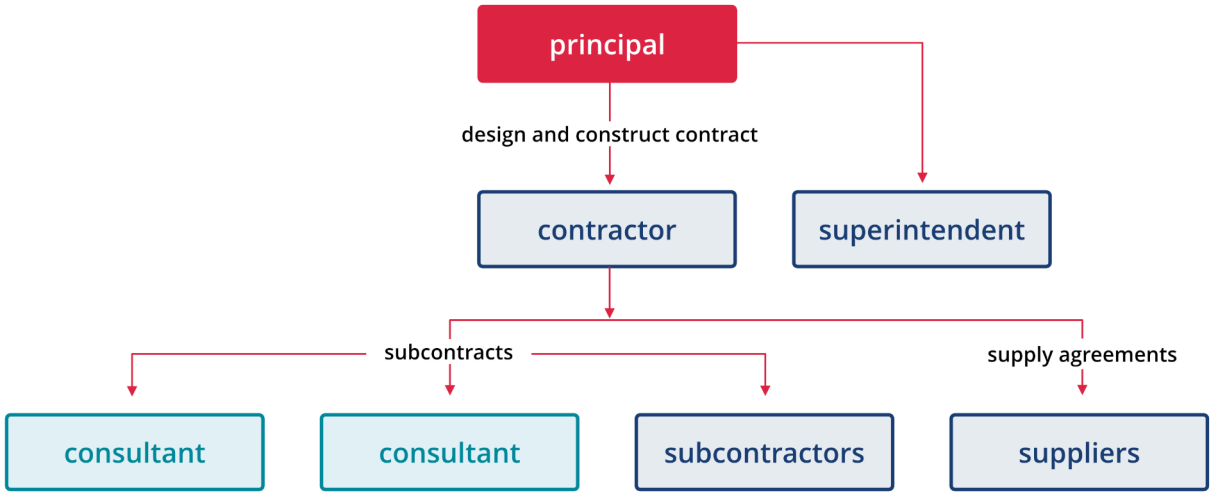


Figure 5 – The typical design and construct contractual relationship matrix.

Consult Australia members expect to be held liable if they have been negligent or breached contract. In the D&C model it is expected that claims by government principals against constructors will flow down proportionally to consultants where the consultant is in some way responsible for the loss.

However, the levels of claims against consultants by private sector clients in the D&C environment are rarely linked back to government principal claims and rarely proportional to the services supplied by the consultant. Most claims are not for actual losses caused by defect rectification in the end-product. The prevalence of these unreasonable claims in D&C means that the model is no longer design and construct, but rather design, construct and litigate.

Claims data

> *"Australia's construction industry remains under public and legal scrutiny with claims activity steady."*
>
> - Bellrock Advisory[3]

Getting to the heart of claims is in everyone's interest, to avoid future claims. HKA has regularly reported on claims through its Annual CRUX Insight Reports, with the data searchable through the interactive CRUX Dashboard.[4] The latest data reveals the top five reasons for claims and disputes on major infrastructure and capital projects both globally (across 2,002 projects) and regionally including for Australia (across 153 projects):

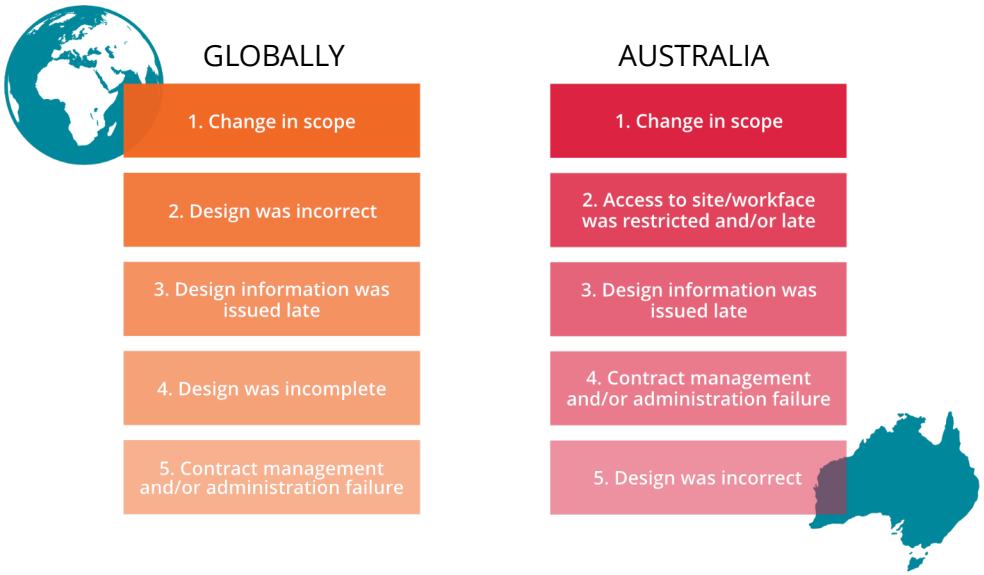


Figure 6 – The top five reasons for claim both globally and for Australia according to HKA's CRUX data.

HKA's findings accord with Consult Australia's own collected claims data on D&C projects which reveals that in 158 projects subject to a claim against the consultant, the reasons given centre around the areas of 'scope', 'delay' or 'design'. Our members also report a rise in misleading and deceptive conduct claims in the past five years, arguably as an ambit claim.

Consult Australia's data indicates that design consultants are bearing a significant burden when compared to their gross revenue, with the quantum of claims against the overall construction cost relatively small therefore hiding the true impact. This might explain why the principal clients have not been forced to confront this issue. Despite the focus by government clients on value for money, claims are a substantial drain on consultants, driving a culture that is contrary to value for money outcomes.

Consult Australia claims data demonstrates that there is significant wastage to the economy, particularly as the significant proportion of the claims against consultants in the D&C model is the result of noticeable back-to-back pass-through of risk. Therefore, to address unreasonable claims against consultants, not only do we need reform to limit avenues of unfair claims we also need to deal with the underlying risk issues impacting the health of the whole ecosystem.

Scope certainty vs scope creep

Change in scope is reported by HKA as a leading cause, both globally and locally, but is a notably higher cause for claims in Australia (51.0%) than globally (36.9%). Consult Australia's data noted scope as a cause for claim in around 29% of D&C project claims considered.

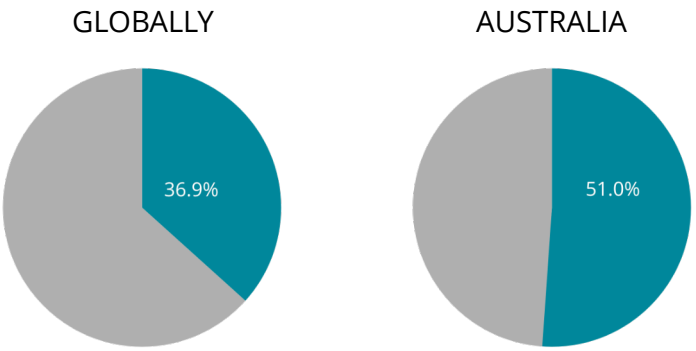


Figure 7 – The percentage of claims both globally and for Australia attributed to change in scope according to HKA's CRUX data.

Claims in respect of scope often relate to where the scope has changed over the life of the project because it was not well defined at the commencement. The tendency for projects to go to market without proper scope is more likely for government-funded projects when there is political pressure to announce early with details (such as cost) that haven't been fully developed. Scope creep/change is also a regular occurrence on highly technical and complex projects with long timelines.

The 'design error' misnomer

Design error is reported by HKA as a leading cause of claims, globally at 21.5% and locally at 19.0% for Australia. In the Consult Australia data, design errors were attributed to over 52% of the D&C project claims considered.

On the face of it, a designer should be held liable for a design error and this is a matter that is generally covered by a consultant's PI insurance policy (where error can be attributable to negligence). However, Consult Australia holds that a significant proportion of these 'design error' claims do not represent actual loss caused by design, otherwise, we would see significant defect rectification occurring in the end-products of these D&C projects.

Consult Australia notes that many of the design error claims can be linked to quantities growth between the tender design phase and the final design phase, invariably due to factors beyond the consultant's control (e.g. changes in scope). This accords with HKA's findings that 'design failures…are often symptoms of other pressures, including political commitments to delivery dates, and provisional costings'.[5]

Consult Australia members also note that fitness for purpose obligations, which Consult Australia notes in its Model Client Policy are not appropriate for consultants, is another area allowing unreasonable 'design error' claims to be made.

Timing

Consult Australia data indicates that claims for delay occurred in over 21% of the D&C projects considered. Claims in respect of delay arise against a consultant in a D&C model because consultant timeframes are significantly impacted by other parties. This is despite the fact that timing is often beyond the consultant's control, and reliant on actions by other parties.

Claims for delay are more frequent when programming is a contractual clause requiring strict compliance. This can limit parties working together to resolve issues to get the project 'back on track'.

The ambit claim – misleading or deceptive conduct claims

Data from Consult Australia members demonstrates that private sector business clients are increasingly using misleading or deceptive conduct claims under the Australian Consumer Law (ACL) in addition to breach of contract and negligence claims. We hold that claims are being made tactically to increase the pressure on members to settle regardless of wrongdoing, noting that increasing the heads of claim made against a consulting business significantly increases the cost of defending such claims. It is also important to note that there is no clear precedent as to whether a contractual limit of liability could be relied upon to limit the liability exposure in the event of a misleading or deceptive conduct claim.

The issues raised in claims for misleading or deceptive conduct against consultants rarely involves marketing or promotional activities (e.g. bait advertising) but is based on the same facts as claims for contractual breaches or breaches of the professional standard of care (negligence). This demonstrates that claims for misleading and deceptive conduct are being used as a 'catch all' to escalate the log of claims even though the contract and common law provides for appropriate remedies without the need to resort to the ACL. The misleading and deceptive conduct claims infrequently make it to court demonstrating that these claims are being used to pressure the consultant into settling, rather than face the costs associated with defending such claims.

The impact of claims on professional indemnity insurance

Design and engineering consultants rely on PI insurance to cover claims of negligence, malpractice, or professional misconduct. It costs time and money to defend these types of claims, and a PI insurance policy provides cover against such claims as well as legal defence costs. A PI policy is intended to provide a business with the ability to settle a claim without jeopardising the entire business (depending on the size of the claim and the sum of insurance held).

Allianz recently published its PI insurance claim insights looking at large loss claims, that is claims above $US1m/€1m. It showed that after the legal profession (at 30%), construction professionals make up 27% of large loss PI claims, with a further 4% for architects and engineers outside the construction sector.

Allianz considers there is a high-risk of an increase in high-profile litigation having a major impact on operations or loss severity. The claims data above shows clearly the link between the claims levelled against consultants in the current environment where the design, construct and litigate cycle is becoming entrenched.

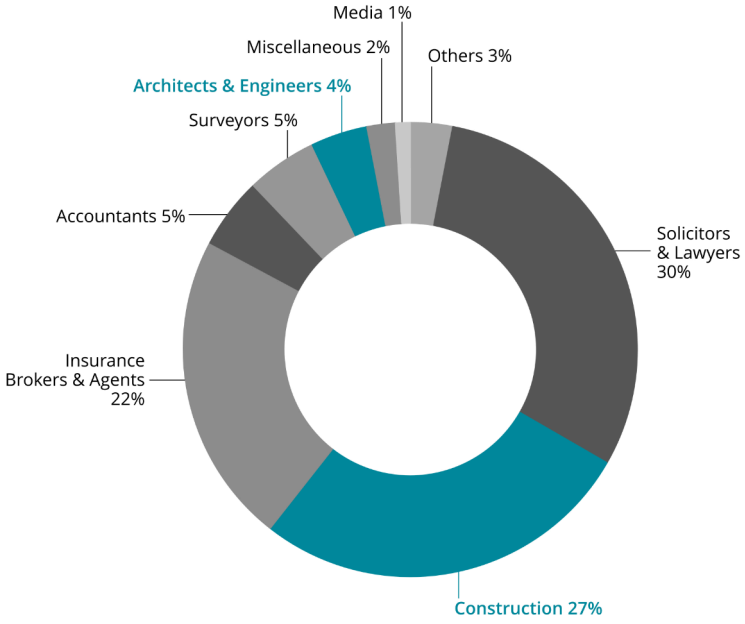


Figure 8 – Breakdown of large loss claims (above $US1m/€1m) against professional indemnity insurance, by profession according to Allianz Commercial. Based on an analysis of 477 professional indemnity claims. From Allianz's Professional indemnity insurance claims insights 2023.

What role, if any, is there for project-specific insurance?

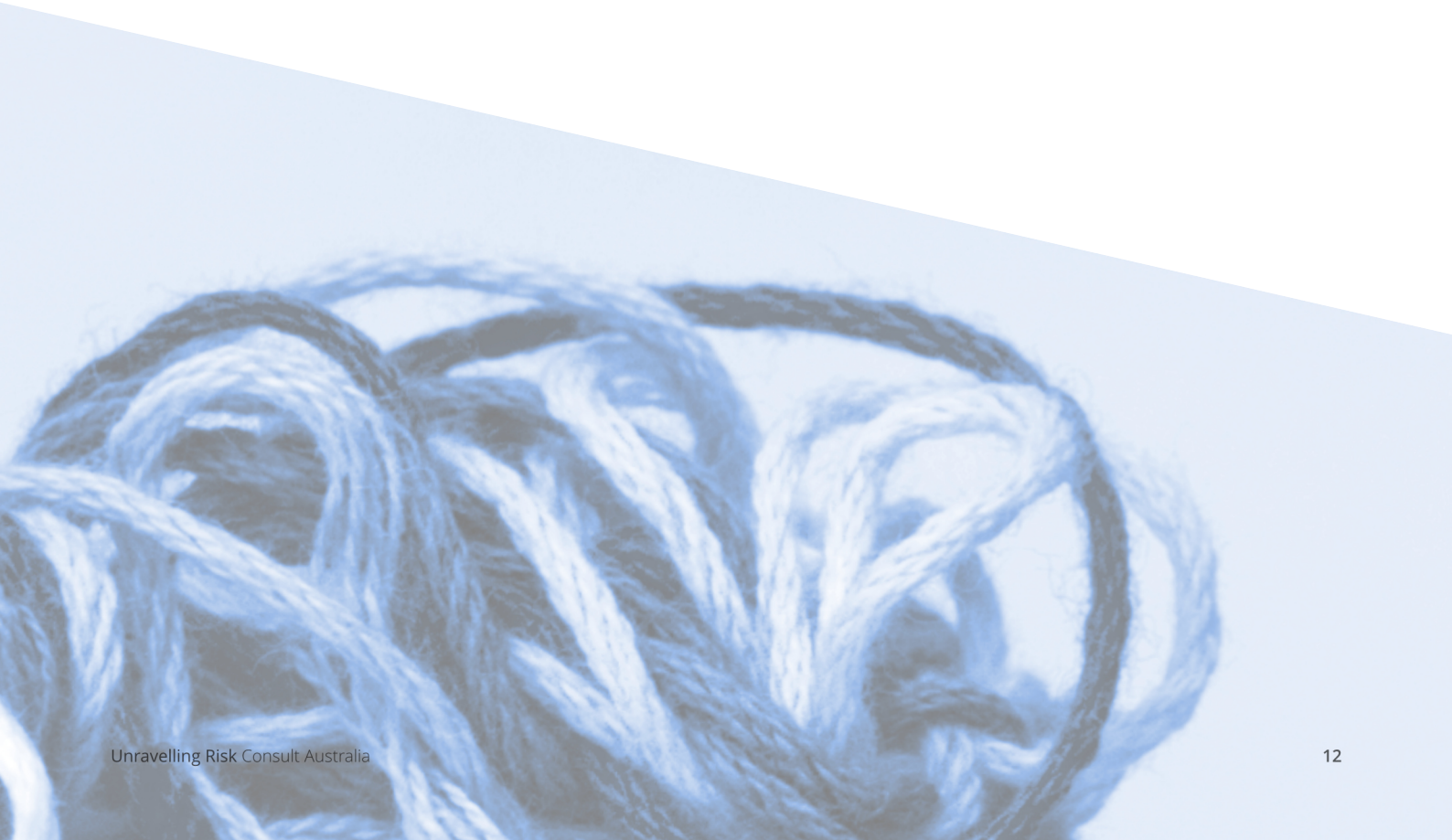
When it comes to major projects with multiple parties, there is a role for project-specific PI (PSPI) or principal-acquired insurance. This is also known as 'wrap-up' insurance where it covers a range of insurances. 'Wrap up' insurance seeks to address the disadvantages of different parties having their own insurance, including the lack of transparency about what was covered and the potential coverage gaps.

> *"Contractors, subcontractors and consultants need to understand the framework of the insurance placement in relation to such projects, and design their contracts to align with the overall project placement. Such projects are often arranged by State or Federal governments on a "principal arranged" basis. Such cover would include material damage, liability and in some cases, project specific professional indemnity."*
>
> – Bellrock Advisory[3]

Unfortunately, PSPI insurance has seen significant contraction over the past five years or so. Consult Australia members report that even when principal-acquired insurance is offered now, it often falls short for consultants. For example, it is usually:

- unclear what coverage, if any, is provided for design services under the policy
- unclear which party is responsible for the excess
- likely that consultants will need to rely on their corporate policies
- where there is a gap in the deductible of the principal-acquired insurance and the consultant's corporate policy an endorsement for each project (or a blanket endorsement) will be required.

> *"The principal-acquired insurance is close to useless for our business and the services we are providing for the project."*
>
> – Consult Australia member



Reform threads

> *"Modern megaprojects are increasingly complex, but the cruel conundrum for the global construction and engineering industry is that these most common causes of claims and disputes are highly predictable and largely within the control of the contracting parties."*
>
> – Renny Borhan, Partner and CEO - HKA[5]

The increasingly complex risk landscape and an adversarial culture has resulted in us not being where we want to be. This is reflected in the claims data. Consult Australia proposes pulling on five reform threads to unravel the risk knot and get us to a collaborative contracting environment: scoping for success, valuing variations, transparent timing, refining the rules and resolution over disputation.

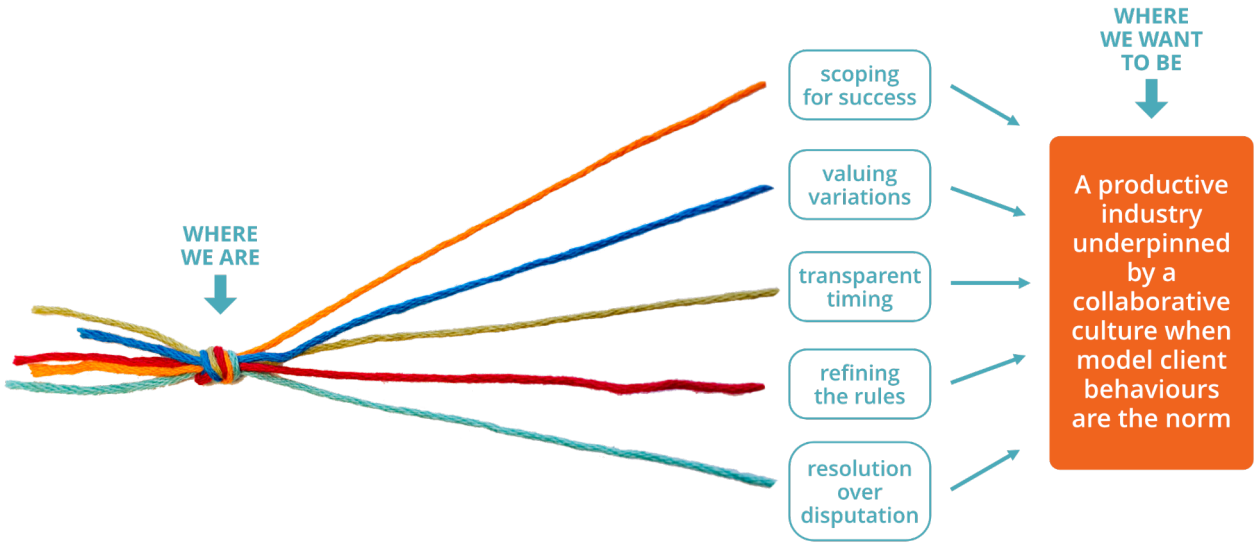


Figure 9 – Consult Australia recommends that unravelling the risk knot requires pulling on five reform threads to untangle the knot and get to where we want to be.

Scoping for success

Collaboration and transparency between parties at the earliest stages of project and program scoping could deal with a significant volume of unnecessary claims.

There is sometimes a disconnect between consultants and clients when it comes to scope, this is what we've heard:

WHO & HOW

Clients need to lead on 'scoping for success' by:

- conducting early engagement with *the industry* for feedback on the proposed project and/or
- engaging a *consultant* to reverse-engineer a project brief.

In the D&C contracting environment, it is very difficult for a consultant's concerns about scoping documents to be communicated with principal clients, as they operate at arms-length. Therefore, we need to rethink how we approach scoping. We need government and industry to work together to scope for success, and to dispel any misapprehension of what is driving the behaviour of other parties.

While scoping a project is a case-by-case exercise, there are several common components:

- an outline of the broad objectives of the client to be realised through the project
- specific project requirements, such as functional outcomes or benchmarks to meet the broad objectives
- background information, including specific project risks
- contractual method for delivering the project.

The best quality scope has:

- input from a wide range of stakeholders (including consultants and contractors) through industry briefings and/or engagement of a consultant to reverse-engineer a project brief
- realistic timeframes and budgets
- an appropriate amount of verified background detail
- clarity that can support appropriate risk allocation.

Valuing variations

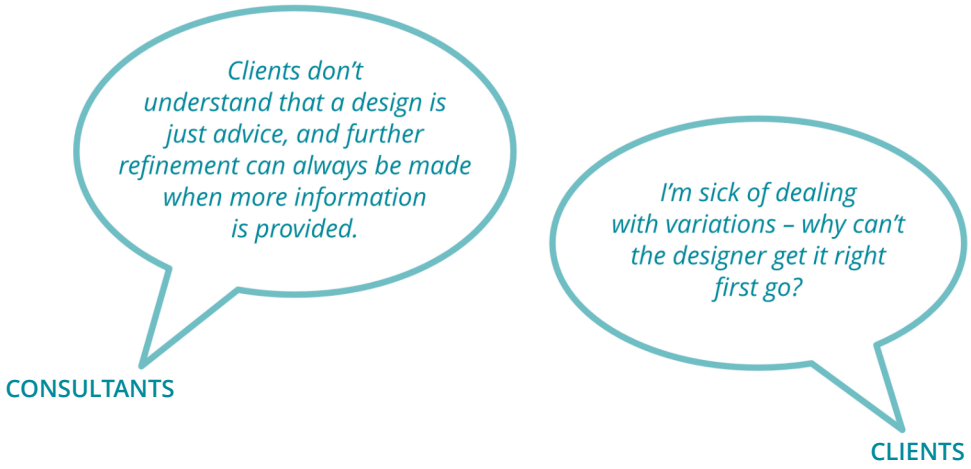
A variation is when a change is made to the original design after a contract has been signed.

There are many reasons why a change becomes necessary, it could be to deal with hidden problems that were not known before.

WHO & HOW

All parties should commit to an early warning process to deal with potential variations (without any blame game).

Unfortunately, in the current environment, there is a tendency towards a 'blame game' between parties, this is what we are hearing:



Variations can be required to deal with:

- unforeseeable circumstances arising in the project
- shifts in the needs or outcomes sought by the principal client
- changes to qualifiers and/or assumptions made at the outset
- increased clarity on essential aspects of the services, including specifications after the contract is signed.

Many of these aspects can be resolved by 'scoping for success' at the outset. For the remaining variations, all parties should avoid the blame game and value the variation process because variations should be about achieving the best outcome for the project. A good starting position is for all parties to be transparent about issues arising that might lead to a variation – in this respect the 'early warning' approach in the NEC4 contracts is a good way to deal with variations in a more collaborative rather than combative way – see the case study below.

Transparent timing

Complex projects require a better way of managing time than deadlines in party-to-party contracts that attract strict liability.

In complex projects, it is not always clear where the delays originated and the resultant flow on impacts. More transparency and better coordination is needed.

WHO & HOW

Clients should ensure there is an agreed program for each project that is a working tool for *all parties.* There should be clear processes for the program to be amended in collaboration between all parties.

Consult Australia intentionally avoids references to programs, timelines, and deliverables in our Contract Suite. This is because strict liability for contractually embedded timelines can conflict with the ability to deliver the services with the appropriate skill, care, and diligence. Also, as demonstrated above, can often lead to disputation between the parties. Further, consultants may not be able to access PI insurance to cover a liability

arising from a provision focussed on program, timeline, or deliverables because the insurer could consider this as going beyond the common law duty or standard of care.

Prioritising collaboration and transparency to deal with issues and resultant delays – instead of penalising parties for changes to the program would alleviate claims and improve outcomes for all parties. The approach in the NEC4 contract suite is a relevant case study.

CASE STUDY – NEC4 Contracts – Early warning and programming

The NEC4 Contract Suite makes the program not only a contract document but also a working tool, to be used by the parties to evaluate progress and to calculate any extension of time granted.

This is combined with the 'early warning process' which is to many users, the 'jewel in the crown' of NEC4 Contracts. Under these contracts, if either party becomes aware of any matter that could affect time, cost or quality, they are required to notify the other party immediately. This is promptly discussed at an early warning meeting to decide how best to mitigate the risk and to decrease the time taken to resolve the issue.[6]

If there are changes to the amount of work the supplier has to do, there are clearly defined processes to handle changes in costs and time called 'compensation events'. The contracts also provide a clear and precise process for evaluating the cost and time implications of compensation events, which include events arising from client scope changes. There is also a process to deal with delays in assessing such events. Therefore, programs and budget are continually updated and agreed as changes and events happen.

THE NEC4 CONTRACT SUITE

The NEC4 Contract Suite offers a comprehensive range of flexible contracts for procuring works, services and supplies. Many contracts have more digestible short versions for smaller projects, and specific forms for engaging subcontractors:

- Alliance Contract (ALC)
- Design Build and Operate Contract (DBOC)
- Dispute Resolution Service Contract (DRSC)
- Engineering and Construction Contract (ECC)
- Facilities Management Contract (FMC)
- Framework Contract (FC)
- Professional Service Contract (PSC)
- Supply Contract (SC)
- Term Service Contract (TSC)

Refining the rules

Clarifying and refining how current legislative provisions are framed and used would reduce the volume of unnecessary and unreasonable claims. This includes:

- modifying the availability of misleading or deceptive conduct provisions of the ACL in line with other provisions to guarantee protection for consumers and small businesses.
- modifying civil liability laws in all states and territories, except Qld to explicitly prohibit contracting out of proportionate liability.
- championing the explicit exemption for professional engineers and architects from the fit for purpose consumer guarantee in the ACL and reflecting that position in contracts for professional services.

WHO & HOW

Government competition regulators should work together to modify the Australian Competition Law to ensure no further misuse of misleading or deceptive conduct provisions.

ACT, NSW, NT, SA, Tas, Vic and WA governments should amend their civil liability laws to explicitly prohibit contracting out of proportionate liability.

Clients should ensure there is no fit for purpose warranties in professional services contracts.

Misleading or deceptive conduct provisions

The ACL is designed to protect consumers and small businesses. Yet, the misleading or deceptive conduct provisions are being misused by sophisticated contracting parties, Consult Australia argues, as an ambit claim. We hold that such contracting parties have sufficient protections under the contract, the common law and other statutory rights and obligations.

Therefore, the rules need refining to ensure consistency with the rest of the ACL.

CONSULT AUSTRALIA'S PROPOSED REDRAFTING OF SECTION 18 OF THE AUSTRALIAN CONSUMER LAW:

18 Misleading or deceptive conduct

(1) A person must not, in trade or commerce, engage in conduct that is misleading or deceptive or is likely to mislead or deceive a consumer or a small business.

(2) A consumer for the purposes of subsection (1) is an individual whose acquisition of the goods, services or interest is wholly or predominantly for personal, domestic, or household use or consumption

(3) A small business for the purposes of subsection (1) is a business that:
  (a) have fewer than 100 employees; or
  (b) makes less than $10 million in annual turnover.

(4) Nothing in Part 3-1 (which is about unfair practices) limits by implication subsection (1).

Note: *For rules relating to representations as to the country of origin of goods, see Part 5-3.*

The benefits of this refinement include:

- The protection for small businesses and members of the public in their capacity as consumers is maintained.
- Sophisticated parties will no longer be able to misuse the ACL.
- There will be no detriment to contracting parties given the availability of appropriate contractual and common law remedies.
- It will de-risk the Australian PI insurance market.
- It will provide greater certainty for contracting parties about liability in the event of a claim, as actions would be limited to contractual and common law actions.

Civil liability laws

Proportionate liability is a statutory right, which ensures that a party is only liable in damages for the proportion of the suffered loss that is attributable to that party. It only applies to financial harm and economic loss, not to cases involving personal injury or death. Proportionate liability was introduced nationally through state and territory civil liability legislation to improve the availability and affordability of PI insurance in Australia following the insurance crisis of 2001 when the insurer HIH collapsed.[7]

Contracting out of proportionate liability opens a party to be liable in damages for more than is attributable to their acts/omissions. This could also attract more spurious claims, once again another pressure tactic used in a market rife with disputation.

The key policy objective of proportionate liability – helping to ensure that PI insurance is available, affordable and dependable – is undermined if design and engineering consultants that rely on PI insurance, are required by a client to contract out of proportionate liability. Only Qld's legislation explicitly prohibits contracting out of proportionate liability. Consult Australia suggests that all other jurisdictions should include similar prohibitions, even if only related to professional services contracts.

Resolution over disputation

The resolution of issues rather than disputation is best for project, relationship and business outcomes.

The reforms above will assist in avoiding disputes. However, there will never be a project without issue – therefore we need ways to resolve potential disputes instead of continuing the cycle of disputation.

WHO & HOW

Clients should incorporate standing dispute boards which actively include the project consultants on all design and contract projects.

Standing dispute boards on projects (see case study below) is a potential circuit breaker in the design, construct and litigate cycle, if extended to include consultants.

CASE STUDY – Dispute boards

The International Federation of Consulting Engineers (FIDIC) is the global representative body for national associations of consulting engineers and its standard contract suite adopts a 'multi-tier dispute resolution mechanism' which is designed to avoid disputes or to resolve them as early as possible, ideally during the currency of the project. A key feature of this is the dispute board.[8] A standing dispute board is established at the start of a project, populated by independent experts who help facilitate the parties' avoidance of disputes. Where that is not possible, the experts engage in the expeditious, efficient, and cost-effective resolution of those disputes.

The NEC4 suite of contracts also includes an option for dispute boards to decide the outcome of any dispute under the relevant contract.

Every party has a role to play

There is pressure on all parties in the construction industry, from rising interest rates and inflationary impacts coupled with challenges such as supply chain disruptions and skills shortages to increasing pressure on public balance sheets. The insecurity felt by businesses and the conservatism and default to the status quo by government also hinders further investment in areas such as digital innovation and workforce development.

As with risk, the roles and responsibilities of different parties also need untangling. The whole ecosystem of the construction industry must be healthy, sustainable, and profitable to ensure the stability of Australia's economy, noting the industry produces around 9% of our GDP.

Construction can pull us out of recession and accelerate recovery when needed through both the private and public sectors. Infrastructure has played a huge role in the government's economic response to the COVID pandemic. According to the Australian Bureau of Statistics, the volume of engineering construction (which encompasses infrastructure) rose by 2.0% during the December 2022 quarter which was 6.4% higher than a year earlier and mostly driven by public sector work.

Lack of productivity is one of the significant challenges impacting the broader construction industry. The performance of the construction sector in terms of multi-factor productivity (MFP) is very low compared to most other industries, as shown in the figure below.

For years industry insiders have said that the construction industry is neither healthy nor sustainable,[9] and now the broader community can see it with the public collapse of several construction companies.

At the heart of all the reform threads are collaboration and transparency, which means that while one party might need to lead, support will be needed from all other parties. From consultants to constructors, clients to industry associations such as Consult Australia, we all have a role to play.

Consultants and constructors

It is critically important to recognise the differences between the role of a consultant and a contractor as well as the limitations of each role:

- **Consultants** provide intangibles, in that they provide professional services. Their promise is to deliver that service to the appropriate level of quality, not to guarantee the future or the outcome. Consultants cannot guarantee the final build as they do not have control of the construction. A consultant's obligation is to perform the services to the standard of skill, care and diligence as is generally exercised by competent members of the consultant's profession performing services of a similar nature at the time the services are provided.
- **Contractors** provide tangibles, in providing the final build. Their promise is to deliver that final build. A contractor's obligation is to deliver that outcome and for it to be of satisfactory quality and fit for the intended purpose.

The consultant sector is highly susceptible to instability in the PI insurance market – the insurance that those firms rely on for business continuity. A stable PI market is essential so consultants can access appropriate insurance cover commensurate with fees to manage unforeseen risks.

The contractor sector is pushed to accept unsustainably low profit margins which in turn feeds into the cycle of insolvencies.

"Building sector profit margins have fallen from around 3 per cent to below 1 per cent and liquidity has collapsed from 15 per cent to below 5 per cent...Most concerningly, over half of all large builders are now carrying current liabilities in excess of current assets—a technical definition of insolvency."

– Jon Davies, CEO, Australian Constructors Association[10]

The reform threads seek to ensure that the value that consultants and constructors bring to projects are enhanced rather than seen as detrimental to each other. For example, scoping for success would involve both designers and constructors to ensure specifications were suitable for design while also accounting for constructibility.

Government

Consult Australia has always believed that the market takes the lead from the government. For example, in our Model Client Policy, we said that the adoption across government clients would set the standard of behaviour for the rest of the industry to follow.

Clearly, the reform threads need the government to take the lead in many respects, both as a client and also as a regulator (especially for 'redefining the rules').

There is also an opportunity for governments to:

- use AI and data to drive project management at first instance
- introduce a risk rating tool in procurement and contracting to highlight where risk is being allocated.
- invest consistently in dispute resolution across whole projects (not just at the head contract level) especially in the D&C model to counter the culture of disputation and embed collaboration and problem-solving/dispute avoidance.

CASE STUDY – Government as an 'active client'

An 'active client culture' was recently noted in a case study of the procurement approach of Major Road Projects Victoria (MRPV). This culture was expressed in different ways. Firstly as a shift away from a passive approach where a project is the contractor's responsibility and MRPV's role is to watch for non-compliance. Another expression was that the successful delivery of each and every project is MRPV's responsibility and MRPV's role is to exercise all the resources and influence it can to that end.

Practical examples of what being an active client meant included:

- Engaging in options to undertake works in 'blitzes' to minimise local community disruptions caused by extended day works.
- Health and safety staff being on site, directly engaging with the project, its safety processes, and behaviours on site.

The case study noted that the procurement model was a 'relationship-based procurement model' which was seen as a paradigm shift for many MRPV staff.

Industry associations

Industry associations allow member concerns to be amplified for impact. The key benefit for government of interacting with industry associations is the ability to gather collective industry views. Interaction with industry representatives is a way the government can mitigate the risk of getting a particular company's self-interested view, greatly increasing the chances of getting a broader industry collective view.

Consult Australia is proud to be the only voice for all consulting businesses in design, advisory and engineering for the built and natural environment. Our solutions-based advocacy is developed in collaboration with broader industries, the construction industry, government and our members. As part of our role we educate and inform all these stakeholders to uplift the whole industry.

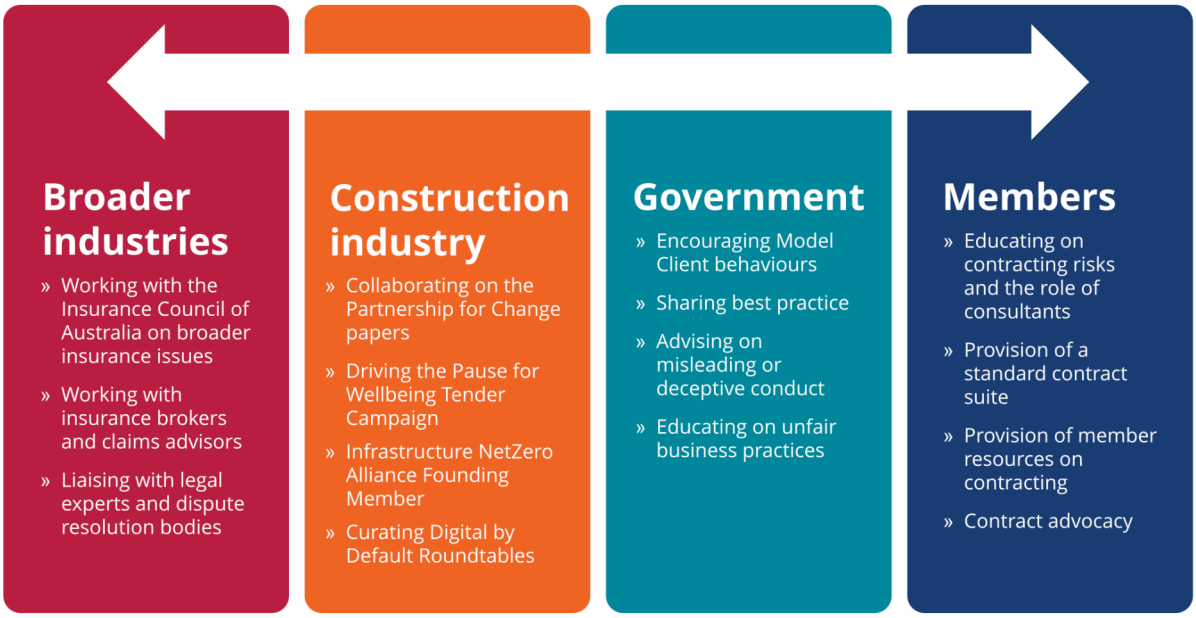


Figure 10 – Consult Australia activities relevant to contracting and risk.

More information on Consult Australia's activities and campaigns are available on our website, including at the Centre for Contracting & Risk.

CASE STUDY – TfNSW Collaboration with industry

Transport for NSW is demonstrating collaboration with Consult Australia, the Australian Constructors Association and the Civil Contractors Federation, having established working groups focussed on three areas:

- **360 health checks** to set collaborative standards of behaviour and interaction on projects with a 360 process for monitoring and reporting on performance.
- **Personnel requirements** to review and implement a portfolio-wide approach to avoid unnecessary and excessive specification relevant to personnel on future projects.
- **Design reviews** to implement agreed collaboration framework on in-flight projects including the removal/minimising duplication of effort.

Next Steps

An active industry voice can only do so much – we need you to act.

Whether you are from a broader industry that relies on consultants, within the construction industry, a government client or a consultant yourself – you need to also act. You can choose to invest more time and energy in the reforms as set out in this paper or work in other ways that deliver collaboration and transparency to relationships and projects.

End notes

1. See https://www.kevinpascoe.net/post/suppressing-subjectivity-objectively-quantifying-risk-allocation-in-construction-contracts
2. See Insurance Council of Australia's submission to NSW Design and Building Regulations
3. See https://www.bellrock.com.au/july-2024-market-update-construction-professionals-pi/
4. HKA CRUX Dashboard
5. See HKA Sixth Annual CRUX Insight Report.
6. See Delivering Better Project Outcomes in Australia
7. 2015 Treasury Briefing, 'Aftermath of the HIH collapse'
8. See FIDIC 2023 Practice Note on Dispute Avoidance
9. The Health of the Australian Construction Industry Research Report (September 2020)
10. See: https://www.constructors.com.au/all-risk-no-reward-revealed-in-building-industry/#:~:text=%E2%80%9CBuilding%20firms%20are%20entering%20administration,to%20below%205%20per%20cent.

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P6: Source: Finity's Marketvue estimates from NCPD data

P21: Source: Courtesy of Transport for NSW

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