

## **The Impact of Construction Insurance on Risk Allocation**

**by**

**Professor Michael Furmston**

The meeting of the Society of Construction Law on 2<sup>nd</sup> November 1999, chaired by Michael Lent of Hammond Suddards, was addressed by Professor Michael Furmston, well known in the legal world both as an academic at the University of Bristol and as editor of the Construction Law Reports. He considered a subject of recent judicial development, the impact of provisions for insurance in standard construction contracts on the allocation of liability.

Professor Furmston stated three propositions. He emphasised that there is no special body of building contract law, although such contracts may give rise to problems not encountered in other areas of contract law. Further, both case law and statute regulate a party's ability to rely on exemption clauses; reliance is possible only if that party has taken steps to incorporate such a clause and if the clause clearly and unambiguously states the circumstances in which it is to apply (such as where that party has itself caused damage by its own negligence). Finally, it is common for one or both parties to insure against events which may give rise to claims: unusually, standard forms of construction contract impose an obligation to do so.

The incidence of insurance however may be considered relevant by the Courts. In *Photo Productions v Securicor* the House of Lords held that the Defendant could rely on a term exempting it from liability for damage caused by its arsonist employee since the sensible course for the Claimant to have taken was to insure its property. Yet, unusually, the Courts have held that the fact that a party is insured is enough to relieve a party from liability even where there is no such exemption clause. Such cases fall into two major groups; cases where the dispute in issue was made between the Employer and Contractor and cases where the relevant dispute involves the Employer and Sub-Contractor.

A case within the first group was *Scottish Special Housing Association v Wimpey*. Wimpey had contracted to modernise 128 houses on the terms of the JCT 1963 edition with quantities local authorities edition 1977 revision. The Scottish House of Lords held that Wimpey could not be liable for damage which was assumed to be caused by it, since under sections 18(2) to

20(C) the Claimant had been obliged to take under insurance in respect of that damage. Following the English Court of Appeal's decision in *Archdale v Con Services* the Court held in a short judgment, that those contractual arrangements excused Wimpey from liability. The case did not establish that whenever an Employer was obliged to take out insurance it would be held to have assumed the risk of damage by the Contractor, as was demonstrated by the Court of Appeal's decision in *Dorset County Council v Southern Felt Roofing*. In that case the Court disapproved the Trial Judge's approach, which had been based on a comparison between the contract in question with the form used in *Scottish SHA v Wimpey*. Instead it considered the contract alone and held that its wording was not appropriate so as to exclude the Contractor from liability.

Professor Furmston commented that the Court of Appeal's decision in *Dorset* was the conclusion one would normally expect a Court to reach in such cases were it not for the decision in *Wimpey*. Where one party had agreed to provide an indemnity to the other the Courts have held that the other party can claim indemnity in respect of damage caused by its negligence only if the wording of the indemnity provisions clearly allow it to do so. The Court took a different approach in *Wimpey*. Although the Joint Contracts Tribunal is apparently content with the decision in *Wimpey* - it has not amended the JCT form - he questioned why it did not make that clear by stating explicitly the effect of the contract.

Professor Furmston considered those cases in which the Employer and Contractor had contracted on terms under which the Employer was to insure its property and that property was damaged by a Sub-Contractor. The House of Lords in *Scruttons v Midland Silicones* had held that exemption terms made in a Main Contract could not be relied upon by third parties. However in two recent decisions, the *Mahkutai and Piling Contractors* case, the Privy Council upheld "Himalaya" clauses in the Main Contract created to protect such third parties. Even in the absence of such clauses Sub-Contractors have sometimes obtained the benefit of provisions obliging the Employer to obtain insurance such as to avoid liability (as in *Norwich City Council v Harvey*).

The position has been recently reconsidered by the House of Lords in the Scottish case of *British Telecom v James Thomson*. Since *Wimpey*, tort law had developed, primarily to restrict liability for economic loss, yet also in cases of damage to property. The Defendant, a

domestic Sub-Contractor, sought to rely on such developments, arguing that it was not fair, just and reasonable to impose a duty of care to prevent damage to the Claimant Employer's property: it argued that the Employer's obligation under the Main Contract (the JCT 1980 edition) to insure such works caused it not to consider the need to insure itself. The House of Lords, although not disapproving authorities such as Wimpey, held that the Defendant did owe such a duty. The relevant section, section 22(C), distinguished between nominated and domestic sub-contractors such that it was clear that BT could not sue nominated Sub-Contractors. By contrast no such provision served to protect domestic Sub-Contractors.

Other recent authority has reduced the extent to which a Sub-Contractor or Contractor can avoid liability. In *Kruger Tissue v Frank Galliers* HH Judge Hicks held that they could not do so where the obligation on the Employer to insure did not extend to insurance against the loss of profit and production claimed by the Employer. The result is that the Employer may be able to sue in respect of some but not all heads of loss.

In the question and answer session which followed his address, Professor Furmston commented that the forthcoming Contracts (Rights of Third Parties) Act may alter the position in that an agreement between parties to a Main Contract to exclude its operation could prevent Sub-Contractors from relying on the benefit purportedly conferred on them by insurance provisions. He added that very few standard form contracts contain Himalaya clauses on which Sub-Contractors may specifically rely, although the Model Form I (Mechanical and Electrical) contract does (with the result that a third party could be exempt from liability).

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November 1999