

JMD ROSS
INSURANCE BROKERS



Fitness for purpose
Professional indemnity insurance

Fitness for purpose

1. Legal position

(a) Duty of care

- The standard duty of care imposed on professionals (including consulting engineers, architects, doctors, lawyers and insurance brokers) at common law is to conduct their services with professional (or “due”) skill and care.
- The duty is imposed regardless of whether it is specifically stated in your professional services contracts (PSCs). A PSC can extend the duty by including phrases such as “highest duty of care” or “utmost skill and care.”
- Standard industry PSCs, such as AS4122-2010 and the Australian Institute of Architects (AIA) document, all contain a clause to clearly set out the standard duty of care expected of a professional. For example: “The consultant shall perform the services to that standard of care and skill to be expected of a consultant who regularly acts in the capacity in which the consultant is engaged ...”

(b) Fitness for purpose background

- Under Australian law, where a person supplies or manufactures goods there is an implied warranty that the goods will be fit for their intended purpose – Competition and Consumer Act 2010 (which superseded the Trade Practices Act 1974).
- The obligation is relevant to building contracts rather than professional services.
- In 2010, amendments were proposed to the Trade Practices Act through the Trade Practices Amendment Australian Consumer Law Bill (no 2).

They proposed removing an implied exemption that had applied to architects and consulting engineers’ services for about 25 years under section 74(2):

“Where a corporation supplies services (other than services of a professional nature provided by a qualified architect or engineer) to a consumer in the course of a business and the consumer, expressly or by implication, makes known to the corporation any particular purpose for which the services are required or the result that he or she desires the services to achieve, there is an implied warranty that the services supplied under the contract for the supply of the services, and any materials supplied in connection with those services, would be reasonably fit for that purpose or are of such a nature and quality that they might reasonably be expected to achieve that result, except where the circumstances show that consumer does not rely, or that it is unreasonable for him or her to rely, on that corporation’s skill or judgement.”

- The premise has been that fitness for purpose guarantees are inappropriate in the context of services provided by architects or consulting engineers and should remain the responsibility of a supplier of the product itself, that is, the contractor.
- Pleasingly, after an industry inquiry reported on the issue, the Federal Government at the time recommended the exemption be retained. Subsequent negotiations with the government led to an agreement to republish the exemption.
- The exemption was also retained under the Competition and Consumer Act 2010 under Schedule 2 Sec B60/61.

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2. Professional indemnity insurance

- The PI market for architects and consulting engineers' services has always aligned itself with the legal position described above and therefore fitness for purpose warranties are excluded from such policies.
- A PI policy is, by its nature, designed to cover professional liabilities, not those applicable to supply or manufacture.
- JMD Ross is unaware of any insurers willing to provide PI coverage to architects or consulting engineers without an exclusion for fitness for purpose liabilities.

3. Clients' current PI insurance policies

- Policies arranged by JMD Ross are some of the widest in the market and JMD Ross has spent a considerable amount of time specifically negotiating policy wordings that benefit our clients. The specifics can be discussed individually with you.

4. Fitness for purpose of design

- Fitness for purpose of design clauses are becoming increasingly common in professional services contracts.
- Such clauses are clearly restricted to obligations about professionals' design duties and so can be clearly distinguished from fitness for purpose of end-product guarantees. Examples of fitness for purpose of design clauses include:
 - The consultant must take reasonable steps to see that the services would be fit for their intended purpose.
 - The consultant must see that any design it prepares and provides for a project would be fit for their intended purpose.
 - The consultant must ensure the services provided are fit for their intended purpose in the context of the obligations set out or reasonably to be inferred from the term of this agreement.
- Our advice to all clients is to omit such clauses from their PSCs as they enhance the common law duty of care to exercise reasonable skill and care.

JMD Ross and clients' insurers are well aware that your clients often take a hard line on omitting fitness for purpose of design clauses so we have considered this in detail in clients' best interests.

- The AIA Client Architect Agreement contains a clause stating that "the architect gives no express or implied warranty that the project or the design is fit for the client's purpose".
- While JMD Ross continues to advise clients to omit such clauses from PSCs because they enhance your potential liability, where that is not possible, law firm CBP offers this advice:

Ensure the "purpose" under such a clause is defined to include the design scope of your services, for example: "The architect warrants and guarantees that its design and documentation is fit for its intended purpose, such purpose as set out in the design scope of works."

It is critical to ensure your "design scope of works" or similar document is restricted to your usual design duties for such an approach to work.

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Such a qualification links the warranty/guarantee to your own duties, thereby limiting the possibility that the clause goes above and beyond the common law position.

- Clients' existing PI policy conditions are crucial to the interpretation above. That includes the "legal liability" basis of cover, performance warranty exclusions, and lack of contract liability exclusions.
- To further ensure you protect your position, JMD Ross recommends such clauses are qualified by referring to your common law duty to exercise "reasonable (or due) skill and care". To that extent, an amended fitness for purpose of design clause could read:

"The consultant warrants and guarantees that its design documentation is fit for its purpose, such purpose being set out in the design brief, having regard to assumptions the consultant can reasonably be expected to make under its duty to exercise reasonable skill and care."

These notes are not exhaustive and, where appropriate, you should seek separate legal advice.

We are always happy to advise you further. Please contact your JMD Ross broker.



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