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Driving business success for consulting firms in the built and natural environment

11 May 2021

South Australian Productivity Commission
30 Wakefield Street, Adelaide, SA 5000

Via email: Hayley.Gossert2@sa.gov.au

Dear Secretariat,

Submission – SA Productivity Commission inquiry into the state’s regulatory framework

Consult Australia welcomes the opportunity to assist the SA Productivity Commission develop recommendations for reforms to better enable investment, employment and productivity growth in SA.

Consult Australia is the industry association representing consulting businesses in design, advisory and engineering. Our industry comprises some 55,000 businesses across Australia, around 97% of which are small businesses (less than 20 employees) and also include some of Australia’s top 500 companies. Our members, no matter their size, provide solutions for individual consumers through to major companies in the private sector and across all tiers of government. Our industry is a job creator for the Australian economy, directly employing 240,000 people. The services our members provide unlock many more jobs across the construction industry and the broader community.

We note that the Commission is interested in regulation that applies principally to businesses that operate in SA. It is worth noting that while we have 30 business members with offices in SA, the number of consulting businesses providing services to SA is significantly more. Our members demonstrated during COVID-19 restrictions that they can provide a vast array of design, advisory and engineering services remotely. We know that over 90% of our members provide services in multiple jurisdictions and there are obvious constraints on having offices in every location you provide services to, especially for small businesses and sole practitioners (who makes up around 50% of consulting business in Australia).

We support the Commission’s consideration of ‘regulation’ as including primary legislation, statutory instruments made under an Act as well as quasi-regulation such as policies and codes. The biggest business critical issues currently facing our members are insurance and capacity issues as demonstrated by our most recent [Industry Health Check Pulse Survey, April 2021](#). We believe that reform to the operation of SA government as a client can significantly improve both these issues.

To assist the Commission, we refer to the *State Procurement Act 2004*, the *South Australian State Procurement Regulations 2005* and the various policies that fit under these.

The first issue to raise is the exemption under the Regulations of building and construction projects above \$165K. This exemption means that any procurement reforms adopted by the State Procurement Board do not flow through to those agencies and authorities predominately focused on building and construction projects (e.g. the Department of Infrastructure and Transport). Consult Australia notes that the devolved nature of procurement at the state level does not deliver the best outcomes for the government, the community or industry. A core concern is the lack of expertise of some procurement teams throughout government. There is a significant productivity drag when industry seeks reasonable changes to contracts but need to educate government officers on the commercial realities including insurance impacts.

We believe that the two core issues that need addressing are:

- the limited use of standardised contracts across the SA government
- unreasonable insurance requirements.

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The use of standardised contracts is limited

Many government agencies in SA use bespoke contracts or make extensive amendments to standard contracts (such as AS4122-2010). Members also advise that the same onerous contract terms are used on complex high-risk projects as well as to engage small to medium enterprises (SMEs) on small lower risk projects. The onerous terms we see include warranties and indemnities that shift liability to the SME regardless of fault, no cap on liability or liability caps tied to insurance proceeds. Remembering that the vast majority of consultancy businesses are small, they do not employ in-house counsel and cannot afford to engage external legal counsel on every procurement to comprehend these contract terms and the implications for their business.

Under the devolved model of government procurement, government agencies often use external counsel to draft contracts, which means that in-house procurement officers are usually less comfortable discussing contract terms with industry members.

Non-lawyer SMEs representatives, if they attempt to negotiate, often find they are doing so with external lawyers who have little knowledge of the role of the SME or their services and so are given very little scope to achieve balanced amendments to the contract.

Case Study

A small business providing flood plain advisory services successfully bid on a small fee advisory tender for a government water agency. The business was provided with over 100 pages of contracting materials and when seeking clarity on terms was advised to have the business' in-house counsel (which it doesn't have) contact the external legal counsel that had drafted the contract. This same contract has been used to engage large businesses on complex projects.

Unreasonable insurance requirements

Tendering and contracting requirements are rarely modified and do not seem to relate to the particular risks of the project, the consultant's fee, the scope of services, or the state of the insurance market.

Consult Australia member businesses are facing a worsening professional indemnity (PI) insurance market, this combined with the economic downturn caused by COVID-19, is significantly impacting the ongoing sustainability of our industry. Many small businesses and sole traders face forced business closures and early retirement based solely on the fact they can no longer get insurance (often at any price let alone affordable insurance).

We have been talking about the hardening market over the last 18 months, [AON's Global Insurance Market Conditions Q2 2020 Report](#) states that the hardening in the market is here to stay for now and that in Australia:

Australian insurers are focused on cost over-runs, loss mitigation, warranties and cross liability, with related exclusions and sub-limits commonplace. As the Australian government tries to kick start the economy with infrastructure investments, capacity may become an issue.

In talking with our members, capacity is already an issue across businesses of all sizes. Australia's building and construction sector is now considered one of the highest risk industries in the world for PI insurance – which impacts all our members whether they work on designing the most complex infrastructure projects or not. Year on year premiums are increasing while coverage amounts decrease – irrespective of a business' claim history. The number of underwriters providing any sort of

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coverage has become extremely limited. Small companies advise that PI insurance premiums are their largest business expense and these businesses providing specialise design, advisory, or engineering services will struggle to survive unless action is taken.

Case Study

A sole trading structural engineer has been forced into early retirement because he cannot secure PI insurance. This is despite having a long-term client of over 20 years, a steady stream of work and income as well as no claims in over 15 years. Without PI Insurance, this sole trader cannot operate, even as a verifier of other's work.

Further, he is unable to secure run-off insurance, to cover any claims that may arise during his retirement for past work. Essentially, this engineer is self-insuring, putting at risk his savings and property holding. The cover required by this engineer to continue working with their long-time client is only \$2-3 million. In past years, the premium for the PI insurance was \$6,500 this increased to \$22,000 last year.

Multiple brokers specialising in engineering and professional services cover have advised this member that there is no cover *'from any insurers, underwriters, or other markets (at any price)'*. This is an untenable position for this engineering consultant who has a long and successful career and could still contribute to Australian economy, but for the hardening of the PI market.

With the current state of the professional indemnity (PI) market, all consultants are under increasing pressure from their insurers to ensure they do not sign up to arrangements that unnecessarily exposes their insurance. The lack of willingness to use standardised and fair contracts combined with unreasonable insurance limits, make contracting with some SA government agencies unattractive and often too risky a prospect for consultants.

The solutions

The above issues can be resolved with real engagement and collaboration between industry and government. In fact, these issues are addressed in our [Model Client Policy](#) which suggests that all government agencies have a responsibility to acknowledge and address the inherent imbalance in market power between government clients and the private sector.

The lost productivity and costs associated with the devolved model of government procurement should also be measured, as we believe that this would support this case for greater standardisation of appropriate and balanced contract terms across SA government.

In terms of standardised contracts for consultants, Consult Australia supports AS4122-2010 General Conditions of Contract for Consultants, FIDIC Consultants Model Services Agreement and NEC4. These contracts avoid the onerous and/or inappropriate terms our members see in some SA government contracts. It is vital that any special conditions added to these standardised contracts do not undermine the intent of the original standard.

If SA government (or an agency of SA government) seeks to develop a bespoke standardised contract, or special conditions to an Australian Standard it is vital that industry associations are consulted on the terms prior to release, to avoid the terms of concern which are often borne out of a failure to understand and acknowledge the difference between consultants and contractors. It is also essential that procurement officers are educated and empowered to discuss contract terms with industry (both individual businesses and industry associations).

Below is a list of typical terms of concern that appear in contracts prepared by SA government agencies:

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- **Fitness for purpose obligations are not appropriate for consultants.** Too often fitness for purpose obligations, which are suitable for contractors that can guarantee the final build, are imposed on consultants who should instead be held to the reasonable standard of care for professional services. For more information I attach our *Client Briefing on Fitness for Purpose*.
- **Contracting out of proportionate liability should not occur in consultancy contracts.** Proportionate liability was introduced into the civil liability framework around the country to alleviate the PI insurance market issues caused by the collapse of the insurer HIH.

However, that policy intent is undermined, and consultant's insurance is subject to too much exposure because government contracts require parties to waive their statutory right and contract out of proportionate liability. For consultancy contracts, proportionate liability must be preserved. For more information I attach our *Client Briefing on Proportionate Liability*.
- **Capped liability must be the default without a reliance on insurance proceeds.** Capped liability ensures certainty for all parties if things go wrong. In a few bespoke contracts around the country, we have seen sensible liability caps undermined by excluding insurance proceeds. In certain instances, liability frameworks can refer to insurance, but when a single cap is set, that cap should be independent of insurance. For more information I attach our *Client Briefing on Liability Frameworks and Insurance*.
- **Contractual warranties must be avoided in consultancy contracts.** Contractual warranties are common in contractor contracts, as contractors (builders/constructors) can guarantee outcomes, however the professional indemnity insurance of consultants will rarely cover contractual warranties. The obligations suitable for consultants can be contained within the contract as obligations, but if they are drafted as warranties insurers can deny cover.

In respect of insurance requirements, once again educated and empowered procurement officers are key to ensuring that minimum insurance requirements are reasonable. Consult Australia is currently drafting a guide to insurance for procurement officers, which I'd be pleased to share with the Commission when complete.

I would appreciate the opportunity meet with you to discuss this further. I invite your office to contact me at jan@consultaaustralia.com.au or on 0408 845 975.

Yours sincerely,

A handwritten signature in black ink, appearing to read "Jan Irvine", with a stylized flourish at the end.

Jan Irvine

Manager for SA, TAS and the Territories

Attachments:

- *Client Briefing on Fitness for Purpose*
- *Client Briefing on Proportionate Liability*
- *Client Briefing on Liability Frameworks and Insurance*