THE JOY OF INSURANCE

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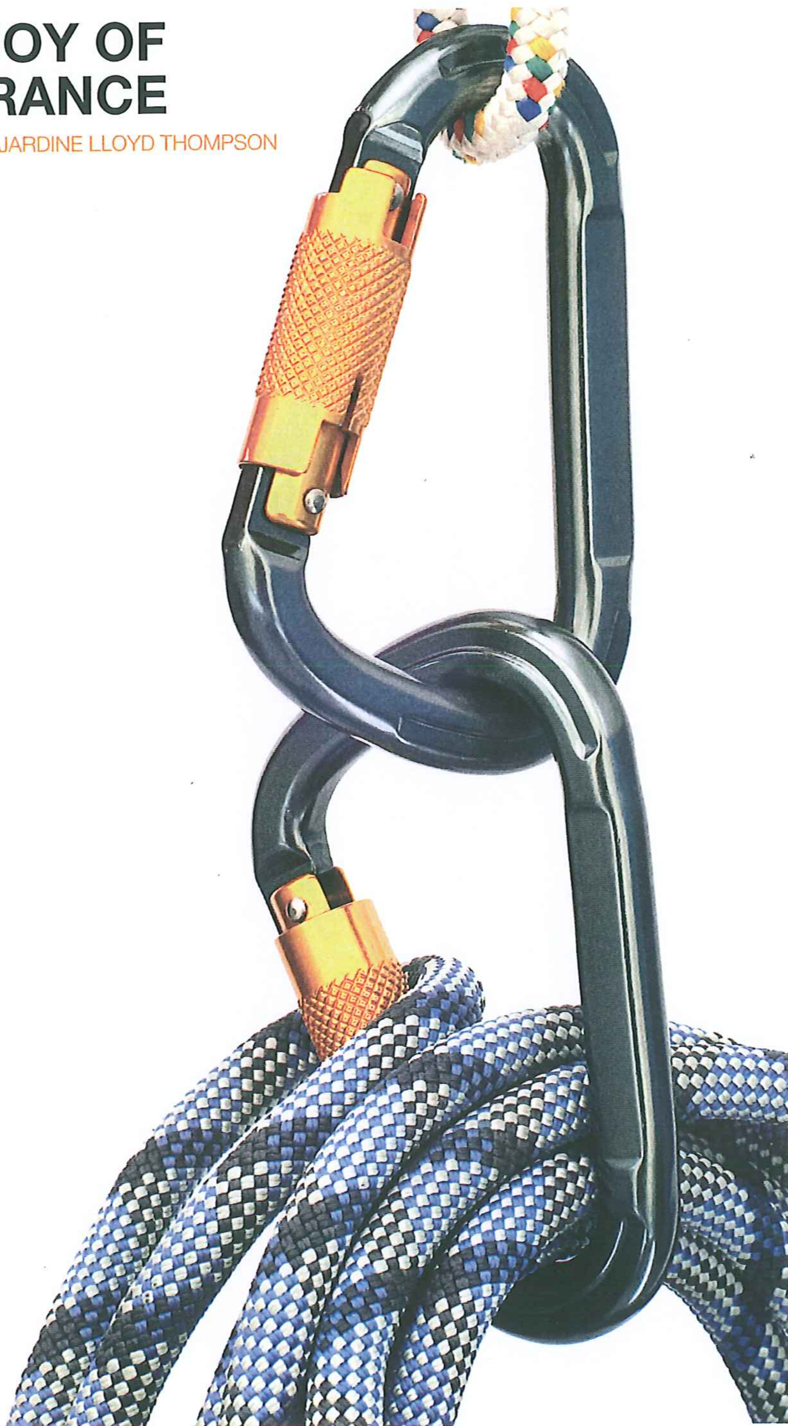

Insurance can be very satisfying if got right – especially in the aftermath of a major claim. Whilst simple in concept, it can be extremely complex to accomplish satisfactorily. It needs careful thought and preparation at the same time as the other details of the building project are getting attention.

Take, for instance, the cover required where the contract concerns work being done to an existing building. That might be an extension, structural alteration or tenant fit-out. Reduced to a simple précis, the insurance requirements of schedule 3, option C in the JCT Standard Building Contract 2005 – echoed in most other JCT forms – call for the employer to arrange cover for damage by certain specified perils to the existing building, and those contents which are his responsibility, together with all risks cover on the contract works. All that insurance has to be arranged in the joint names of the contractor and the employer. In that way, the insurers have no right of recovery from the contactor if any damage is caused by his negligence.

As I said earlier – simple!

Well it might be if the employer is the owner of the property and arranges the insurance on it – and, of course, if the insurers are willing to co-operate. They may not be able or willing to oblige as the risk obviously changes, for example from an office to a construction site – something that many property insurers do not cover. However, for many contracts the employer is a tenant. The building will be insured by the landlord, or even his landlord, the freeholder, and the employer will have little or no control over such insurance. It is certainly unlikely that the tenant will be a joint insured under that insurance. Under the terms of the lease, it is possible that the tenant will enjoy a waiver of subrogation rights – whereby the insurers could otherwise seek to recover from a third party any costs they have to meet for negligent damage. However, that waiver

would not extend to include the contractor.

It is increasingly unlikely that the insuring party will be willing to extend the cover to meet the terms of the contract. The general professional advice given to property owners is that to do so might prejudice their claims experience – potentially causing a serious impact on the future cost of premiums. As these are usually spread across a portfolio of properties, any increase would disadvantage all tenants. That is not a good thing at a time when all occupation costs are under the microscope.

To add to the problem, not having control of the existing building insurance, it will also be more difficult, if not impossible, for the tenant to be able to arrange the all risks cover on the works. So, all may not be as simple as it seemed at first sight.

Clearly, if cover cannot be arranged in compliance with the contract, something needs to be done. But, action will only be taken if the problem is identified at an early stage: there lies the nub of the problem.

After a long career in real estate and development, I know how low down the priority list insurance comes. In fact, I have seen many examples where the deficiency is only recognised when a claim comes along. Even if that is not the case, the employer will be in breach of contract and facing significant costs to rectify the problem.

That the situation has got that far may not be the responsibility of the employer. In reality, he is not likely to be an experienced client of the construction world and will be depending on the advice of his professional construction advisers, including the contractor. The fact is that they may not be any more knowledgeable on the details of construction insurance than the employer – who should be seeking professional insurance assistance. Sadly, that is not always done, especially if the problem is not identified until the contract is agreed and works underway.

A simple – that word again – solution would be for the contractor to extend the public liability insurance he is required to arrange in respect of personal injury and death together with damage to third party property that arises from his negligence in carrying out the work. That cover follows the indemnity given to the employer in clauses 6.1 and 6.2 but there is another complication as clause 6.2 specifically excludes damage to the existing structure; such damage is meant to be insured by the employer in joint names and so the contractor has no liability, at least not to the employer. However, if damage does occur, the owners of the building or their insurers will have recovery rights against the contractor. The court, if the issue goes that far, will be looking at the issue of negligence rather than who is responsible under the contract. If the employer has not arranged the required insurance, the contractor will have to attempt to recover any damages from him. If the employer no longer exists – sadly a possibility in this economic climate – the contractor will be on his own, potentially without the benefit of insurance.

It is perhaps worth pausing there, before looking at other remedies, to examine the contractor's position. Serious damage to the building, if multi-occupied, is likely to affect other tenants and their businesses. Any liability for that, together with damage to the building by a cause not included in the specified perils to be insured[1] – any of which could be substantial – is not excluded from the contactor's indemnity and should therefore be covered by the public liability insurance that the contractor has to arrange in accordance with clause 6.4. I have certainly been involved in cases where such damage – for the accidental escape of water or a fire, for instance – has cost many tens of millions of pounds.

That exposure, added to the risk of damage to the building itself, is likely to be far more than the amount of public liability cover usually required, especially from small contractors.

An example is the damage to the State Apartments of Windsor Castle in 1992, when a spotlight being used by decorators ignited a curtain. The resultant damage cost over £37million to repair and there is no record of the consequential losses that accrued. It is unlikely that a small contractor would carry anything like that in terms of liability insurance. In fact, many contracts do not call for a realistic limit of cover – especially when the job is small but within a large building with many tenants; the fit-out of a unit in a shopping centre, for instance.

Any consideration of this issue must reflect that the standard indemnity and insurance clauses in whatever version of the JCT contract is being used may need amendment. The ways of doing that are varied and depend on the specific circumstances of each contract.

It is possible that the party insuring the building may be willing to obtain a waiver of the insurer's subrogation rights against the contractor – possibly on payment of an additional premium. That is often done in exchange for an obligation by the contractor to maintain a specified limit of public liability insurance. In that case, the indemnity provisions of clause 6.2 will also have to be amended to reflect that there is now liability for damage to the property being worked upon.

Whatever is finally decided, the issue will have to have received some attention. The construction industry is full of innovation and creative thinking. It is a shame that the insurance elements of a contract do not often benefit from that intellectual capital. Giving it the attention it needs and deserves might just bring you the Joy that insurance still gives me after more than 45 years in the game.

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[1] Fire, lightning, explosion, flood, escape of water from any water tank apparatus or pipes, earthquake, aircraft or other aerial devices or articles dropped there from, riot and civil commotion.