PROJECT INSURANCE FOR SUB-CONTRACTORS

Ruling leaves questions to be answered

Law, insurance and subrogation: a combination of topics not exactly designed to combat sleepless nights. But it's worth paying attention to a landmark legal case which could affect the whole way large construction projects are financed and insured. A High Court judgment last year seems likely to set a precedent for the whole way insurance policies and claims involving Project Contractors and Sub-contractors are organised and managed (Haberdashers' Aske's Federation Trust Ltd and Others vs Lakehouse Contracts Ltd and Others [2018] and first reported in **integrated** Issue 4). Mr Justice Fraser ruled that insurers can pursue a subrogation claim against a Sub-contractor even if the Sub-contractor is (or believes it is) already protected under the single insurance policy commonly used in large construction project financing.

According to Phil Durrant, Managing Director EMEA at Integra Technical Services "that judgment was due to go to the Court of Appeal in January this year, and was expected to be either clarified or overturned. But the case settled out of court before the hearing. So, for the time being at least, the ruling stands."

Single policy

When arranging insurance for a large project it is usually simpler, more cost-effective and more transparent (in terms of both coverage and cost) for the Owner, Developer or lead Contractor to take out a single policy covering the whole project, with Sub-contractors named as joint Insured parties.

Typically this single policy is then supported by a standard Joint Contracts Tribunal (JCT) construction industry contract between the Contractor and the Sub-contractor; along with a requirement for the Sub-contractor to arrange Public Liability insurance on its own account (usually up to £5m) to cover death, injury and property damage.

Phil explains "under this approach, if a loss transpires the insurer pays out without being able to subrogate any claim back to the Sub-contractor (because it is Co-insured under the single policy)."

In the Haberdashers' Aske's case, in line with the practice outlined above, the main Contractor entered into a Project Insurance Policy which included cover for Sub-

contractors. Subsequently the contractor engaged a Sub-contractor to perform some roofing works. Unfortunately while the works were under way a fire broke out, causing extensive damage to buildings. The Insurers indemnified the main Contractor, but then also filed a subrogation claim to recover some of the indemnity payment from the Sub-contractor.

No subrogation?

Again in line with usual practice, the Sub-contractor argued that the subrogation claim was not valid because it was a Co-insured party under the single project policy.

However the legal contract between the Contractor and Sub-contractor had featured an express requirement that the Sub-contractor would obtain its own Third Party Liability insurance: which it had indeed done. Consequently, the project Insurers argued, the Sub-contractor was not entitled to be considered a co-insured party and was not protected from a subrogated claim.

Mr Justice Fraser accepted that argument, ruling that reference must be made to the conditions of the contract between the Insured Contractor and the Sub-contractor who is seeking cover under the policy. Other legal arguments – relating to agency and the policy being a 'standing offer' from the insurers – were also considered and rejected under the ruling.

Phil suggests that "even before the Haberdashers' case, the principal that the Insurer could not exercise rights of subrogation in the name of one Co-insured against a second Co-insured had its limitations, normally defined within a Multiple Insureds Clause (or similar) and concerning Vitiating Acts." Basically, if a Co-insured commits a Vitiating Act then the Insurers can treat the party as uninsured and pursue a subrogation action.

Conclusion

This ruling appears to open a further loophole. Insurers receive premium for providing cover for Sub-contractors but when (as is the case in many instances) Contractors include in their standard terms a clause requiring the Sub-contractor to obtain its own insurance, it now appears to leave the Sub-contractor open to a possible subrogation claim.

Of course, it's possible there will be a new legal challenge to such a far-reaching ruling. But those kinds of challenge take a long time to emerge, and there is no guarantee of the outcome. For the time being, the precedent applies. And it might, or perhaps should, be causing sleepless nights for all parties.

FOUR QUESTIONS TO CONSIDER

Aside from the potentially significant precedent, the ruling raises some important questions.

1. Are more Insurers starting to use the judgment to subrogate against Sub-contractors?
2. Are we likely to see an increase in claims now that the precedent has been established? Might it open the floodgate to a new high level of litigation, especially for larger claims?
3. Has it affected the way Project Insurance proposals are now being structured, including the insurance advice being given to Sub-contractors?
4. Should all parties – Owners, Developers, Contractors and Sub-contractors – now be considering the potential implications of the ruling when agreeing new standard contracts?