Construction Insurance - Important Things You Need to Know

CIBSE
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Insurance policies commonly required in construction projects

- Professional indemnity insurance
- All risks insurance
- Public liability insurance
- Product liability insurance
- Employers’ Liability Insurance

(The first 3 will be discussed)

Note: Insurance is aimed at protecting against defects and damages claims/losses.
Insurance provisions in JCT Design and Build Contract, 2011 Edition

- Section 6 and Schedule 3
- Types of insurance required:
  - Public liability
  - Employers’ liability
  - Insurance against non-negligent withdrawal of support
  - Insurance of the works and insurance of existing structures
  - Professional indemnity insurance
Complexity: Number of parties

Contract Diagram for a Traditional Commercial Property Development

- Funder
- Purchaser
- Tenant 1
- Tenant 2
- Developer
- Employer
- Sub-Consultant
- Sub-Consultant
- Structural Engineer
- Services Engineer
- Architect
- Project Manager
- Planning Supervisor
- Quantity Surveyor

= Sub-Contractors
= Sub-sub-Contractors
Complexity: Number of principal agreements
Complexity: Number of procurement methods

- Traditional
- Design & Build
- Partnering
- Management
  - Management Contracting
  - Construction Management
Contents of policies - generic

- **Schedule** - setting out terms specific to actual policy (e.g. limits of indemnity; period of insurance; territorial limits)

- **Policy wording** - standard terms of policy, and extensions/endorsements (if any)
**Terminology**

**The Insured** = The party receiving a benefit on the occurrence of a specified event

**Period of insurance** = The period of time during which the policy operates to provide cover

**Excess/Deductibles** = Amount of each loss borne by the Insured

**Policy Limit/Indemnity** = Total amount payable by Insurers under the Policy; on an each and every claim or aggregate basis [enabling two or more losses covered by the policy to be treated as a single loss for policy limit and other purposes when they’re linked by a specified unifying factor of some kind]

**Primary Layer; Excess Layers** = Policy cover may be arranged in layers. When the primary layer is used up, this triggers the next layer, and so on.
All Risks Insurance

- Covers physical damage to contract works and site materials
- A contract may specify whether the contractor or employer carries the insurance
  - In joint names of employer, contractor and any other party with interest, e.g. funder (e.g. JCT Standard Building Contract)
  - Maintained until Practical Completion
- Contractors also usually carry contractors’ all risks insurance in course of their business
- Cover is on an ‘all-risks basis’ i.e. covered unless otherwise excluded
Public Liability Insurance

- Covers:
  - Damage to third party property
  - Death and personal injury to third parties excluding insured’s employees
- Cover on a losses/events occurring basis, i.e. covers damage, death and personal injury occurring during period of insurance.
- Example of common policy wording: “each and every occurrence or series of occurrences consequent upon or attributable to one source or original cause” basis.
Professional Indemnity policies

- Covers professional negligence
- May include cover for infringement of intellectual property rights, breach of confidentiality and destruction/loss of documents
- Cover on a claims made basis, i.e. claims made during period of insurance (even if damage/loss occurred earlier).
- Example of common policy wording: “any one claim” or “each and every claim” basis
- Defence Costs usually in addition to limit of indemnity
Latent Defects Policies

- Damage caused by defects (unidentified at completion) caused through defective workmanship, materials or design
- No requirement to prove fault [Insurers will take the more expensive process of recovering from parties responsible, via subrogation rights]
- Normally 10 or 12 years
- Typically covers defects in the weatherproof envelope and structure of building, but no other defects
- Availability of cover dependent on insurer being satisfied about original construction and payment of significant premiums
Single Project Insurance

- Composite policy
- Covers differing interests of various parties - Employer and Contractor and possibly others, e.g. sub-contractors
- May include professional indemnity, latent defects, all risks insurance and land and buildings insurance
- Cover ends after expiry of Defects Liability Period
- Decreases costs of duplicating policies; avoids gaps and arguments as to which policy responds
- Rare; limited to large projects; more costly up front
- New potential product: Integrated project insurance
Comparing operation of Professional Indemnity and Public Liability in Claims - Example Scenario

Warehouse floor sinking in places due to piles not being in load-bearing strata.

Piles are in good condition, but need to be replaced with longer piles.

Warehouse floor cracking as a consequence.

Claim against main contractor, flooring sub-contractor (designed and installed the floor) and piling sub-contractor (designed and installed the piles).

Which insurers are involved for each of these parties?
Common exclusions for All-Risks and Public Liability Policies

- Negligent design
- Defective workmanship and materials
- Defective design, plan, specification, materials and workmanship - DE1 to DE5 exclusions.
- Employer’s liability
- Loss or damage to the contracts works during the Defects Liability Period
- Public liability policy will exclude contract works
Common exclusions for professional indemnity policies

- Claims arising out of any performance warranty, guarantee, penalty clause or liquidated damages clause unless the liability would have existed in absence of the clause
- Guarantees of fitness for purpose
- Supply of goods or products
Common exclusions for all policies

- Excess/Deductible
- Previously disclosed/notified matters
- Matters insurable elsewhere
- Exclusions for asbestos and pollution
- Exclusions for US and Canada
Policy exclusions issues - Example (PI policy)

“The Insurer shall not be liable in respect of:
any Claim arising out of liability assumed by the Insured under any contractual arrangement (including any Collateral Warranty or Duty of Care agreement or similar agreement) in respect of:

A) any warranty or agreement under which the Insured assumes a standard of care greater than the standard of reasonable skill and care normally expected in the Insured’s profession

B) any acceptance or guarantee of fitness for purpose

C) any warranty or agreement which provides greater or longer lasting benefit than that given to the party with whom the Insured originally contracted

D) any express guarantee contractual penalty or liquidated damages in so far as liability under such agreement exceeds the amount of the Insured’s liability in the absence of such agreement”
Exclusion (A)- duty of care

- The “permissible” standard is that of the ordinary skilled man exercising and professing to have that special skill

- Usually duty of skill and care expressly provided for in consultant’s appointment

- If it demands something more from the insured, such as “the consultant shall at all times, perform and complete the Services”, it will fall foul of (A)
Exclusion (B)- fitness for purpose

A design obligation, by itself, is fulfilled if undertaken with reasonable skill and care.

Contractors sometimes have an additional contractual obligation that the end product is reasonably fit for the intended purpose. If it is also necessary for the insured to undertake design, that design also needs to ensure that the end product is fit for purpose.

Materials supplied also need to be reasonably fit for the purpose for which they will be used (s.14 Sales of Goods Act 1979).

Failure (to achieve desired result of fitness for purpose) is conclusive evidence of breach of term.

To avoid breaching this exclusion, usual for D&B contractors to limit their design obligation: “The contractor shall have in respect of any defect or insufficiency in such design the like liability as would a professional designer, holding himself out as competent to take on such a design.”
Noteworthy terms contained in all policies

- **Basis of Contract clause** - All statements in Proposal Form constitute part of the Policy
- **Conditions:**
  - **Notification:** Of claim or circumstance that may/are likely to give rise to a claim - e.g. ‘immediately’ or ‘as soon as possible’
  - **Disclosure:** Duty to act in utmost good faith
- **Innocent non-disclosure clause**
Non-Disclosure/Misrepresentation

- Misrepresentation
  - Untrue statement of past or present fact
  - Induces the insurer to enter into the policy
  - Misrepresentation Act 1967 - if negligent misrepresentation, then claim damages
- Non-disclosure
  - Breach of duty of good faith
  - Test (Pan Atlantic v. Pine Top)
    - Materiality (objective)
      - Influence the **prudent** underwriter’s judgment - accepting the risk or setting terms
      - Marine Insurance Act 1906, s18(2)
      - Expert evidence
    - Inducement (subjective)
      - Influence the **actual** underwriter’s judgment - accepting the risk or setting terms
      - Evidence of actual underwriter (or next best person)
- Errors on the proposal form/basis of contract
- Is there an ‘innocent non-disclosure’ clause in the policy.
- Reservation of rights
If during the Period of Insurance the Insured receives any Claim...

... shall as a condition precedent give written notice ... as soon as reasonably possible.

All Claims must be notified prior to the expiry of the Period of Insurance.
No liability for:

A) the consequence of any circumstance
   1) notified under any insurance which was in force prior to the inception of this Insurance
   2) known to the Insured or which should have been known to the Insured at the inception of this Insurance which might reasonably be expected to produce a Claim

B) any Claim made against the Insured prior to the Period of Insurance
Qu: Has the claim been notified properly so that it is covered?

1. Yes
2. No
Answer:

No.

The Courts will most likely enforce a strict interpretation of the policy wording, which would produce an (arguably) odd result - the cover would fall between two policy years on this wording.
What if a party becomes insolvent?

- Third Parties (Rights Against Insurers) act 1930
- Third party with a debt claim provided with a direct claim against insurers for the debt, where the insured is insolvent and certain other specified circumstances exist
Mini checklist when reviewing insurance clauses in construction contracts

- Insurance clauses should reflect the actual cover being maintained.
- Are there any clauses for which cover would be excluded?
- Is there a mechanism to check that the required insurance is being maintained?
- Does the clause require the party to maintain insurance with a reputable insurer and/or a mechanism if the party fails to do so?
- Is the level of cover required sufficient to cover reasonably foreseeable liabilities to the employer and third parties?
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