Trade Practices Amendment (Australian Consumer Law) Bill (No. 2) 2010

Submission to Senate Standing Committee on Economics

23 April 2010

SUBMISSION BY

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PURPOSE

- This submission is made by the Australian Institute of Architects (the Institute) to the Senate Standing Committee on Economics as the completion of the Institute's initial summary submission on 16 April 2010.
- At the time of this submission the Institute's Executive Committee consists of: Melinda Dodson (National President), Karl Fender (President-Elect), Howard Tanner (Immediate Past President), Rod Mollett and Shelley Penn.
- The Chief Executive Officer is David Parken.

INFORMATION

Who is making this submission?

- The Australian Institute of Architects (the Institute) is an independent voluntary subscription-based member organization with approximately 9171 members, of which approximately 5,150 are practising architect members.
- The Institute, incorporated in 1929, is one of the 96 member associations of the International Union of Architects (UIA).
- The Institute represents the largest group of non-engineer design professionals in Australia.

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1.0 INTRODUCTION

1.1 Purpose of submission

1.1.1 The Institute is pleased to provide comment to the Senate Standing Committee on Economics on the effect of s.61 of the Trade Practices Amendment (Australian Consumer Law) Bill (No 2) 2010 [the Bill].

1.1.2 Section 61 of the Bill will imply a guarantee of fitness for a particular purpose into contracts for the provision of services by architects to consumers. The section provides as follows:

> **61 Guarantees as to fitness for a particular purpose etc.**
>
> (1) If:
>
> (a) a person (the ***supplier***) supplies, in trade or commerce, services to a consumer; and
>
> (b) the consumer, expressly or by implication, makes known to the supplier any particular purpose for which the services are being acquired by the consumer;
>
> there is a guarantee that the services, and any product resulting from the services, will be reasonably fit for that purpose.
>
> (2) If:
>
> (a) a person (the ***supplier***) supplies, in trade or commerce, services to a consumer; and
>
> (b) the consumer makes known, expressly or by implication, to:
>
> (i) the supplier; or
>
> (ii) a person by whom any prior negotiations or arrangements in relation to the acquisition of the services were conducted or made;
>
> the result that the consumer wishes the services to achieve;
>
> there is a guarantee that the services, and any product resulting from the services, will be of such a nature, and quality, state or condition, that they might reasonably be expected to achieve that result.
>
> (3) This section does not apply if the circumstances show that the consumer did not rely on, or that it was unreasonable for the consumer to rely on, the skill or judgment of the supplier.

1.1.3 In our commentary at Section 3.0, we express the Institute's strong objection to the increased liability which s.61 will impose on architects (and engineers). An Executive Summary appears at Section 2.

1.2 Expertise of the Institute

1.2.1 The Institute seeks to advance the professional development of the architectural profession and highlight the positive benefits of good design in addressing the concerns of the community in relation to sustainability, quality of life and protection of the environment.

1.2.2 The Institute promotes responsible and environmentally sustainable design, and vigorously lobbies to maintain and improve the quality of design standards in cities, urban areas, commercial and residential buildings.

1.2.3 The Institute has established high professional standards. Members are obliged to operate according to the Institute's Code of Professional Conduct and must undertake ongoing professional development. The Institute's Professional Development Unit offers an extensive program at national and state level, continuing to keep members informed of the latest ideas, technology and trends in architecture and the construction industry.

1.2.4 The Institute represents the profession on numerous national and state industry and government bodies, advising on issues of interest to the architectural profession and the construction industry.

1.2.5 Particular areas of expertise include:

- quality assurance and continuous improvement
- industry indicators and outcomes
- risk management and insurance
- policy development and review
- technical standards
- environmental sustainability.

1.2.6 The Institute is the owner of a subsidiary, IBL Limited, which under its trading name Architects Professional Risk Services negotiates the terms of and manages the operation of a professional indemnity insurance facility for architect members of the Institute. Through this facility a professional indemnity insurance policy underwritten by a major Australian insurer is offered. Under its trading name Planned Professional Risk Services, IBL also operates as an insurance broker for professional indemnity insurance of non-member architects as well as engineers. Currently, the majority of architects insure through the Institute's subsidiary. As it negotiates for the best terms for architects, it is in an informed position in relation to insurance for architects in the Australian market.

1.2.7 Through the Institute's other subsidiary, Archicentre Limited, the Institute is in also in close contact with the residential market as it relates to consumers. The primary focus of the services to consumers offered by Archicentre is to introduce them to member architects with whom these consumers may choose to independently contract with for alterations, renovations or new homes.

2.0 EXECUTIVE SUMMARY

2.1 The Institute strongly objects to the inclusion of architects and engineers as service suppliers subject to the proposed statutory guarantee to consumers of fitness for purpose. The statutory guarantee would then apply to consumers who engage an architect for their house, but not to those who will on-sell their home as a developer. The Institute and its members believe that this amendment will adversely impact on architects who constitute a significant number of its members, either as principals of smaller practices in particular, or employees dependent upon them for employment as architects.

2.2 The nature of architects' work with consumers in residential projects leaves architects (and engineers) exposed to undue liability, which is particularly severe on sole practitioners and small to medium practices. There is no evidence that an additional head of liability is necessary or that it addresses a systemic failure in the recourse consumers presently have for loss attributed to architects, through negligence, misleading and deceptive conduct under s.52 or s.51A of the TPA, and/or contractual claims.

2.3 No substantiated reasons appear to have been advanced for the removal by s.61 of the Australian Consumer Law Bill No. 2, of the exemption contained in the existing equivalent Trade Practices Act (TPA) section 74(2).

2.4 The Commonwealth Consumer Affairs Commission (CCAC) report makes reference to New Zealand consumer law as a template for the ACL, and the Bill. However, the Institute submits that NZ consumer law does not offer any useful support for the removal of the exemption in NZ's less litigious environment.

2.5 Refuting claims for such liability in addition to the forms of legal recourse already available to consumers, imposes a potentially significant additional cost burden on small architect (and engineer) practices that is not justified, in the Institute's view, by any benefit to consumers. This is particularly so where the costs of refutation go beyond legal support to inability to attend to business while claims are being defended. S61 alone may ultimately reduce the breadth of architectural services available to consumers, while also increasing its cost to consumers.

2.7 Availability of insurance to protect the business of architects (and engineers) from claims under this proposed head of liability is uncertain. No such insurance for voluntarily assumed warranties of fitness for purpose is available to architects at present, whether through the facility available to Institute members through its subsidiary, or elsewhere in Australia. If such insurance is offered as a result of this proposed law, all indications are that it will be at a significant premium increase.

2.8 Costs of risk mitigation, including the additional cost of insurance, if available, cannot help but be passed in to the consumer in increased fees. This can only position an architect designed home further from the average consumer.

2.9 The exposure to liability is heightened unnecessarily by the addition of a guarantee in connection with the consumer's *implied* purpose to be achieved by the services. Because of the nature of residential design, implied purposes can be subjective and come into existence in hindsight during the 6 year period of liability provided under the Bill.

2.10 Architect members responding to our survey also suggest they will avoid innovative solutions or that some will even decline engagement where an innovative solution is requested by a client. New solutions in housing that can benefit all of Australian society require experimentation that often takes place only where clients are relatively speaking, able to afford it. However, the response of members suggests the threat of a guarantee that can affect their livelihood if the experiment does not deliver, is enough to deter many architects.

2.11 The Institute submits that there will be a resulting avoidance of residential design for consumers, and/or withdrawal of some practitioners from the market, lessening competition and the availability of services to consumers. Survey response of Institute members in relation to the proposed law suggests strongly that this is a real possibility.

2.10 The proposed law appears to impose, in effect, a penalty of forfeited fees where the consumer may terminate the contract of engagement and demand return of fees, as well as sue for compensation for loss or damage. This seems both unfair and excessive – given work for that client may be a substantial part of the architect's revenue.

2.11 The proposed law is also unclear about how an architect or engineer would mitigate their liability, particularly where several 'disclaimers' about inability to meet expressed client wishes, may amount to a purported contracting out, which is otherwise void.

3.0 COMMENTARY

3.1 Background to the Institute's commentary

3.1.1 Save for the following remarks, this submission is confined to the effect of the Bill on architects, which will greatly increase the risk of liability for architects of home design for consumers. Section61 proposes removal of the exemption for architects currently provided under s.74(2) of the TPA.

3.1.2 The Institute fully acknowledges that there are other professional services providers, within and without the building industry, that have not been exempted by s.74(2) since 1986.

3.1.3 Nothing in our submission should be taken to imply that we consider that s74(2) of the existing TPA, or the proposed s.61 and its associated sections of the Bill ought to apply to other professional service providers, but not to architects and engineers. Many of the arguments we will put for continuance of the exemption could equally be made for bringing other professional services providers within the exemption of the current s,74(2), or removing s.74(2) of the TPA and by inference s.61 of the Bill altogether.

3.1.3 In response to the Bill, the Institute recently surveyed its members who are principals of architectural practices. The Institute obtained 1001 responses to its survey about the proposed removal of exemption, a response rate of 36%. Of the respondents, 96%indicated that their practice provides residential design services, and 53% responded that they provide very many such services (in the course of their business).

3.1.4 While it is not possible to determine the proportion of these services for consumer residential designs (as opposed to multi-unit or developer initiated housing) it is well known by the Institute that the primary work of smaller architectural practices is usually consumer oriented.

3.1.5 Within the Institute's membership, there are some 495 single practitioners and 1,212 practices of 1-3 principals. The Institute believes that changes to the law adversely affecting the profession's activity in relation to consumer residential design, including a negative impact on the viability of architects' businesses, will resonate strongly with its membership, including employees of such small practices. The response rate of 36% of principals to the survey bears this out.

3.2 The nature of architects' professional services to consumers

3.2.1 Unlike the provision of many professional services, architects' services to which this legislation applies almost always result in a physical product – a home, whether new, or post-alteration.

3.2.2 Housing designed by architects is almost invariably 'bespoke' in nature. Such homes are not "products" in the nature of others, which can readily be tested before release to consumers. Rather, virtually every bespoke home resulting from architects' services is analogous to a prototype. However, unlike the prototypes for a manufactured product which can be tested and refined before sale or delivery, the bespoke product of an architect's work comes together on completion, at which point it is 'delivered' straight to the consumer.

3.2.3 Our Members suggest that no amount of explanation or technology is a guarantee of consumer comprehension of the product they have ordered by approving the design, one member comments:

> *".....most clients in* (the) *residential sector are not "professional clients" and find it hard to read plans and even 3D renderings".*

3.2.4 Once a consumer has taken delivery of their home the consumer will potentially identify things which work better for them than anticipated and those which do not. As an Institute member observes of the process of housing design:

> *"The process of designing and building residential projects is extremely complex and personal - it will never be possible to predict and document every aspect of a project with respect to a client's implied expectations. There are many aspects of a completed building that the client will not have been able to imagine as an issue during the design stage."*

3.3 Removal of exemption first proposed in the CCAC report

3.3.1 Removal of the exemption of fitness for purpose for architects (and engineers) was not raised as an issue for consideration in the original discussion paper prepared by the Commonwealth Consumer Affairs Committee (CCAC).

3.3.2 However, the CCAC's subsequent report, released in December 2009, proposed removal of the exemption. The only justifications given (page 121) are to note that the exemption does not exist in New Zealand and that removing the exemption promotes simplicity, uniformity and fairness.

3.3.3 There is no suggestion made in the report that the notion of fairness applies to consumers. Rather, it appears to be fairness to other professional groups already exposed to liability that has driven the CCAC proposal.

3.3.4 No market failure has been identified, nor does the CCAC propose that removal of the exemption will correct one.

3.3.5 None of the fundamental changes proposed in the Bill intended to improve the operation of consumer protection law, depend in any way on the removal of the exemption from s.61.

3.3.6 The Institute submits that the interests of good law for Australia are not served by mere "simplicity and uniformity" at the expense of real problems for the delivery of services by architects (and engineers) which will be caused by s.61, on which we elaborate below.

3.4 Operation of New Zealand Consumer Law is not a good enough reason for change

3.4.1 Generally, the CCAC report cites the NZ consumer legislation as more effective than Australia's Trade Practices and Fair Trading Acts.

3.4.2 In fact, in over more than 15 years, there has been very limited use in general by NZ consumers of the NZ Consumer Guarantees Act 1993 (CGA). The minimal use by consumers pursuing redress under the CGA is causing similar concerns to NZ's government as the minimal use by consumers pursuing redress under the Trade Practices Act and Fair Trading Acts in Australia.

3.4.3 The CCAC report offers no explanation for this general lack of use, and we submit it is no argument for removal of the exemption in Australia. On the basis of our enquiries, the Institute believes it reflects a far less litigious culture in New Zealand.

3.4.4 Despite the fact that the CGA contains no exemption for architects and engineers in its equivalent section 29, there is a dearth of recorded consumer action against architects under that section. Even with the post 2006 existence of the specialized "New Zealand Weathertight Homes Tribunal" as an alternative to the courts, in which one might expect claims against architects or engineers under s.29, there are none reported.

3.4.4 It is the translation of s.29 of the CGA to the increasingly litigious Australian legal landscape that greatly concerns the Institute and its members.

3.5 Disincentives arising from added liability – unintended consequences

3.5.1 The survey response of Institute members shows that 41% believe that their fees would rise at something over 5% as a result of this proposed change. In fact 23% of those consider the necessary fee rises to cover costs would be more than 10% over current levels.

3.5.2 While the reasons for the probability of such rises are discussed under following headings, the Institute submits that this proposed change to the law is not a benefit to consumers in general when it will place the services of architects further beyond reach for many.

3.5.3 This is not just a problem for consumers who may like to but cannot have an architect. It is well accepted that architects are often at the forefront of advancement in home design, the benefits of which filter through the housing market. The needs of the community for sustainable cities in the face of projected massive population growth are both palpable and imperative. Australia must learn how to be more sustainable in its housing and how to mitigate the effects of climate change. Architects pursuing their livelihood conduct applied research through their work in solving real problems for clients.

3.5.4 A guarantee of fitness for purpose, applying irrespective of an architect's genuine effort in application of care and skill, will hamper innovation. Sixty four percent of our survey respondents indicated that faced with the imposition of no-fault liability, they would avoid any client request for an innovative solution. As an Institute member observes:

> *"Architects do not design in a vacuum. The client has continuous input into their house. This law is likely to inhibit leading edge and innovative design as architects play it safe. In the process the clients are likely to be more dissatisfied with their architects because they appear to be less responsive to their aspirations."*

3.5.6 At what level of risk would an inspirational and dedicated innovator such as the Pritzker Prize winner and Gold Medallist such as Glenn Murcutt, begin to become too cautious to innovate? While the Institute cannot and does not purport to speak for him, if this the consequence for even some of the leaders of architecture at the forefront of innovative home design, the inventiveness that Australia needs to learn new solutions to build sustainable cities and towns for its rapidly increasing population must suffer badly.

3.5.7 The Institute's survey also indicates that for a significant proportion of architects, the removal of exemption from fitness for purpose will tip the balance against providing home design services for consumers, thereby reducing competition and exacerbating housing affordability problems in Australia. 5% indicated they would 'definitely avoid' residential projects and a further 44% indicated they would be more likely to avoid them.

3.5.8 While the following is but one response by a member, it indicates the reaction of Institute members to the prospect of this change in the law:

> *"As a part-time architect working from home solely on residential homes and additions, the proposed changes would put such a high risk for so little return, that I would probably have to consider if it is worth continuing my practice".*

3.6 No-fault liability for architects' professional services is not justified

3.6.1 It is common for the threat of, or actual negligence claim, to be raised by consumers in response to a claim for payment of outstanding architectural fees. A claim, even if not ultimately made out, has dire consequences for the architect in terms of insurance premiums and loss of productive time in managing the claim.

3.6.2 The nature of claims made in the consumer housing market against architects is that they are often brought in 'consumer tribunals' under the specialized housing legislation that exists in virtually every state and territory. For the plaintiff client, these are virtually a legal cost free environments where legal forms that contain costs are not entertained, and untested interpretations of the law are relatively easily explored by consumers.

3.6.3 The opposite is true for architects. Either there are the legal representation costs in meeting claims by represented or self-represented clients, or there are the significant costs of inattention to one's practice while defending claims. Complaints by members to the Institute about the costs of defending client claims in lower courts and tribunals in the current circumstances of liability in negligence, misleading and deceptive conduct and breach of contract, are common. The Institute believes the new s.61 will only exacerbate this problem.

3.6.4 The proposed law raises several questions, including whether the consumer's implied purpose is a subjective rather than objective one. As one Institute member has commented in response to the proposed law:

> *"Even if you could adequately defend yourself with masses of documentation the opening would be there for Clients to at least have a go* (sic) *because 'implied' is such an open term. A small practice could go broke just defending claims."*

3.6.5 The Institute takes no issue with a guarantee that the architect will use due care and skill (s. 74(1) of TPA and s.60 of Bill No. 2), as this is a well understood, insurable legal obligation under the law of negligence. However, there is a real issue with a guarantee that an implied purpose *will be* attained. This means that no matter how much care and skill is applied to achieve the result, if a purpose also implied by that result is not achieved, liability is strict (indefensible). An Institute member observes:

> *"...fit for purpose is different for every individual client -- a legal nightmare to resolve and very difficult to pre-empt no matter how diligently you prepare your brief and communicate with your clients"*

And another notes:

> *".....I've had two separate clients who are trained chefs who have vastly different ideas on how a kitchen should operate, and would hate the other's ideas...so where does that leave us when we use that experience for other clients?....."*

3.6.6 It is in the Institute's view, inequitable that in addition to liability in negligence, an implied purpose can be identified in hindsight by a consumer who wishes to obtain both a refund of professional fees and damages, under s.267 – 269 of the Bill,

To quote a member's reaction:

> *".....the client can always argue that 'they didn't expect the outcome' - notwithstanding they 'agreed' to go forward with a design. In design you are buying an outcome not a product - how can you warrant* (guarantee) *a reaction to an outcome"*?

Another member comments on the situation 'post-delivery' when the architect's response to a client's purposes is brought to fruition:

> *"How does one measure subjective less tangible and subjective qualities - 'bright and airy spaces', ' a feeling of spaciousness', 'an inspirational quality', 'comfortable in summer without air-conditioning', etc"*

3.6.7 Under the current situation, mere failure to achieve a desired purpose does not of itself bring about liability – there must also be a failure to have applied the requisite standard of care (and skill). The standard to be applied incorporates the court's interpretation of the state of knowledge a reasonable architect would have had at the time of designing.

3.6.8 The liability in negligence may also be offset by the degree to which the client contributed to the failure through their own negligence.

3.6.9 In a related way, architects and engineers are subject to claims of misleading and deceptive conduct, either under the present s.52 of the TPA, or concerning representations as to the future under the present s.51A. This exposure will continue under the ACL, and the Institute takes no issue with this liability continuing.

3.6.10 Conversely, under a guarantee, none of what could be called 'mitigation', applies. Failure to achieve the purpose means liability is automatic. Consideration of whether the architect failed to apply the required standard of due care and skill at the time of design is irrelevant, as is whether the client also contributed to the failure to achieve the purpose.

3.6.11 Under s.61, liability for a design which failed to achieve the purpose will apply unless the design could have been reasonably expected to achieve the purpose. However, consideration of what the purpose is could occur up to six years after the design was undertaken.

3.7 Protection of architect's businesses by insurance is uncertain

3.7.1 As s.61 will directly impose a guarantee of fitness for purpose, there is an immediate issue about the ability of architects to manage the risk of potentially crippling liability – particularly for smaller architect practices.

3.7.2 The Institute is aware that the relatively high cost of professional indemnity insurance is commonly the single most expensive business expense for a small architect practitioner. As we noted above, there are currently 1,212 practices with between 1 and 3 principals (whether these are the practice's partners, owner-directors or similar). Of these, about 494 are sole practitioner practices. The prospect of substantial increase in the cost of insurance is very worrying to the survey respondents, with a full 90% (900 of the 1001 respondents) telling us that it would concern them either 'quite a lot' or 'very much'.

3.7.3 However, professional indemnity insurance for warranties (or guarantees) of fitness for purpose is not available to architects. We are advised by IBL that insurance underwriters almost invariably decline requests for specific policy endorsement by insured architects and their brokers.

3.7.4 This reflects the fact that a warranty or guarantee is fundamentally different to negligence, which is insurable, from a risk underwriting perspective. In the context of professional services to a client, liability in negligence only arises where the architect has failed to apply due care and skill in accordance with the objective standard required.

3.7.5 Insurance of architects (and engineers) is a unique line of insurance. The comfort of an insurer with fitness for purpose guarantees for other types of professionals is no indicator of the propensity of architect or engineer underwriters to endorse policies for them.

3.7.6 In any event, if professional indemnity insurance becomes available, it is very likely that significant premium rises are involved which themselves will affect the viability of smaller architect practices, as borne out by the survey results noted above.

3.7.7 Dealing with insurance premium rises, (if insurers in Australia are prepared to offer such insurance to architects) is not simply a matter of increasing fees. There is a limit to the costs that an architect can successfully pass on to consumers while remaining competitive.

3.7.8 For those remaining in the market, increased transactional work to manage risks is also likely. A member observes:

"…… (the new law) *may greatly increase amount of required consultation with* (the) *client* (and) *lead to more defensive relationship with* (the) *client where disclaimers and description of negative scenarios will dominate all dialogue*."

3.7.9 Such work, including insurance, if available, as discussed above, adds business costs ultimately passed through to consumers, wherever possible. However, as we note above, there is only so much in costs that can be passed through, and the viability of smaller practices in particular is compromised by such costs.

3.8 Uncertain operation potentially bringing about unduly severe consequences

3.8.1 As noted, this liability on the basis of a guarantee that the services would reasonably be expected to achieve the result, is "no-fault" liability for the architect if the consumer reasonably relied on the skill and judgment of the architect and the purpose the consumer had in mind was implied (or express). No fault means, as noted, that the liability applies even where the architect applied reasonable skill and judgment, or exemplary skill and judgment.

3.8.2 The customary remedy for liability of an architect to its client is damages, that is, monetary compensation for the actual loss suffered by the client.

3.8.3 As noted above, s.267 – 269 of the Bill which provides the remedies for consumers, also provides for refund of professional fees. There is nothing in the proposed s.267 – 269 to suggest the refund is less than refund of *the whole of* the fees.

3.8.4 If that is Parliament's intention then the remedy for consumers is draconian as applied to architects.

3.8.5 This is because architect's services to consumers for home design are intense, detailed, provided over a considerable period, and any one client can often provide a major proportion of an architect's annual revenue. Such fees, if lost through liability, whether or not in addition to damages, are likely to be in many cases, crippling for an architectural practice, if not terminal.

3.8.6 Even if insurance against such liability becomes available, loss of the whole fee is a disproportionate remedy as it is almost inconceivable that the whole of the architect's work is not fit for purpose.

3.8.7 In any event, insurance for architects does not cover refund of fees. If it were to do so, it again is very likely that premium increases will be significant with the attendant threats to small architect practices noted above.

3.8.8 Under this proposed law, it seems an architect could not protect his or her livelihood from an unachieved implied purpose not identified by the architect at the time of design.

3.9 Apparent unavailability of risk mitigation

3.9.1 Section 61(3) of the Bill provides that the no guarantee of fitness for purpose will apply where circumstances show that the consumer did not rely on the supplier's skill or judgment that the service would be fit for a particular purpose, or, that it was unreasonable for the consumer to have so relied on the supplier.

3.9.2 Nevertheless, it remains unclear how the second part of s.61(3) would work in practice, given that s.64 makes an exclusion of the guarantee by contract void.

3.9.3 Where the purpose is expressly made known, the architect could similarly expressly inform the consumer that the services may not achieve the consumer's intended purpose. That would seem to imply that the circumstances were such that the consumer could not rely on the services to achieve the purpose.

3.9.4 However, that raises the question, unresolved by the proposed law, of what would happen if the architect's response to any intended purpose drawn to attention was to respond that its services may not achieve the intended purpose. In other words, how often could an architect respond in this way before these 'disclaimers' would be considered to be 'contracting out' and thus becomes void under s.64?

3.9.5 If Parliament's view is that some number of responses like this by the architect would be a 'contracting out', how would the architect mitigate the risk of serious commercial consequences if the client made known several intended purposes which could not reasonably be guaranteed to be achieved?

3.9.6 The Institute submits that the imposition of liability which cannot be mitigated is not an acceptable way to ensure the interests of consumers are protected.

April 2010