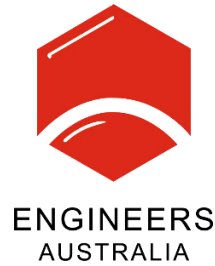


## INQUIRY INTO FURTHER INQUIRY INTO THE REGULATION OF BUILDING STANDARDS

**Organisation:** Insurance Council of Australia, Engineers Australia and Consult  
Australia

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**1 Sept 2021**

Public Accountability Committee

Parliament House

Canberra ACT 2600

Dear Members of the Committee,

Thank you for the opportunity to contribute to the Public Accountability Committee *Further Inquiry into the Regulation of Buildings Standards*. This is a joint submission from Engineers Australia, Consult Australia and the Insurance Council of Australia (ICA). Two of the joint signatories (Engineers Australia and Consult Australia) will be making separate submissions.

This letter is intended to assist the Committee's deliberations by providing a brief overview of the practical operation of the insurance requirements contained in the *Design and Building Practitioners Act 2020* (the Act) and the *Design and Building Practitioners Regulation 2021* (the Reg). Outlined below are some of the ongoing challenges within the professional indemnity (PI) insurance market and the specific impact of the NSW Government's reforms.

We note that the Act partially implemented the Building Confidence Report (the Report), which was undertaken by Peter Shergold and Bronwyn Weir on behalf of the Building Ministers' Forum and released in February 2018. The Report undertook "an assessment of the effectiveness of compliance and enforcement systems for the building and construction industry across Australia". Making 24 Recommendations across a range of subject matter, the Report outlined a range of challenges within the building industry. Among other things, it stated:

*After having examined the matters put to us, we have concluded that their nature and extent are significant and concerning. The problems have led to diminishing public confidence that the building and construction industry can deliver compliant, safe buildings which will perform to the expected standards over the long term.*

It is agreed that in the current insurance market there is minimal appetite to underwrite the risks of practitioners involved in the building and construction industry. Critical elements of the NSW reforms will help alleviate some of those concerns, especially where there is evidence that the issues identified in the Report have been successfully addressed.

However, there are other elements of the NSW reforms which do not assist to reduce risks in the market and in fact increase the risk and therefore should be reconsidered.

## The Professional Indemnity Insurance Market

The broader PI market has experienced loss ratios of over 95 per cent for the past three years.<sup>1</sup> A gross loss ratio of more than 100 per cent means that insurers do not have sufficient income from premiums alone to pay out claims.<sup>2</sup> Claims incurred have grown from around \$1.2 billion in 2017 to \$2.7 billion in 2020, representing a 125 per cent increase over the past 4 years while average premiums have risen from around \$2,504 in 2017 to \$4,078 in 2020, representing a 63 per cent increase over the past 4 years.

Partially this tightening is a reaction to previously understated risks, which was highlighted by the combustible cladding related fires at Grenfell Tower in London and the Lacrosse Building in Melbourne. However, the lessening availability and affordability of PI insurance is not just being experienced by professionals involved in approving such materials, although it is true that certifiers and building surveyors were initially hit hardest.

Domestic and overseas insurers reacted by increasing premiums to reduce their losses, acquiring capital from reinsurers at higher rates (which are then passed back to their customers) or placing restrictions on cover that cannot be underwritten, for example exclusions for non-compliant combustible cladding.

These trends should also be understood from a global perspective. Many of the insurers operating in this space, operate globally. If Australia is perceived globally as a challenging market, then that will affect the desire of global insurers to operate here. The Australian building and construction industry is considered as being particularly litigious which also impacts on the market.

Reducing risk, particularly in the building and construction industry is therefore key to bringing the PI insurance market back to a healthy state. This includes:

- reforms on practitioner behaviour and competence to bring confidence back to the market
- addressing the litigious nature of the industry.

## The Impact of the NSW Building Reforms on the Insurance Market

While the signatories support the Act's overall intentions, we note specific challenges which do not help reduce risks within the market, but instead make the challenge greater, especially the onerous insurance requirements, the duty of care and the failure to ensure proportionate liability.

The Report stated:

*...insurance is not currently available for the range of practitioners proposed to be registered. This weakness needs to be addressed. There should be ongoing discussion*

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<sup>1</sup> These figures relate to the broader PI market and are not specific to building and construction. More detail on PI market trends is included in the ICA's January 2021 submission to the Department of Customer Service consultation *Design and Building Practitioners Regulations* ([link](#))

<sup>2</sup> In practice, claims cost is only one component of an insurers cost of doing business meaning that a lower loss ratio is required to sustain profitability. This will vary between insurers and portfolios but as a general guide is often around 70%.

*between governments and the insurance industry to ensure that the best possible insurance is available to all categories of registered practitioner.*

The ICA, Consult Australia and Engineers Australia agree that ongoing discussions are needed to ensure that insurance is available to categories of registered practitioner and engineer. Unfortunately, the Act went beyond the recommendations of the Report in several ways, which are in fact detrimental to the insurance market including:

- **Duty of Care.** The legislation imposes a duty of care on any ‘person who carries out construction work’ to avoid economic loss caused by defects in or related to a building for which the work is done, and arising from the construction work. This arguably extends beyond the practitioners regulated by the Act as the wording could be read to apply to “a person who does construction work”, rather than just a person regulated by the Act. This duty is owed to all subsequent building owners. The duty of care is retrospective for ten years. The duty of care is subject to the *Civil Liability Act 2002* (NSW) which expressly allows contracting out of proportionate liability. These elements each significantly expand the scope of potential litigation.
- **Insurance Requirements.** The legislation requires design practitioners, principal design practitioners, building practitioners and engineers to obtain insured indemnity against “any liability to which the practitioner may become subject” or as part of another arrangement “approved by the regulations”. These elements do go to practitioner behaviour and competence.

Read together, these elements would require that any insurance product valid for the purposes of the NSW reforms would need to cover not only prospective buildings but also the previous ten years of construction. Significantly, this would require coverage of buildings constructed prior to the implementation of the Shergold/Weir reforms. The position of insurers was put in a January 2021 submission by the Insurance Council, which stated that:

*Insurers will not have an appetite to provide cover for the historical stock of buildings where work was undertaken without sufficient oversight.*

This has been the experience to date. To develop insurance products for a given market, insurers need to understand the risks inherent in that market so that they can price their products appropriately. As insurers have no way to accurately price the ten-year retrospective risks, no such insurance products have emerged. The practical impact therefore would be that relevant practitioners would be unable to source insurance products that satisfy their registration requirements – or attest to it as required by the Regs. While we note that the Government has provided a one-year transition period for these requirements, we do not see any prospect of such products emerging. Reducing risks within the market has a longer trajectory than one year, especially when it comes to changing industry culture and becoming less litigious.

## **Next Steps**

We trust that this submission has been of use. Engineers Australia and Consult Australia will make separate submissions to elaborate their respective views and positions. The ICA refers to earlier submissions,<sup>3</sup> which elaborate insurance industry views in more detail.

Yours sincerely

Andrew Hall  
Chief Executive Officer  
Insurance Council of Australia

Dr Bronwyn Evans AM  
Chief Executive Officer  
Engineers Australia

Nicola Grayson  
Chief Executive Officer  
Consult Australia

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<sup>3</sup> Insurance Council of Australia, January 2021, Submission to the Consultation on the *Design and Building Practitioners Regulations* ([link](#))