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Insurance

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Introduction

Construction work involves the production of a long lived capital product. It is the result of the complex interaction of design, construction, finance, law and insurance. This interaction involves a wide range of risks, and one of the fundamental ways of dealing with risk is through insurance.

This seminar note serves as an introduction to insurance and focuses on those issues raised by construction insurance, which may be considered under three main parts. First, the fundamental principles of insurance and the general classes of construction insurance. Second, the types of insurance available in the construction industry and some specific aspects arising from construction insurance. Finally, insurance under the standard forms.

General principals

There is no statutory definition of insurance. This may be surprising given the volume of legislation regulating insurance companies and the manner in which they conduct their business. However, a widely recognised general description of the nature of insurance was provided by Channell J. in the case of *Prudential Insurance Co. v IRC* [1904] 2 KB 658:

> "It must be a contract whereby for some consideration, usually but not necessarily in periodical payments called premiums, you secure to yourself some benefit, usually but not necessarily the payment of a sum of money, upon the happening of some event…the event should be one that involves some amount of uncertainty. There must be either uncertainty whether the event will happen or not, or if the event is one which must happen at some time there must be uncertainty as to the time at which it will happen. The remaining essential is…that the insurance must be against something."

The leading texts on insurance law refer to this case as offering a widely recognised or general description and so it appears that the case is widely recognised today. Levine and Wood consider that Channell J's description identifies five main requirements:

1. Contract;
2. Consideration;
3. Benefit on the happening of some event;
4. Uncertainty; and
5. Against something.

1. Contract

Insurance is essentially a creature of contract in which the insurer indemnifies the insured in certain circumstances. Contractual principles apply and the insured is contracting on the basis that its claim will be properly considered, rather than the hope that the insurer might exercise a discretion in the insured's favour. The insurance contract is usually referred to as a "policy" which is a document issued after the insurance has been entered into. An insured normally completes a proposal form and the insurance is effective when the insurer initials a document called a "slip". Peculiarities of insurance law are such that the slip is not the contract of insurance, but merely evidence of its terms. If the policy document does not accurately reflect the terms of the slip, then it is possible to rectify the policy.

Hudson (page 1424) considers that insurers, much like Bondsmen:

> "expend considerable ingenuity in drafting and designing policies which on the surface appear to offer, but on informed and close analysis do not, the full protection expected and required by the assured, and also in implying any device of subrogation, or of settlement of claims in return for assignment of rights, in order to transfer, reduce or eliminate their own liability".

Care is needed when considering the wording of an insurance policy, the interpretation of which will turn upon the particular terms used. Particular attention must also be given to the notice mechanisms set out in the policy which must be followed when making a claim.

A recent case dealing with the interpretation of policies of insurance is *Pilkington United Kingdom Limited v CGU Insurance Plc* [2004] EWCA Civ 23. In that case the appellant, Pilkington, was the manufacturer of heat soaked toughened glass panels that had been installed in the roof and vertical panelling of the Eurostar terminal at Waterloo. Some of them proved to be defective. Pilkington were joined to proceedings commenced by Eurostar against the contractor and professional team. Pilkington made a contribution, recovered some money from their professional indemnity insurers and sought a further sum from CGU under the terms of a products liability insurance policy.

In order to make out the claim, Pilkington had to demonstrate that their loss arose from "physical damage to physical property not belonging to the insured". The panels manufactured by Pilkington had not caused any damage to the terminal but because of the fractures they presented a future risk of damage and possibly injury to persons. The court had to consider whether this potential future damage was damage covered by the policy. The Court of Appeal rejected Pilkington's argument that a potentially dangerous or defective product could constitute a "loss of or physical damage to the other property not belonging to the insured." Therefore, the defect was not covered by the policy.

Horbury Building Systems Limited v. Hampden Insurance NV [2004] EWCA Civ 418 is another case about the extent of cover offered by an insurance policy. Horbury Building Systems Limited had erected ceilings within in a cinema complex. The ceiling to one of the cinemas collapsed, and the whole complex closed for several weeks. Clause 4.1 of the insurance policy said that Hampden Insurance would indemnify Horbury Building Systems "in

respect of … damage to the Property". Horbury Building System argued that the loss of profit caused by the closure of the entire cinema complex arose as a consequence of the damage to one of the cinemas. The insurance company did not agree, believing that the damage related only to a single cinema and not the whole complex. The judge agreed with the insurance company, and Horbury Building Systems appealed.

The Issue for the Court of Appeal was whether the closure of the complete cinema complex as a result of one ceiling collapsing and/or was the closure of the complex consequential damage caused by the collapsed ceiling? They decided that the Judge at first instance was correct. The insurers had not indemnified Horbury Building Systems for loss of profit to the whole cinema complex. The policy covered liability for the physical consequence of the collapse of the ceiling in the cinema and the economic or financial losses caused by that physical damage. It did not extend to the closure of the entire cinema, especially given that the collapse of the ceiling in one cinema did not prevent the rest of the complex from operating.

This was a case, therefore, about the extent of cover offered by the insurance policy. The insurance company indemnified the builder in respect of the financial consequences of damage to the property. In this instance, the damage was caused to only one cinema, and so the building was covered for the financial losses arising from the loss of the use of that cinema. However, it did not cover the building for closure of the rest of the complex, even if the builder was held liable for the cinema operator's loss of profit for the whole development. The case demonstrates, as indeed do may insurance cases, that insurance cover is only as wide as the terms of the policy which may be more limited than the liability of the insured to others.

2. Premium

The policy provides for a premium which is to be paid by the insured as consideration for the policy. The premium may be paid periodically or as a one off payment. The Court of Appeal in *Hampton v Toxteth Co-operative Provident Society Limited* [1915] 1 Ch 721 held that an absence of a premium was not fatal to the formation of insurance. In practice, policies state that the payment of the premium is a condition precedent to the insurer's liability.

3. Benefit

The benefit conferred is usually "monies worth" although an insurer might elect reinstatement. It is worth considering, at this stage, the distinction between indemnity based insurance and contingency based insurance. In the case of *Medical Defence Union v Department of Trade* [1979] 2 AER 421 Megarry VC described indemnity contracts as providing an indemnity against a specific loss such as fire. On the other hand, contingency contracts provide a payment contingent upon an event such as death.

4. Uncertainty

Uncertainty relates to the risk of the occurrence of an event which leads to loss. From a practical point of view, risk managers often make a distinction between risk and uncertainty. The term "risk" is associated with a loss which can be predicted and therefore can be insured. On the other hand, uncertainty cannot be predicted and therefore cannot

be insured. The purpose of this somewhat artificial distinction is to classify and categorise risks and the chances of loss associated with those risks.

5. "Against something"; insurable interest

Finally, the statement that insurance must be "against something" is generally taken to mean that the insured must have an insurable interest in the subject matter.
Insurance law is, therefore, essentially one of contract but there are perhaps eight fundamental principles which are peculiar to the area of insurance contracts. Before considering these principles it is useful to outline the component parts of the insurance market.

The insurance market

The insurance market in the United Kingdom has three main tiers:

1. The brokers who arrange insurance on behalf of their clients and act as intermediaries;
2. The underwriters, insurance companies and the societies who take on the risks; and
3. The loss adjusters or loss assessors who negotiate and settle claims on behalf of the underwriters or the insured.

The number of organisations providing insurance has been steadily reducing due to amalgamation. Insurance is therefore being undertaken by a decreasing number of expanding organisations. A distinction can be made between proprietary institutions (capital being received from shareholders) and the mutual societies where the benefits of any profits accrue to the policy holders. In addition to these insurance companies and societies, there is of course Lloyds of London. The development of Edward Lloyd's Coffee House in London in the 17th Century is widely known and is probably the most important insurance institution in the world. Currently, however, Lloyds only accounts for around one third of British insurance business. The corporation does not in fact undertake insurance business, as this is done by its members. The underwriters are authorised to agree to insurance, set the premium and issue the insurance policy.

Fundamental principles

Insurance law builds upon a range of fundamental principles, although the number of principles vary depending upon the manner in which the subject is analysed. For the purposes of construction insurance, there are eight fundamental principles:

1. Insurable Interest

A fundamental requirement of insurance law is that the insured must have a "insurable interest" in the subject matter of the insurance. An insurable interest is an interest which is recognised and enforceable at law. It may be legal or equitable, a proprietary right or a contractual right. So, any one who is liable (or potentially liable) by contract to pay a sum of money in the event of a lost property will have an insurable interest. The term "insurable interest" is not defined, nor is the law in the area settled.

Chitty on Contracts (26th Edition) (page 4, 207) states:

> "It is generally true that a person who would forseeably suffer financial loss from the occurrence of an event has an insurable interest in the subject matter which it is sought to insure against that event."

An insurable interest includes all legally enforceable liabilities whether they are based on a statutory duty, in tort or in contract. It is essentially a pecuniary interest in the subject matter of the insurance, so that upon the happening of an event the insured suffer any loss or some legal liability.

An insurable interest is not required under general contract law, but is necessary under insurance because:

1. of a statutory requirement; and/or

2. it is inherent in the nature of the contract of insurance (e.g. indemnity insurance).

Section 1 of the Life Assurance Act 1774 states that insurance covered by the Act must relate to an insurable interest. If an insurable interest is absent then the policy is null and void. The Act does not just apply to life cover, but also to "any other event or events whatsoever" and is therefore wide enough to cover indemnity insurance. The Act does exclude some risk, for example "insurance on ships, goods and merchandises".

In relation to construction, it is usual practice for the main contractor to insure in his own name and also on behalf of the sub-contractors for the entire work against all risks. This is the basis of contractor's all risks "CAR" policy. This principle was challenged in the case of *Petrofina (UK) Limited v Magnaload Limited* (1983) 2 Lloyd's Rep 91. The main issue in that case was whether the head contractor's name could be used in subrogation proceedings against an allegedly negligent sub-contractor who had caused the loss. The Court refused to allow it on two grounds:

1. On the construction of the insurance policy, the defendants were sub-sub-contractors for the purposes of the policy and were therefore joint assured. Rights of subrogation are not available against those who are joint assured; and

2. Each insured under the policy was covered in respect of the whole of the works.

Recently, the case of *Deepak Fertilisers and Petrochemical Corporation v Davy McKee (London) Limited & Others* [1999] BLR 41 CA touched on the subject of insurable interest, the case involved a methane plant which had exploded after the plant had been completed. The employer and contractor had the benefit of joint insurance during the course of the works, but the question arose as to whether the contractor maintained an insurable interest after the plant was complete. The Court of Appeal held that the contractor had an insurable interest during the construction of the plant as damage would prevent the contractor from earning remuneration from the contract. However, co-insurance ceased once the works were complete and so the contractor could not rely on the *Petrofina* argument.

2. Utmost good faith

The principle of utmost good faith is frequently referred to by the Latin tag of "Uberrimae Fidei" which means the most perfect frankness. It requires each party to make full disclosure of all material facts which might influence the other party in deciding whether to enter into the contract. The principle operates to some extent in other areas of the law, for example; suretyship, guardian and award, solicitor and client etc, but it is a fundamental principle of insurance law.

The classic statement of the principle is set out in the case of *Carter v Boehm* (1766) 3 Burr 1905:

> "Insurances of contract upon speculation. The special facts, upon which the contingent chances to be computed, lie commonly in the knowledge of the insured only: the underwriter trusts to his representation, and proceeds upon confidence that he does not keep back any circumstances in his knowledge, to mislead the underwriter into a belief that the circumstance does not exist, and to induce him to estimate the risque as if it did not exist. The keeping back of such circumstance is a fraud, and therefore the policy is void. Although the suppression should happen through mistake, without fraudulent intention: still the underwriter is to cease and the policy is void, because the risque run is really different from the risque understood and intended to be run at the time of the agreement".

It appears that the only remedy for non disclosure is avoidance of the entire contract. The duty arises because it is generally only the insured that is in possession of all of the facts concerning the risk, and so the insurer must be entitled to rely and trust the representations made by the insured. The duty does, however, apply equally to the insurer as well as the insured.

Utmost good faith is therefore essentially about a duty of disclosure which requires each party to:

1. Disclose all material facts known to them; and

2. Not to misrepresent any of the material facts. This will include statements which are true but which are misleading because they are incomplete (*Aaron's Reefs v Twiss* [1986] AC 273).

A fact is material if it *might* but not would influence the judgment of a prudent insurer in deciding whether to take on the risk and in fixing the level of the premium. It is not necessary that a prudent insurer would refuse the risk or even charge a higher premium, but would have liked the opportunity merely to consider the position (*Container Transport International Limited v Oceanus Mutual Underwriting Association* [1982] 2 Lloyd's Rep 178 CA and *Saint Paul's Fire and Marine Insurance Co (UK) v McConnell Dowell Constructors* [1993] 2 Lloyd's Rep). However, the leading House of Lords case *Pan Atlantic Insurance Limited v Pinetop Limited* [1994] 3 WLR 677 clearly indicates that the insurer cannot merely rely on the non-disclosure, but must prove that they were induced by the non-disclosure.
The majority of the disputes in the area of good faith relate to the materiality. Material facts are facts which affect the risk and may be classified as;

1. Physical facts – concerning the likelihood of loss or the degree of loss; or

2. Moral hazards – concerning whether the insured is a fit person to insure, because for example, the insured has a criminal record for dishonesty.

The duty is a positive one and therefore omission can constitute a breach. Importantly it may not be sufficient simply to answer the question set out in the proposal form. Care needs to be taken and material facts not specifically requested in the proposal form must be disclosed.

This fundamental principle applies to formation of the insurance contract and also at each renewal. It is common practice for the policies to include a term requiring the insured to notify the insurer of any material fact arising during the term of the policy. If the policy contains such a term then the duty of utmost good faith will also apply to these communications (*Black King Shipping Corporation v Massie, "the Litsion Pride"* [1985] 1 Lloyd's Rep 437).

A breach of the duty of utmost good faith allows the innocent party to avoid the contract. Essentially, the contract is rendered voidable at the insurer's option. Any money paid over by the insurer must be repaid. A breach by the insurer would allow for return of the premium, but it does not give rise to a remedy in damages.

If all or part of a claim is made fraudulently the insured cannot recover any part of the claim (*Manifest Shipping Co Ltd v Uni-Polaris Co Ltd* (2001) UKHL 1). The same rule applies to a claim that was made honestly, but is later fraudulently exaggerated or supported by fraudulent evidence (*Agapitos v Agnew* (2002) EWCA Civ 247).

A fraudulent claim will not only be void, but will void another otherwise valid claims that have been made. In the case of *Axa General Insurance v (1) Clara Gottlieb (2) Joseph Meyer Gottlieb* [2005] EWCA Civ 112 the insured defendants made 4 claims in respect of property damage. Two were validly made, but the other 2 were found to be tainted by fraud. At first instance the judge held that the 2 fraudulent claims were void, but the other 2 were valid. The Court of Appeal did not agree. They held that the effect of a fraudulent claims was to retrospectively remove the insured's existing cause of action. This mean that even the valid claims were void. Their reasoning was that those who are insured should not have the expectation that if the fraud fails they will still recover the valid claims and therefore loos nothing by making the fraudulent claim.

3. Indemnity

A fundamental principle of insurance is that the insured can only recover what it has lost. If the principle is not expressed, then it will be implied. There are three exceptions. First, life policies, second, value policies where the parties agree the value of the subject matter, and finally, where a surplus arises following a subrogated claim.
In practical terms, this means that the occurrence of an event covered by the insurance policy does not in itself entitle the insured to payment. The sum could of course be further restricted by the limit of indemnity stated in the policy which affixes the maximum liability of the insurer. An insured can only recover the actual loss that he is able to prove and is not allowed to make a profit.

4. Subrogation

Subrogation is the complimentary principle of indemnity. It arises from two principles of common law. First, an insurer cannot avoid liability on the basis that the insured has a right to claim against some third party (*Colinridge v Royal Exchange Assurance* [1877] 3 QBD). Secondly, a third party cannot avoid liability to an insured on the ground that the insured will be indemnified for the loss by way of insurance (*Bradburn v Great Western Railway* [1874] LR 10 Ex 1).

The principle of subrogation provides the insurer with two benefits:

1. To stand in the shoes of the insured and avail himself of all the rights and remedies available to the insured against the third parties (*Masons v Sainsbury* [1782] 3 KB 61). The action by the insurer is brought in the insured's name and the third party can raise any defences which would have been available against the insured; and

2. To recover from the insured any benefit received by the insured from third parties which reduces the loss covered by the insurance (*Castellain v Preston* [1883] 11 QBD 380 CA).

These principles have an important and far reaching impact upon the relationship between the insured and the insurer, and the practical implications of the occurrence of a loss. For example, if the insured agrees to waive all claims against the third party then the insurer would be able to sue the insured for the amount otherwise claimable. By way of further example, the expiry of the limitation period would be a defence available to the third party.

The insurer can only exercise a right of subrogation when:

1. The insurance is indemnity insurance;

2. The insurer has made payment under the policy, unless the policy provides otherwise. However, it is not clear whether the insured must have been fully compensated; and

3. The policy does not exclude the rights of subrogation. It may be possible to exclude subrogation from the policy for an additional premium.

This last point is particularly applicable to construction operations. In return for an additional premium, the insurer might waive its subrogation rights against all other parties connected with the particular construction projects. Rights of subrogation cannot be exercised against those jointly insured under an insurance policy (*Petrofina (UK) Limited v Magnaload Limited* [1983]).

In addition, rights of subrogation cannot be exercised against a body who although not named as an insured is a party for whose benefit (even if only in part) the policy had been taken out and who had contributed to the premium (*Mark Rolands v Bernie Inns Limited* [1985] 3 AER 473). It may be that the Court of Appeal in *Bernie Inns* based the decision on both the third parties contribution to the premium and the insured's intention to insure on the third party's behalf. In that case the third party was a tenant who had paid for the insurance by way of an "insurance rent".

The parties can in their primary contract agree that they will be joint insured, or that one will insure for the benefit of the other, which has the similar effect. An example of the latter, is the case of *BP Exploration Operating Co. Limited v Kvaerner Oil Field Products Limited* [2002] 2 AER 266. In this case Kvaerner entered into a contract with BP for the design, engineering and procurement of sub-sea control modules which were to be used to recover oil from the seabed. Faults were discovered in the equipment. BP then suffered losses associated with recovering, repairing and replacing the equipment from the seabed. A claim was brought by BP that was pursued by its insurers who had exercised their rights of subrogation.

Clause 10.5 of the contract provided that BP would take out and maintain insurance against physical loss or damage and general third party liability. However, BP argued that the cover was in respect of loss or damage arising from the performance after the manufacture and installation. By contrast, they argued that the losses flowed from events occurring during the manufacture, because it was the faulty manufacture that led to the problems and the loss.

The court concluded, based upon expert evidence, that it was common practice in the oil and gas industry for main contractors to have the benefit of the insurer's cover damage under the operator's policy. Kvaerner pointed out that their contract sum did not take into account the cost of their obtaining all risks cover, because the contract provided that BP would take out that type of cover. Mr Justice Colman concluded that BP was obliged to provide Kvaerner with the benefit of an all-risks policy. That insurance should therefore have covered Kvaerner's performance, as a result the insurance company could not use its rights of subrogation against Kvaerner. The claim against Kvaerner therefore failed.

5. Proximate cause

The principle of proximate cause is implied into contracts of insurance and requires the insured to show that the loss was caused by an insured peril. Proximate cause means the effect of the common, dominant or real cause of the loss and will be a question of facts in each case. The principle may of course be modified or even excluded by the contract. It is therefore important to consider the two following questions when applying the principle:

1. Is the loss caused by an insured peril? If there has been a succession of causes, the last of which has been insured against, then the loss was caused by that peril. Where the preceding cause (not the last cause) is the one insured against, then one needs to consider whether the last cause was so closely connected with the preceding one (which is of course the effect of the last cause) that the loss is the effect of the preceding cause and therefore caused by an insured peril. Basically, if there is no break in the sequence of causes the insured peril is the cause of the loss. If a new and independent cause interrupts the sequence then the cause is the intervening cause, which may or may not be insured against. Finally, where causes operate concurrently the cause is taken to be the insured peril and the other causes are ignored.

2. Is the loss caused by an excepted cause? If an insured peril and an excepted cause arise independently then they are covered by the insurance contract (in the same manner as concurrent causes referred to above). However, if the

loss appears to be due to the combined operation of an insured peril and an excepted cause then the outcome will vary. First, if an insured peril is proceeded by an excepted cause then there is no loss as the peril insured against resulted from the excepted cause. This is unless the insured peril is a new and independent cause of the loss. Second, if the excepted cause precedes the insured peril then the loss will be covered providing that there is a causal connection with the loss. Finally, where the loss is caused by the combined operation of two concurrent and independent causes (one insured peril and one excepted cause) the loss is not covered. This is because the loss would have been caused by the excepted cause in any event.

6. Contribution

An insured may have more than one insurance policy covering the same loss. An insured can recover the full amount of his loss from whichever insurer or insurers he chooses unless a term of the policy or policies in question provide for the contrary. In any event, an insured cannot recover more than his total loss regardless of the number of insurance policies because of the principle of indemnity.

The right of contribution allows an insurer who has discharged its obligations to an insured, to claim from the other insurers their proportion of the payment. The right of contribution is an equitable right between the insurers. In order for an insurer to exercise this right the insurance policy must:

1. Cover the particular event;

2. Cover the same subject matter; and

3. Contain no provision stating that the policy only applies after other insurances have been exhausted.

This final proviso is referred to as a "non-contribution clause" and is frequently encountered in policies.

Another frequently encountered clause provides that in the event of double insurance the insurer will only pay a rateable proportion of the loss. This means that the insurer will only be liable for a rateable proportion. The effect is that an insured may not recover the full loss if an insurer under one of the policies is entitled to avoid payment for any reason. On the other hand, where two policies both contain a provision stating that where another policy covers the same risk then indemnity cover will not be provided, the Court will not allow the policies to cancel each other out (*Steelclad Limited v Iron Trades Mutual Insurance Co Limited* [1984] SLT 304).

7. Warranties

A warranty is a term of the insurance policy which if broken entitles the insurer to terminate the contract from the time of the breach regardless of whether the breach is material. In the law of insurance the term "warranty" is therefore used in a similar sense to that more readily associated in general contract law with the term "condition". Breach of a

warranty justifies the injured party's refusal to further performance. The policy will usually establish express contractual warranties which may or may not relate to the risk and loss. For example, the insured usually warrants that its statements in the proposal form (and therefore the contract of insurance) are true and "the basis of the contract" which has the effect of converting the insured's answers into warranties. Breach entitles the insurer to avoid the contract from the date of the breach.

The position is given a statutory footing in section 33(3) of the Marine Insurance Act 1906 which states that "a warranty is a condition which must be exactly complied with. If it is not so complied with, then…the insurer is discharged from liability as from the date of the breach of the warranty". These words were considered by the House of Lords in *Bank of Nova Scotia v Hellenic Mutual War Risks Associates (Bermuda) Limited "The Good Luck"* [1991] 2 WLR 1279 where a ship had been insured under a policy which entitled the insurers to declare certain areas as prohibited. The policy was assigned to a bank and the insurers undertook to notify the bank promptly if they ceased to insure the ship. The ship was struck by an Iraqi missile while trading in the Persian Gulf which had been declared by the insurers as a prohibited area. A claim on the policy was rejected by the insurers as the ship had been in a prohibited area. The House of Lords held that the insurers were liable on their undertaking to the bank. The insurers had "ceased to insure" the ship as soon as she had entered the prohibited area. This breach of "warranty" automatically released the insurers without any need for them to give notice.

8. Reinsurance

Reinsurance is a means by which insurers insure themselves by the passing on or "laying off" part of their liability to a re-insurer.

Third Parties (Rights Against Insurers) Act 1930

The Third Parties (Rights Against Insurers) Act 1930 allows a third party who has a claim against an insolvent insured to stand in the shoes of the insured and make a direct claim against the insurers. The Act only applies in the following circumstances:

1. The insured becomes bankrupt or goes into liquidation either before or after incurring a liability to a third party under section 1(1) of the Act;
2. There is a contract of insurance; and
3. The insured is liable to the third party.

The Act only applies where the insured's liability to a third party has been established by a judgment, award or admission and so the insured may raise the defence that the third party has not pursued the insolvent insured to judgement (*Post Office v Norwich Union* [1967] 1 AER 577; *Bradley v Eagle Star Insurance Co Limited* [1989] 1 AER 961). A claim which has not been settled is insufficient. It is not unusual for the insured company to have been dissolved and removed from the Register of Companies. If this has occurred then the insured company must be restored to the register for the purposes of being sued under section 651 of the Companies Act 1985 and section 141 of the Companies Act 1989.

The Act provides that the third party receives identical rights against the insurer as were initially possessed by the insured. This of course means that if the insurer has a right to avoid the policy or deny liability then those rights continue against the third party (*Aswan v Iron Trade Mutual*). For example, if the notification provisions have not been complied with then the third party may not be able to recover under the policy.

Section 3 allows the third party to avoid any agreement which restricts the insured's rights against the insurer after the insured has become insolvent. Unfortunately section 3 does not apply to pre-insolvency agreements limiting the insurer's liability. The case of *Normid Housing Association Limited v Ralph and Others* [1989] 1 Lloyd's Rep 265; 43 BLR 18 highlights problems in this area. In that case the defendant was being sued for negligence by the plaintiff and decided to settle with his own insurers in respect of the total claim thereby releasing the insurers. The plaintiff sought an injunction to prevent the settlement as the defendant would be unable to meet even a small proportion of the damages. The Court refused the injunction on the basis that the defendant was not obliged to effect professional indemnity insurance or deal with the policy in any particular way. Had the defendant become bankrupt before the agreement then the plaintiff would have been able to use the 1930 Act to step into the shoes of the bankrupt defendant and bring a claim directly against the insurers.

Section 2 of the Act allows the third party to obtain details relating to the insured's policy from not only the insured but also the insurer for the purposes of enforcing third parties rights vested in him under section 1. Once again, case law in the area shows that this right is relatively restricted. It was held in *Upjohn v Aldridge States Investment Co* [1993] 1 Lloyd's Rep 535 that section 2 is only applicable once the insured's liability has been established as it is only then that the rights are transferred. This means that, in the absence of an admission of liability, the third party will have no choice but to sue the insolvent insured before the third parties becomes entitled under the Act to establish whether the insured has liability insurance (and of course whether the insurers have any right to deny liability for the claim).

More recently the case of *First National Tricity Finance Limited v OT Computers Limited (In Administration)* [2004] EWCA Civ 653 provided some relief to the restricted approach that has been taken to the scope of Section 2 of the Act in the past. In this case OT Computers gave its customers extended warranties and First National Tricity Finance provided credit to OT Computers' customers. As part of providing the finance facility, First National became liable to the customers under the warranty claim. If a claim was made OT Computers compensated First National. However, OT Computers went into administration. OT Computers had an insurance policy with AXA in respect of these warranty claims. First National Tricity tried to rely upon the 1930 Act to bring a claim against AXA because OT were worthless.

First National tried to obtain a copy of the policy but were refused. First National then sought a Court Order. OT Computers argued that the policy of insurance did not cover the liability, but in any event, they were not obliged to provide a copy of the policy until OT Computers was found liable by way of a judgment, or award.

The Court of Appeal did not accept that this was correct. They pointed out that the wording of the Act was very general and covered liabilities that might arise. Further, the Court of Appeal recognised that a third party needed to know whether the party in

administration had an insurance policy that would meet the claim. The Court of Appeal believed that this was the purpose of the Act. As a result of this more recent case, it seems that a third party does have a right to seek the insurance policy in order to determine if the policy covers the claim, regardless whether liability has been established.

Whilst the act is useful it is relatively restricted in its application. It is therefore sensible to seek the co-operation of the defendant and their insurers before commencing proceedings under the Act.

Insurance mediation directive

The Insurance Mediation Directive (2002/92/EC) came into force by an amendment to SI 2003/1476 to the Financial Service s and Markets Act 2000 (regulated activities) Order 2001 (SI 2001/544). It came into force on 14 January 2005 and introduces EU regulation dealing with insurance brokers and others that provide insurance services. These are referred to as "Insurance Mediation Services".

An insurance mediation activity basically includes advising on dealing in or arranging contracts of insurance. It covers an agent or person assisting in the administration of an insurance contract. It only applies to those who act in this capacity as a part of their business, which requires them to receive some form of payment by virtue of their activities. The payment can be made to them indirectly. The main aim therefore of the legislation is to regulate insurance providers and insurance brokers.

However, the frequently encountered standard forms, and even bespoke forms, used in the construction industry establish joint insurance policies and include a waiver of subrogation rights. So, for example, a contractor constructing a new build development under the Standard JCT 1998 Form will take out insurance in the joint names of himself and also the employer. The contractor will be paid by the employer. As a result, it seems that the directive will apply to the contractor who is carrying out an insurance mediation service. Further, the contractor may be in a similar role when arranging insurance for a project which effectively covers the sub-contractors.

The effect of the Insurance Mediation Directive is that any person carrying out insurance mediation services must be authorised by the Financial Services Authority, be an appointed representative or agent of an authorised person or fall within one of the exceptions. A breach of the regulations is a criminal offence and may result in an unenforceable contract of insurance. The consequences are therefore extremely important.

One reading of the legislation is that the person arranging the insurance must receive remuneration from "third parties" (Recital 11). If, as is the usual case, the contractor is arranging insurance for himself and others, then it seems unlikely that the contractor will be caught by the directive. Nonetheless, there is currently no court ruling on this point. Further, other forms of procurement could lead to a position where a contractor, or someone else in the procurement chain is effectively arranging insurance for others. Under those circumstances, it seems highly unlikely that the person in question would be caught by the directive and would need to be authorised.

Classes of insurance

There are two main categories of insurance. The first relates to damage occurring to property or the works themselves during construction and is referred to as "property" or "works" insurance policies. This category covers the property, contract work, materials, equipment and machinery connected with it. The second category is liability insurance dealing with claims by third parties for personal injury and property damage.

The insurance market has then generated a range of discreet insurance products dealing with sub-divisions of these categories, and the insurance policies available in the market place may cover one or more of the sub-categories and even cover both main categories identified above. The categories of insurance table set out in Table 1 below identify the main insurance sub-divisions relating to construction work:

	Property Insurance or "works" insurance covers the property, damage to the contract works, materials, equipment and machinery connected with the works	**Liability Insurance** covers claims by third parties for personal injury and damage to their property
Developer	1. Covers any part of the works taken over 2. Latent defects 3. Loss of profit/rent	1. employer's liability 2. public liability – for a limit in excess of that required by the contract, or limit not indemnified by contractor 3. public liability for non-negligence
Design Team		1. employer's liability 2. public liability 3. professional indemnity
Contractor	1. contractor's all risk "CAR"	1. employer's liability 2. public liability 3. public liability for non negligence 4. professional indemnity for design undertaken by contractor 5. motor insurance 6. marine insurance

Table 1: Adapted from figure 1 in Levine and Wood (1991)

A further distinction may be made between a "single policy" and a "floater policy". A single policy provides cover for the whole or a part of a specific project. A floater policy is an annual policy maintaining cover on a range of projects undertaken during the term. It

is not possible to get a single policy covering all classes of insurance for a construction project as the insurance industry currently considers that the risks are too vast.

The more common classes of insurance are considered below.

Property or material damage

A material damage policy covers loss or damage to the property in which the insured has an insurable interest. It will only cover loss or damage to the property specified. A contractor's all risks "CAR" policy is a material damage policy. It usually covers the contract works, construction plant during the course of construction and whilst being erected and dismantled, goods in transit and damage to employee's property.

Liability Insurance

Liability insurance covers the insured's liability to third parties. There are three main types:

1. Employer's liability – The employer's liability to his employees under a contract of service or apprenticeship for personal injury or disease arising out of the course of employment. Employer's are required to maintain employer's liability insurance under the Employer's Liability (Compulsory Insurance) Act 1969 which came into force in 1972. The statutory minimum is £2 million per occurrence, although until 1994 most insurers offered cover on an unlimited basis. However, since 1994 most standard policies provide cover up to a maximum of £10 million.

2. Public liability – This covers liability for accidental injury or death to any person (other than employees) and loss or damage to a third party's property. Usually designed to cover common law liability to adjoining owners and the general public arising during the course of or in connection with the work on site. Public liability insurance therefore covers the contractor's liability to the employer for damage to property which is adjacent to the site but not belonging to the employer.

   Most standard forms of construction contracts provide that the contractor indemnify the employer in respect of the liability covered by public liability insurance. However, it is usual for the indemnity to exclude liability caused by the negligence of the employer or the employer's agent. It is therefore sensible for the employer to maintain public liability insurance in respect of his own negligence.

3. Professional Indemnity – Indemnifies the insured against legal liability arising from the insured's professional activities. The activities can of course vary tremendously, and therefore must be defined in the policy.

Claims procedure

There is probably an implied duty to give insurers notification of any loss which occurs and that the duty of utmost good faith will also apply to that notification (*The Litsion Pride*). A method of notification is usually dealt with in some detail in an insurance policy,

and indeed absence of such a provision in a policy would be exceptionally unusual. Most policies require notification to be given of any circumstances which *might* give rise to a claim. This means that the insured must give notice of any event which could give rise to a claim and it is not sufficient to wait until a claim is made.

Policies usually require notification to be made "immediately", "forthwith" or "as soon as possible". These terms have been held to imply prompt and vigorous actions without any delay. In such circumstances it will be vital that an insured notifies the insurer of the circumstances or claims as failure may allow the insurer to avoid the policy. In the absence of any express term the notification should be made within a reasonable time.

The manner in which notification is made is once again usually expressed in the policy. This must be strictly followed. It may be sufficient to notify the agent or broker, although it is preferable to notify the insurer direct.

The notice must include "such as will enable the party to whom it is given to take steps to meet the claim by preparing and obtaining appropriate evidence for that purpose" (*A/S Rendal v Arcos Limited* [1937] 3 AER 577). It is perhaps best to keep the notification fairly general as a specific notice may amount to non-disclosure at a later date.

Particular aspects of construction insurance

The following section considers some of the main aspects arising from construction insurance. Contract works insurance and professional indemnity insurance are initially considered before reviewing some of the more frequently encountered discreet construction specific policies.

Hudson considers that:

> "It is of crucial importance to appreciate that required insurance is almost invariably defined, in both areas, to cover those situations where the contractor would otherwise be contractually responsible to the owner by virtue of express or implied terms of the contract if no insurance was present." (Hudson, 15.002 page 1422)

The purpose of insurance in construction contracts is to cover losses which would normally be incurred by the contractor as a consequence of the contractor's contractual liabilities to the employer, but for commercial practical reasons, the employer pays for the insurance in order to "safeguard himself against the heavy losses" that he would incur if the contractor did not have the financial resources to meet those liabilities. The standard forms address this issue by the inclusion of dual provisions. First, the contractor indemnifies the employer against specific liabilities and, second, the contractor or employer are contractually obliged to insure those liabilities. For new construction works it is usual for the contractor to insure the works, whilst civil engineering works are normally insured by the employer. The decision is mostly economic, in the sense that most building contractors are able to obtain a more economic premium than employers, whilst on the other hand employers for large civil engineering projects are able to obtain more economic premiums, mostly due to their size and financial standing. Regardless of whether the employer or the contractor insures it is usual for the policy to recognise both of them as joint insured.

Joint names insurance and sole risk

A joint named insurance policy simply recognises that more than one person is insured under the policy. It may be appropriate where several parties have an interest in the property (for example, the contract works) or where the policy is intended to cover the legal liability of more than one person.

The usual rules apply and so each insured should obtain from the insurers confirmation of cover regardless of any act or omission of another insured, for example, non-disclosure. One of the benefits of being named as joint insured is that the insurer will not be able to exercise the usual rights of subrogation against any of the joint insured as this would amount to depriving the insured of a remedy (*Simpson v Thompson* (1877) 3 APP Cas 279 HL; *Petrofina* [1984]. The same result is achieved if the building is placed at the "sole risk" of one party and that party is required to insure the building. Such an arrangement prevents the employer from suing the contractor because the term "sole risk" has been held to place the risk of negligence by the contractor solely upon the employer (*James Archdale & Co Limited v Comeservices Limited* [1954] 1 AER 210, [1954] 1 WLR 459, CA).

In addition, the Court of Appeal in *Norwich City Council v Harvey* [1989] 1 WLR 828; [1989] 1 AER 1180 held that the negligent sub-contractor was protected from the attempts of an insurer to exercise its rights of subrogation, and further that the sub-contractor did not have a duty of care to the employer. In that case property damage was caused by a sub-contractor's employee who negligently started a fire. The Court of Appeal appears to base its decision on the fact that the works were at the employer's sole risk and that this clearly demonstrated that the sub-contractors were not to be held liable.

Noting of interests

The noting of interests is an alternative to arranging cover in joint names. However, noting confers no legal right against the insurers unlike joint names cover. For example, the insurer is not under an obligation to inform the noted party if cover ceases. In theory, an insurer could exercise rights of subrogation against the noted party, however, in practice this is unusual.

The Association of British Insurers has established a scheme between its members and specified banks under which the insurer gives an undertaking to a Bank whose interest has been noted on the policy. The insurer undertakes to notify the Bank of certain breaches or cancellation of the insurance and gives the Bank an opportunity to maintain the policy by paying the premium.

Contract works insurance

This must be the most important insurance in terms of providing protection to the employer under a building contract. Works insurance insures the works executed by the contractor against damage from the insured risks during construction. As a minimum, the usual insured risks are fire, lightning, explosion, impact, storm, bursting and overflowing of pipes and tanks, earthquake and civil commotion. The works are usually covered for both full reinstatement value, but of course always subject to the applicable limit of indemnity. The cover, in addition to the value of the executed works, usually extends to the value of unfixed goods on site and off site goods, contractor's plant tools and equipment as well

as the cost of demolition and removal of debris together with a percentage addition in respect of the additional professional fees. In some instances it may be sensible to subject the cover to indexes in order to keep pace with increased building costs.

As an alternative to the "insured risks" it is possible to obtain "all risks insurance". The property is covered for all loss and damage however caused, except for those risks specifically excluded by the terms of the policy. The most important excluded risks include:

1. Wear and tear, obsolescence, deterioration or breakdown. For example, the collapse of a tower crane due to its own defect would not be covered but damage to the works caused by the tower crane's collapse would be covered;

2. Loss or damage due to a defect in its own design, materials or workmanship;

3. War, invasion, hostilities, etc; and

4. Pressure waves caused by aircraft.

Professional indemnity insurance

The insured is indemnified against legal liability arising from its professional activities. The activities may vary tremendously, and so the activities covered by a policy are usually expressly defined. Once the nature of the insured's business has been defined, then the indemnity insurance covers liability at law subject to specific exclusions. For example, the insurance may be expressed to cover "failure to exercise reasonable skill and care required by the law" or "negligence, errors or omissions". As a general rule, professional indemnity insurance excludes cover for fitness for purpose and at the other end of the spectrum does not cover "error or omissions" which are non-negligent.

In the case of *Wimpey Construction UK Limited v Poole* [1984] 2 Lloyd's Rep 499 it was held that the word "omission, error or negligent act" should be read literally and that an "error or omission" need not be caused by negligence. The case demonstrates that a consultant can be liable for an error or omission without being negligent, but the insurer may not necessarily cover the consultant for that type of liability.

Most professional indemnity policies contain four main parts. First, the indemnity in respect of any claim made against the insured during the period of insurance which are a direct result of negligent acts. This usual cover, for an additional fee, be extended to cover liability for fraud, wrongful trading, deformation, and costs. Second, the limit of liability may include the insured's costs and expenses. Third, the policy conditions will contain a range of commonly found terms. For example, a "QC" clause which states that the insured should not be required to contest the claim unless a QC has advised that the claim is worth contesting. An exclusion of liability for public liability or property damage is usual. The insurer will frequently agree to waive its right of subrogation in relation to the insured's employees, except in the case of fraud or dishonesty. The policy is usually confidential between the insured and the insurer and disclosure of the policy by the insured may make the policy void. Finally, the policy will contain a list of exceptions. These will of course vary from policy to policy, but may include the excess, claims for fraud etc, debts, and claims for consequential loss.

Professional indemnity insurance is issued on a "claims made" basis. This means that the policy covers the insured for claims first notified to the insurer during the period of cover. There will often be a corresponding clause requiring the insured to notify the insurer as soon as the possibility of a claim exists. The "claims made" approach should be contrast with "claims occurring". This second approach is usually found in employer's liability insurance and covers the hazards prevailing during the period of insurance, and so covers claims made many years after the plaintiff's exposure.

Policies were, until recently, most frequently made on an annual basis, although now biannual policies with a separate limit of indemnity for each year are becoming more frequent.

There are three important points to note in relation to the "claims made" approach:

1. The policy covers claims made during that year even if the activity leading to the claim occurred years before;

2. There is no protection for claims notified after the policy has expired; and

3. The insured has a duty of utmost good faith when applying for cover to notify the insurer of any circumstances which might lead to a claim. The insurer is therefore entitled to refuse insurance or avoid the policy for non-disclosure. This leaves the insured in a somewhat dubious position as the insurer on receiving information at the time of the renewal date which indicates the possibility of a major claim may actually withdraw cover altogether. Hudson points out the irony of this situation by noting that the insurer will be retrospectively depriving the insured of cover despite the insured having made payment of the premiums for the years in which the liability had accrued (15.036, page 1442).

The limit of indemnity is usually expressed in one of three ways:

1. "Each and every claim" – the insured may make an endless number of claims, but each distinct claim cannot exceed the limit of indemnity. The liability of the insurer is therefore potentially inexhaustible, subject to the limit for a distinct claim.

2. "Any one claim and in all" or "in the aggregate" – the insurer will not be liable for a level greater than that of the indemnity. This limit may be absorbed by a single claim or a series of claims which cumulatively use up the limit of indemnity. At the renewal date the level will be topped up or renewed depending on the value of claims made.

3. "Aggregate cover subject to one or more reinstatements or unlimited reinstatements" – Once the insurer has met the limit of indemnity for a claim or claims, the indemnity is reinstated in full for any claims remaining or further claims. However, the insurer will not be liable for any single claim in excess of the original indemnity amount, nor for a greater level than the total number of reinstatements. Unlimited reinstatements operates in much the same way as "each and every claim" but the insurance is provided in layers.

Finally, the limit of indemnity usually includes damages, claimants costs and expenses, and the cost of defending the claim. The excess may operate in respect of each and every claim, or in the aggregate, or even a combination.

The above points relate to the construction of professional indemnity insurance. From a slightly different perspective, the case of *Pozzolanic Lytag Limited v Bryan Hobson Associates* [1999] 89 BLR 267 considered whether a project manager owed a duty of care to the client to ensure that the professional indemnity insurance of the consultants was adequate. The case concerned the construction of a concrete dome, which due to a design defect collapsed causing considerable financial loss to the employer. The main contractor was primarily liable under the JCT Design and Build Form of Contract, but did not maintain adequate insurances required by the contract. The TCC Judge held that the defendant engineer was liable to the employer for not ensuring that the contractor had adequate professional indemnity insurance, and for not ensuring that professional indemnity insurance was in place. The defendant engineer pleaded contributory negligence on the part of the employer for not himself checking the insurance. This plea was rejected by the Judge.

Project insurance

As the name suggests, a project insurance policy covers a particular contract or project. It operates in much the same way as an all risks insurance policy, but often includes public and product liability and may include cover for non-negligent liability to third parties. The policy is usually taken out by the developer and the contractor is named as joint insured. Project insurance is more frequently encountered on large projects, although it may of course be used on any project. The advantage to the developer is the degree of control over the terms and extent of the insured risks.

Product Liability Insurance

Product liability insurance provides indemnity cover against the legal liability for accidental death or injury (except to employees) or accidental loss or damage to property during the period of insurance. It is important to note that the cost of replacing the product or rectifying the defect is excluded from the cover, but the consequential losses arising from the defect are covered by the policy. Product liability insurance is encountered where a sub-contractor or supplier is providing specialist products such as lifts, raised access floors, cladding, windows and curtain walling. The sub-contractor or supplier is not carrying out design to the same degree as a specialist in the area of piling, structural steel work or mechanical and electrical services, but they are providing proprietary products.

A distinction can be made between professional indemnity cover and product liability cover. Product liability insurance does not cover the cost of replacing nor repairing the defective item, but professional indemnity cover does include the cost of replacement and/or repair. On the other hand, product liability insurance covers common law liability for the defective item and is not restricted to liability arising from a failure to exercise reasonable skill and care.

Latent defects insurance

Latent defects insurance is sometimes referred to as inherent defects insurance or decennial insurance. The cover is designed to indemnify the person having an interest in the premises for damage to it due to defects in design materials or workmanship and importantly irrespective of any legal liability in respect of the damage. Policies have only been available in the United Kingdom since the early 1980's, mainly as a result of NEDO's BUILD Report in 1988 and the experiences with similar insurance in France.
The advantage of latent defects insurance is the provision of long term cover for the specified property which avoids the extensive delay often associated with persuading professional indemnity insurers to meet claims. Further, the level of cover is far greater than that associated with a majority of professional consultants indemnity levels.
Cochram states that there are four essential elements to latent defects insurance (1998 7[146]):

1. The building is insured against damage resulting from inherent defects in the structure;

2. Cover is provided on a no fault basis;

3. A single premium provides non-cancellable long term insurance for 10-12 years; and

4. The policy is assignable between successive owners and tenant's interests are usually noted on the policy.

Terrorism insurance

The insurance industry introduced a general terrorism exclusion clause as a result of bombings in the City of London in 1992. The exclusion removes cover for fire or explosion caused by terrorism and cover for these risks may be reinstated by way of a specific terrorist provision. A special provision provides a cover limited up to £100,000 for specific categories of property related claim providing a maximum cover of £500,000 for any one property. Cover is not automatically reinstated and may be cancelled on only 7 days notice.

This cover is usually inadequate, but additional cover can be obtained from a mutual re-insurer known as Pool Reinsurance Company which is frequently referred to as "Pool Re". It was established under the Re-Insurance (Acts of Terrorism) Act 1993 and comprises several hundred insurers and Lloyd's Syndicates, and the Treasury acts as the re-insurer of last resort.

Environmental insurance

The Environmental Protection Act 1990 and subsequent legislation in the area has led to an increased liability in respect of contaminated land. Before the passing of the 1990 Act, claims for pollution were dealt with in the same manner as any other claim by insurers. However, much like terrorism cover, a standard exclusion was introduced by most insurers. It is therefore important to consider the extent, if any, of contamination or potential contamination and investigate those insurers who are willing to insure the

risk. Those insurers who provide professional indemnity cover to consultants in the area usually do so on a limited aggregate basis.

Joint code of practice on fire protection

Fire damage represents the greatest hazard on any construction site. In an attempt to reduce the level of fire damage and improve fire safety procedures a code was introduced in May 1992. The current edition was published jointly in January 2000 (5th edition) by the Construction Confederation and the Fire Protection Association. A contract provision requiring compliance with the code is becoming more common, and in some instances compliance with the code is a condition precedent to insurance cover. The code distinguishes "large projects" which are expressed as being those with a contract value in excess of £20 million. It establishes a more extensive regime in respect of those projects. A more limited regime is set out in the code in respect of projects below £20 million which are normally expected for projects in excess of £2.5 million, although the more restricted regime could sensibly be applied to any low value project. The code applies to all projects with a contract value of £2.5million and above.

Insurance under the standard forms

JCT Standard Form of Building Contract 19080, 1998 and 2005

The JCT 1980 Building Contract (now replaced by the 1998 Edition) has been demonstrated to be the most frequently used Standard Form Building Contract in the building industry. The main provisions within the JCT Form relating to insurance are:

- Clause 20 – Injury to persons and property, and indemnity to employer
- Clause 21 – Insurance against injury to persons or property
- Clause 22 – Insurance of the works
- Clause 22A – Erection of new buildings – all risks insurance of the works by contractor
- Clause 22B – All risks insurance of the works by an employer
- Clause 22C – Insurance of existing structures – insurance of works in or extensions to existing structures
- Clause 22D – Insurance for employer's loss of liquidated damages
- Clause 22FC – Joint fire code – compliance

The JCT 2005 edition incorporates re-drafted insurance provisions. Section 6 deals with injury, damage and insurance, while Schedule 3 sets out the insurance options. Professional Indemnity cover may no be required. The 3 options remain, but are covered in the Schedule rather then the body of the contract.

Sole risk

Of particular interest are a series of cases relating to the construction and interaction of the indemnity clause 20 and the works insurance Clause 22. The case of *Scottish Special Housing Association v Wimpey Construction UK Limited* [1986] 2 AER 957 concerned the JCT 1963 Form. Clause 20C (now amended clause 22C) required the existing structure to be at the employer's "sole risk" in respect of specified perils including fire. Fire was caused by the contractor's negligence damaging the client's property. The House of Lords ruled that the contractor could not be liable, as imposing a duty of care would run against the express agreement of the parties.

This principle appears to have been extended by the Court of Appeal in *Norwich City Council v Harvey* [1989] 2 AER 1180. In that case a fire was caused by a domestic sub-contractor. The Court would not allow the sub-contractor to take the benefit of the term in the contract to which it was not a party. Nonetheless, in considering whether to impose a duty of care in tort the Court of Appeal considered the whole network of contractual rights and obligations. Clause 20C established that the employer was to bear the entire risk of the fire, and so the Court of Appeal held that the sub-contractor was not legally responsible for the consequences of its negligence.

The case has been subject to much criticism, although it has not been overruled. However, subsequent cases have avoided the rule. In the case of *National Trust for Places of Historic Interest or Natural Beauty v Haden Young Limited* (1997) 72 BLR 1 the Court of Appeal considered the construction of the JCT minor works in order to determine a nominated sub-contractor's liability for setting fire to the existing structure. The minor works contract did not state that the existing structure would be at the employer's "sole risk", but instead imposed liability for damage on the contractor. The Court of Appeal held that the nominated sub-contractor was fully liable for the damage.

The move towards "joint insured"

In addition, the JCT 80 clauses are significantly different from the older JCT 63 Clauses. For example, the phrase "sole risk" has been omitted from the more recent clauses. Nonetheless the case of *Ossory Road (Skelmersdale) Limited v Balfour Beatty Building Limited* [1993] CILL 882 demonstrates that the contractor will still escape liability for negligently setting fire to the existing structure. The position is not the same with regards to sub-contractors.

The exception: domestic sub-contractors working under Clause 22

The recent House of Lord's case *British Telecommunications plc v James Thomson & Sons (Engineers) Limited* [1999] 2 AER 241 concerned a claim in negligence against a domestic sub-contractor who was lagging ventilation pipes which caught fire allegedly due to the sub-contractor's negligence. The House of Lords held that domestic sub-contractors (unlike nominated sub-contractors) did not have the benefit of being an insured party nor the benefit of a waiver of the insurer's right of subrogation. The case turns on the construction of Clause 22.3 which requires the contractor and employer to insure in the joint names of each other, and recognise nominated sub-contractors. It goes on to state that the provisions in regard to recognition of waiver should also apply to domestic sub-contractors "[e]xcept in respect of the Policy referred to in Clause 22C."

The defence specifically pleaded the *Norwich* defence, which was rejected by the House of Lords. An analysis of the case suggests that this turned upon the construction of the clauses, although some commentators suggest that the case goes further and that the House of Lords have rejected the *Norwich* approach. In other words, the person who negligently causes a fire should be held liable for the ensuing damage, and that contractual obligation for a party to insure will not be adequate to take away the a right in tort.

Contribution and contractual insurance provisions

The Civil Liability (Contribution) Act 1978 states, at section 1(1):

> "…any person liable in respect of any damage suffered by another person may recover contribution from any other person liable in respect of the same damage (whether jointly with him or otherwise)…"

In addition, section 6(1) states:

> "A person is liable in respect of any damage for the purposes of this Act if the person who suffered it… is entitled to recover compensation from him in respect of that damage (whatever the legal basis of his liability whether tort, breach of contract, breach of trust or otherwise)."

It was thought that the Act would cure the defects in the previous legislation where no contribution could be claimed by two wrongdoers who were not joint tortfeasors or two equitable wrongdoers. The purpose of the Act was only to deal with damage, and was not to affect the existing rules in respect of contribution between debtors.

The case of *Co-operative Retail Services v Taylor Young Partnership* [2000] BLR 461 considered whether an architect and structural engineer who were being sued by the employer could seek a contribution from the contractor and a sub-contractor for work carried out under a JCT 1980 Contract when the contractor was co-insured with the employer. The Court of Appeal held that the architect and engineer could not seek a contribution from the contractors because the contractors were jointly insured with the employer and the insurer bringing the claim could not exercise rights of subrogation against the joint insured. In the absence of the contractors' liability to the employer, the contractors were not liable to make any contribution under the Civil Liability (Contribution) Act 1978. An appeal to the House of Lords confirmed the approach of the Court of Appeal [2002] 1 WLR 1419.

The House of Lords has also recently considered the meaning of "same damage". In the case of *Royal Brompton Hospital National Health Service Trust v Frederick Hammond & Ors & Taylor Woodrow Construction (Holdings) Limited,* (2002) 1 WLR 1397 HL the hospital had entered into a building contract with Taylor Woodrow. The contract overran and the architect granted extensions of time. Taylor Woodrow claimed loss and expense, and the hospital counterclaimed for liquidated and ascertained damages. The hospital also sued the architect for negligence in issuing the certificates, alleging that the architect should not have issued extensions of time. The architect then commenced a third party action against Taylor Woodrow (as a Part 20 Defendant).

The House of Lords held that the architect was not entitled to a contribution from Taylor Woodrow. This was on the basis that the architect and Taylor Woodrow were not liable in

respect of the same damage. Taylor Woodrow was essentially liable for delay, while the architect was liable for negligent certification, which in itself did not lead to the delay. Lord Bingham said:

> "It would seem to me clear that any liability the employer might prove against the contractor and the architect would be independent and not common. The employer's claim against the contractor would be based on the contractor's delay in performing the contract and the disruption caused by the delay, and the employer's damage would be the increased cost incurred, the sums it overpaid and the liquidated damages to which it was entitled. Its claim against the architect, based on negligent advice and certification, would not lead to the same damage because it could not be suggested that the architect's negligence had led to any delay in performing the contract".

Finally, the Court of Appeal recently considered the case of *GD Construction (St Albans) Limited –v- Scottish & Newcastle Plc* (22nd January 2003). This was an appeal of a decision of HHJ Seymour QC in the TCC in respect of a preliminary issue of law. Permission to appeal was refused, but granted by Dyson LJ.

The Employer and Contractor entered into a JCT IFC 1984 Standard Form of Building Contract for refurbishment work to a public house in Reading. The contract was dated 30th September 1996. The contract provided that the Employer (the Claimant in this case) was to take out an insurance policy in the joint names of both the Employer and the Contractor (clause 6.3C.1). The policy was to insure against any damage to the existing structure caused by the Specific Perils, "including fire". The Employer failed to take out the policy. During the refurbishment a fire damaged the existing building of the public house. For the purposes of the preliminary issue it was assumed that the fire was caused by the negligence of sub-contractors working on the roof of the public house. The Employer sued the contractor for damages, relying on a liability and indemnity clause in the contract. Clause 6.1.2 of the IFC 84 states:

> "The Contractor shall be liable for, and shall indemnify the Employer against, any expense, liability, loss, claim or proceedings in respect of any loss, injury or damage whatsoever to any property real or personal insofar as such loss, injury or damage arises out of or in the course of or by reason of the carrying out of the Works and to the extent that the same is due to any negligence, breach of statutory duty, omission order fault of the Contractor, who servants or agents or of any person employed upon or engaged upon or in connection with the Work. … This liability and indemnity is subject to clause 6.1.3 and were clause 6.1.3.1 is applicable, excludes loss or damage to any property required to be insured there under caused by a Specific Peril.

The contractor also relied on the same liability and indemnity clause in order to exempt it from liability from the Employer's claim. The key issue was whether liability for damage to the identified property which results from the negligently caused fire is excluded, because the parties have agreed that a clause defining the Contractor's liability and obligation to indemnify the Employer excludes loss or damage to the identified property which is required to be insured by the Employer against specific perils including "fire".
Mr Justice Aikens reviewed the contractual provisions and compared the general scope of clause 6.1.2 to clause 6.3.C.1. He considered it necessary to identify 3 things in order to

work out the extent of the exclusion of the contractor's liability under clause 6.3C.1. First, what was the type of property to be insured under that clause? Second, is the nature of the specific peril to be covered by insurance? Was the loss or damage complained of caused by one of the specific perils.

These Specific Perils included "fire", and at paragraph 26 he considered:

> "For nearly 200 years when the word "fire" has been used in an insurance policy to describe one of the perils covered by the policy, the meaning of the word "fire" has been clear. Unless qualified by other words or a warranty in the policy, the peril "fire" covers loss approximately caused by a fire, whether the fire was started by accident, was caused by the negligence of the assured, or by any third party or was caused by the deliberate act of a third party… If, "fire" is an insured peril in the policy then a loss that is approximately caused by "fire" is covered by the policy. It is irrelevant that the fire was itself caused by negligence or even the deliberate act of the third party. But, in the absence of express words in the policy, the parties would not have intended to cover losses by fire when fire was caused by the deliberate act of the insured itself".

He then considered some competing case law. The case of *Archdale (James) & Co Limited v Comservices Limited* [1954] 1 BLR 459 and *Scottish Special Housing Association v Wimpey Construction UK Limited* [1986] 1 W LR 995 could be distinguished on the basis that the provisions in those contracts stated that the existing structures etc would be at the "sole risk" of the Employer. Provisions in the JCT Contract moved away from the "sole risk" basis towards a joint names insurance policy.

Mr Justice Aikens referred to the recent House of Lords case of *Co –Operative Retail Services Limited v Taylor Young Limited* [2002] 1 WLR 1419. In that case Lord Hope concluded that the insurance and indemnity provisions of the main contract should be read together, and the result was that the contractor was not liable to the employer for loss or damage to the works by fire which had taken place before completion. Instead that liability was provided for by way of an insurance policy, which very importantly was to be in the joint names of the employer and the contractor.

The key point was that where two parties enter into a contract stipulating that one was to obtain insurance in joint names then one joint name insured could not sue the other where the loss was covered by the insurance. A term would be implied into the contract preventing such an action. He concluded at paragraph 52:

> "…that it is in the totality of the contract structure in the present case that leads me to the conclusion that the Contractor is under no liability to the Employer in respect of the cost of the repairs to the existing structure".

In conclusion, the first instance judge was wrong, and the appeal was allowed.

Longmore LJ agreed, and noted that *Dorset County Council v Southern Felt Roofing Co Limited* (1989) 48 BLR 96 and *London Borough of Barking & Dagenham v Stamford Asphalt Co Limited* (1997) 82 BLR 25 could be distinguished on the basis that there was "no express link between the exclusion of the contractor's liability for liability for fire and the employer's obligation to insure". Therefore, in those cases it could not be said that the obligation of the employer to insure against fire did not extend to an obligation to insure against

fire negligently caused by the contractor. However, this cannot apply where an insurance policy is to be in joint names. Ward LJ agreed.

ICE Conditions of Contract 7th Edition

The ICE insurance clauses have always been shorter, and it is submitted much clearer, than the JCT clauses. The main provisions in the ICE 6th Edition includes:

- Clause 20 – Care of the works, excepted risks and rectification of loss or damage
- Clause 21 – Insurance of works and extent of cover
- Clause 22 – Damage to persons and property, exceptions, indemnity by employer and shared responsibility
- Clause 23 – Third party insurance, cross-liability and amount of insurance
- Clause 24 – Accident or injury to workpeople
- Clause 25 – Evidence and terms of insurance, excesses, remedy on contractor's failure to insure and compliance with policy conditions

The Engineering and Construction Contract 2nd Edition

The ECC has been drafted for use on both building and engineering projects. Clauses are short, and insurance is dealt with swiftly. The main provisions are:

- Clause 80 – Employer's risks
- Clause 81 – The contractor's risks
- Clause 82 – Repairs
- Clause 83 – Indemnity
- Clause 84 – Insurance cover
- Clause 85 – Insurance policies
- Clause 86 – The contractor does not insure
- Clause 87 – Insurance by the employer

Clause 80 lists those risks which are the liability of the employer, and clause 81 merely states that the contractor's risk are, from the start date until the defect certificate, those risks which are not carried by the employer. The indemnity clause 83 is short and to the point requiring each party to indemnify the other against events which are at its risk. Insurance cover under clause 84 is demonstrated by the use of an insurance table which deals with the categories of insurance. As is usual, the insurances are required to be in the joint names of the employer and contractor.

The impact of adjudication

The swiftness of adjudication and speed with which an Adjudicator's decision can be enforced has curtailed the ability of defendants to delay payment. As a result many insurers are called upon not only to fund the defence, but also to fund the payment of adjudication claims. In some respects this new pressure on the insurance industry has been increased by fears of enforcement of erroneous decisions as a result of *Bouygues (UK) Limited v Dahl Jenson (UK) Limited* [2000] 13 July 2000 Court of Appeal. In that case the Adjudicator made a mistake in calculating the retention due in the decision. As a result Bouygues had to pay Dahl Jenson £207,000.00, rather than receive £141,000.00

from Dahl Jenson. At first instance Sir John Dyson upheld the decision, and the Court of Appeal reinforced that approach.

As a result insurers have introduced special provisions in relation to adjudication. This includes strict notification provisions, limited cover, requirements as to the adjudicator, and a requirement that the decision is not finally binding. The notification procedures are extremely strict, often requiring that the insured notify the insurer within 2 days regardless of bank holidays and weekends. In addition, notification is required to be given once the insured has received as much as an informal threat. The Act requires adjudicators to be impartial but not independent. Many insurance provisions insert that additional requirement. Settlement of a claim will usually require the insurer's consent, and there must be no restriction on the insurer's ability to make the disputes to arbitration or court proceedings.

Future developments

Risks associated with construction and the potential losses demand that insurance is an important, if not fundamental aspect of construction work. The enormity of claims in early 1990 has lead to the development of codes and distinct types of insurance cover have increased the complexity of insurance, the contractual provisions and the nature of the claims made.

An increasing focus on the insurance of post construction defects, the insurance recommendations of the Latham Report (1994) and subsequent working parties has the potential to develop the approach to insurance in the construction industry. These moves together with increased competitiveness, and the urge to reduce litigation (allowing insurers to spend money on damages rather than lawyers) demonstrates moves toward greater efficiency. Finally, the increasing international dimension to the provision of insurance and the greater activity of European insurers in the domestic market has the potential to provide the wider range of standard cover policies at increasingly competitive premiums.

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REFERENCES

Statutes

Environmental Protection Act 1990

Employer's Liability (Compulsory Insurance) Act 1969

Insurance Mediation Directive 2002/92/EC

Life Assurance Act 1774

Marine Insurance Act 1905

Re-insurance (Acts of Terrorism) Act 1993

Third Parties (Rights Against Insurers) Act 1930

Codes

Joint Code of Practice on the Protection from Fire of Construction Sites and Buildings Undergoing Renovation (5th Edition) January 2000

Association of British Insurers Scheme for Noting of Interests