Contractual Risk and Professional Indemnity Insurance – TSA

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THE SURVEY ASSOCIATION
SUPPLIER

Speakers

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Agenda

1. Boundaries to Professional Indemnity Insurance (PII)
2. PII Perspectives on Contract
3. Worked Examples & Rectification
4. Q&A

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Boundaries

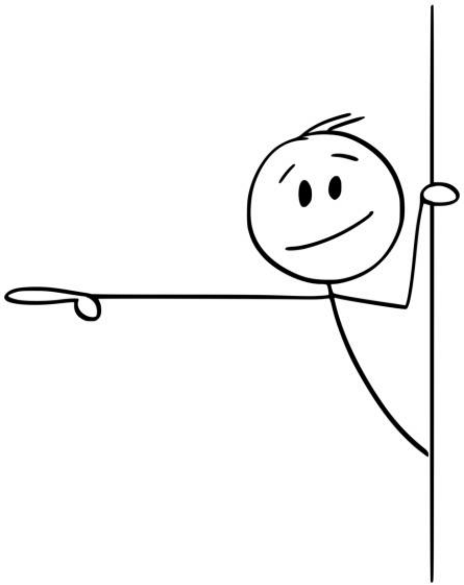
The raison d'être of PII is to cover negligence, subject otherwise to the policy terms and exclusions.

Breach of contract can also be covered but insurers do not provide a blank cheque for any form of liability created or accepted in contract.

(Insurers doing so would be on a short road to insolvency…)

As a result, there is insured contractual risk and uninsured contractual risk.

Claims Made basis of Insurance



It is the policy in place at the time a claim and/or circumstance is notified that will respond.

In order for cover to be maintained, PII must be maintained.

If a firm has ceased, it is no longer there to keep purchasing PII.

Contractual Liability Exclusion

Common examples from Construction Sector PII:

"Any liability assumed by any Insured under any express contract, agreement, indemnity, penalty clause, liquidated damages clause, guarantee or warranty except to the extent that such liability would have attached to such Insured in the absence of such express contract, agreement, indemnity, penalty clause, liquidated damages clause, guarantee or warranty." – Endurance v1.2 A&E 12-08-16

or

"Any liability assumed by the insured under any contractual agreement (including any collateral warranty or duty of care agreement) in respect of:

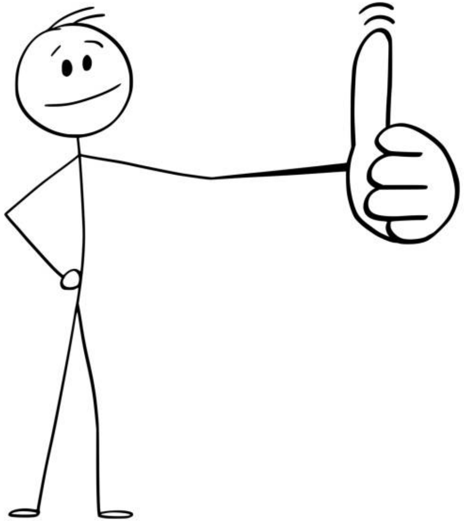
(a) any warranty or agreement under which the insured assumes a standard of care greater than the standard of reasonable skill, care and diligence normally expected in the insured's profession;

(b) any acceptance or guarantee of fitness for purpose;

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

(d) any express guarantee contractual penalty or liquidated damages in so far as liability assumed by the insured exceeds the amount of the insured's liability in the absence of such agreement;" – Omnyy OMYPISPP.11-24 (non-RICS surveyors' wording)

Silver Linings...



Firms are free to enter into contracts without interference or prohibition from insurers.

Entering into a contract containing onerous elements does not "switch off" PII cover.

The insurance market views this as the commercial prerogative of the firm. The principals should be free to make commercial decisions appropriate to the circumstances and their firm.

This is what is intended by "making a commercial decision" (when considering coverage rather than something which does not relate to PII at all...)

Good Corporate Governance

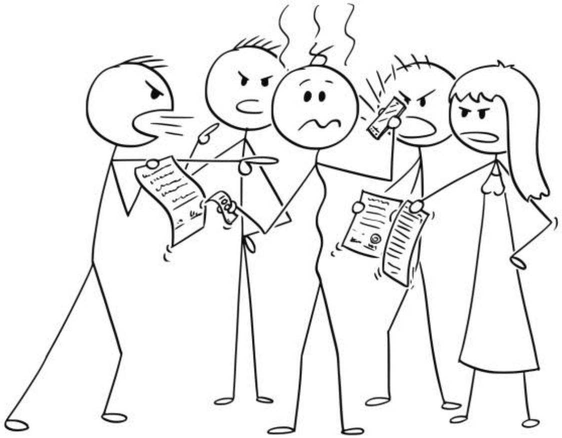
Directors owe a duty to the company to manage and mitigate risk.

A well run business does not regularly expose itself to unlimited and uninsured commercial risk?

This duty and exposure can be explained to clients (Employers, Funders etc)…

…Our corporate governance demands attention to this area!

Standard Off the Shelf Contracts



Don't assume that a standard contract form is PII supported!

For example, the JCT Standard SCWAE 2011 has a performance guarantee in it:

"2.2…The Sub-Contractor further warrants to the Employer that:….he will satisfy any performance specification or requirement contained in or referred to in the Sub-Contract"

Standard contract forms can be onerous or professional friendly or compromise agreements.

Professional body issued forms (RIBA, ACE, RICS …) and Construction Industry Council forms are more professionally friendly.

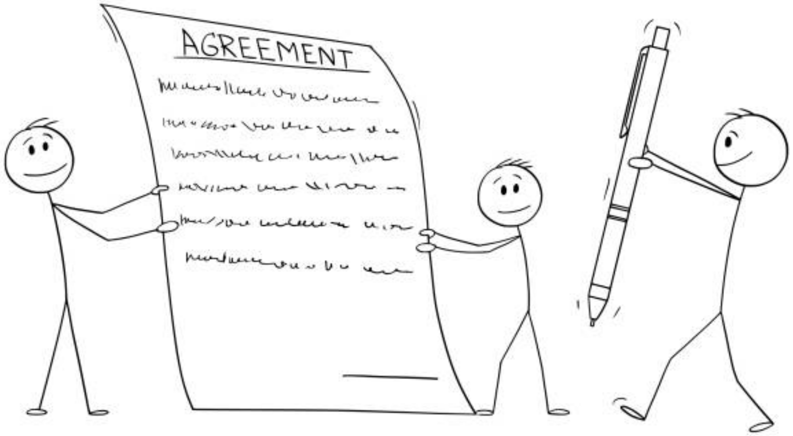
No Contract means no Liability?

Unfortunately not…

Burgess v Lejonvarn (2017)

But…

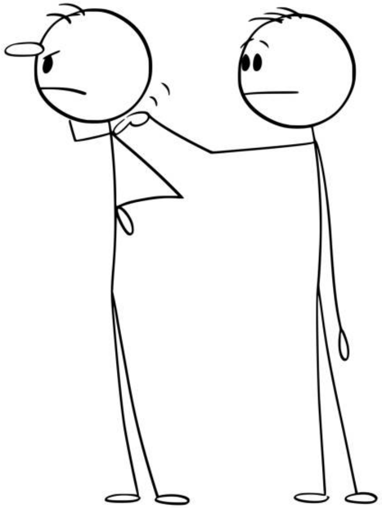
A missed opportunity to include contractual protections?



Cap on Liability

Maintenance of Insurance Clause…

The Consultant has and shall continue to maintain professional indemnity insurance for the duration of the Services and for a period of at least 12 years…



Cap on Liability…

…in any such action or proceedings the Consultant's liability for loss or damage shall not exceed the amount of the Consultant's professional indemnity insurance specified in clause (X)…

Onerous clauses/language

'Absolute' Obligations

These can appear innocuous in the context of the project & services but the language used is very important.

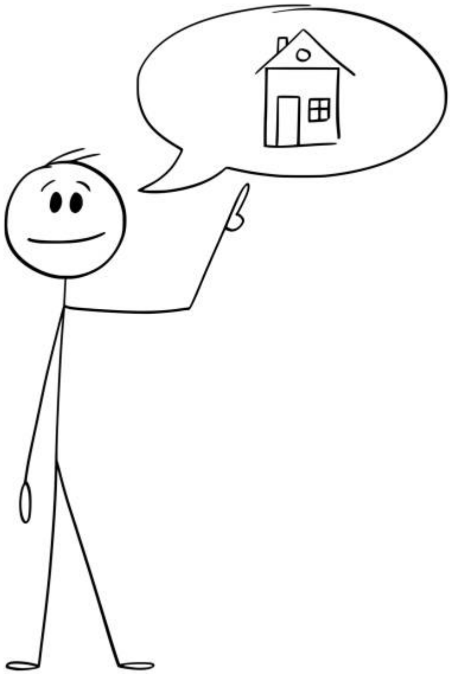
For example:

The Consultant will adhere to the Programme.

Reasonable Skill & Care language

The Consultant will use reasonable skill and care to adhere to the Programme.

Absolute Obligations – an example



A real-world example from case law involving a valuer…

Platform Funding Ltd v Bank of Scotland plc

Onerous clauses/language

MT Hojgaard V Eon (2017)

This case confirmed the Reasonable Skill and Care clause/obligation does not mitigate conflicting provisions unless it is expressly stated to do so.

For example, strict language in a schedule of services can create more onerous obligations, such as a performance guarantee, which is not caveated or diluted by the general requirement to use reasonable skill and care.

Add an overriding reasonable skill and care clause.

The contract is not interpreted in terms of reasonable skill and care unless this is expressly stated.

Overriding Reasonable Skill And Care Language

Notwithstanding anything that may appear elsewhere to the contrary, whether under this Agreement or otherwise, the Consultant's Services, duties and obligations shall be deemed to be subject to the exercise of such reasonable skill and care and nothing contained in this Agreement or elsewhere shall be construed as imposing on the Consultant any greater duty than the exercise of such reasonable skill and care

Reasonable Skill & Care language

Amend “duty or liability” to “duty of care”

Onerous clauses/language

Waiving your and/or your insurers’ defences

No approvals/consents clauses

No approval or inspection of the Development or of any designs or specifications nor any testing of any work or materials by or on behalf of the Beneficiary and no omission to inspect or test shall negate or diminish any duty or liability of the Consultant arising under this Deed.

Onerous clauses/language

Indemnity Clauses

To the extent that the indemnity clause changes the ordinary legal process or position, it is prejudicial to the insurers.

To the extent that it extends liability, the additional liability is uninsured.

Ideally Delete.

...Or Mitigate

....the Consultant shall indemnify any reasonable, reasonably forseeable and fully mitigated loss arising directly from a negligent act or omission of the Consultant....

Positive Statements of Limitation

Delete positive statements of liability

In the absence of such a statement limitation is set by the ordinary operation of English/Scottish law

Identifiable as a statement that the limitation period “shall” be the specified period

It is a potential coverage issue as it could override a shorter limitation period which would have meant that a claim was statute barred (and then the claim will be excluded under PII by Onerous-Liability-Accepted-In-Contract Exclusion)

Limitation in Time clauses

For example:

No action or proceedings whether in contract or in tort or in delict or in negligence or for breach of statutory duty or otherwise shall be commenced against the Consultant after the expiry of 12 years from the date of practical completion of the relevant part of the Development under the Building Contract or, in the event that practical completion is not achieved, the date that the Consultant finishes its services for the Client under the Appointment. *CIC/ConsWa/P&T Second Edition 2018*

Try to include a limitation in time clause…but its not essential from the PII perspective

Delete positive statements of liability

Try to include but not essential from PII perspective (because ordinary legal position otherwise applies)

Spot the Difference

Positive Statements:

The claimant <u>shall</u> be allowed to make a claim in the specified period

Limitation in Time:

The claimant <u>shall not</u> be allowed to make a claim <u>after</u> the specified period

Collateral Warranties – why?

Purpose – to create a contractual link between parties such that the beneficiary can bring a claim for breach of contract in the event of a loss (rather than having to hope that a duty of care in tort exists)

Doubt had been thrown on the efficacy of tort due to legal cases such as *Murphy v Brentwood District Council (1991)*

The original collateral warranties were simply restating a duty of care in contract (only!) i.e.

"*The Consultant shall use reasonable skill and care in the performance of its services under the Appointment*"

CIC Warranties - a practical solution?

The Construction Industry Council (CIC) issues a number of standard templates including collateral warranties

A number of insurers explicitly state in their policy wording that their onerous-liability-accepted-in-contract provision does not apply if a CIC template is used

It is not the case that every Construction PII insurer states this but nevertheless the CIC is the closest to a PII insurance industry acceptable standard as currently exists

Even in the absence of explicit endorsement the CIC have been sensitive to insurance coverage 'norms' in drafting and the warranty form is notably more 'professional friendly' than many others

A line of least resistance – propose the use of a CIC warranty and no further negotiation is needed! (template downloadable from CIC website for circa £30)

Make sure that a no greater liability provision is included in every collateral warranty

Make sure that the no greater liability provision applies to the whole warranty and not just to individual provisions within the warranty (for example “provided that” language may limit to the clause in which the link is included)

‘No greater liability’ provision

Standard exclusion in PII policies of any liability which is greater or of longer duration than the liability owed to the professional’s actual client under their appointment. Address this with a “no greater liability” provision (sometimes referred to as ”equivalency” provision)

For Example:

The Consultant shall be entitled in any action or proceedings by the Purchaser/Tenant to rely on any limitation or exclusion in the Appointment and to raise the equivalent rights in defence of liability as it would have against the Client under the Appointment.

Futureproof the position by restricting assignments even if there is no present exclusion based on assignments?

Assignments

Exclusions of claims arising from collateral warranties (or other reliance rights) which have been assigned more than a specific number of times remain common in PII policies

RICS Approved Minimum Wording only permits 1 assignment (quantity surveyors, contract administrators, land surveyors etc)

(ignoring additional provision for funders which vary from policy to policy)

Any questions?

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Independence changes everything.