Construction and Infrastructure Projects
– Risk Management through Insurance

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This paper is intended only to provide an alert service on matters of concern or interest to readers. It should not be relied upon as advice. Matters differ according to their facts. The law changes. You should seek legal advice on specific fact situations as they arise.
1. **Overview**

In this paper, we review:

- the types of risks commonly associated with construction and infrastructure projects;
- the role of insurance as a means of managing such risks;
- outline the types of insurance typically involved in an Infrastructure Project; and
- analyse some of the current issues with construction insurance.

For the purposes of this paper, we have focussed upon insurance as a risk management tool for larger infrastructure projects. However much of what is said will apply equally to smaller construction projects.

Insurance is, of course, only one means of managing risks associated with such projects. It needs to be put into context and understood that not every risk can be insured against, insured against adequately or insured for a price that is acceptable.

It is important to understand the extent of the insurance contract before contractual terms are finalised to avoid circumstances where risks have been assumed based on the wrong assumptions of a party's ability to obtain particular insurance at a commercially acceptable price (or at all).

This is of particular concern in the current climate where insurance premiums are higher, policies contain many exclusions and the number of insurance products available on the market is, if anything, contracting rather than expanding.

There are two "take home" messages from today's presentation:

1. to emphasise the need to consider risk assessment and insurance needs at the outset of negotiations so that the limitations on any insurance policy is understood; and
2. to tailor all the project documents including the insurance contracts to ensure that the allocation of risk is clear.

2. **Risks and Construction/Infrastructure Projects**

2.1 **Why identify risk?**

The provision of insurance is generally considered important and indeed in the event of a major loss, the insurance may be the only viable means of repaying financiers or ensuring that the Project is back on track. However paradoxically, rarely does insurance receive the attention it deserves, either within the overall context of the deal or in the detail of the interrelationship between the drafting of the construction and franchise agreements and the insurance wording.

In order to put insurance into context, it is necessary to start at the beginning. The identification of risk is obviously the first step towards the development of risk management and reduction strategies. In an ideal world, every job would be delivered on time, without problem for the greatest possible margin of profit. Identification, allocation and
management of risk, by whatever means is deemed appropriate, is the best prospect of
ensuring the closest approximation to the ideal.

Risk identification is relevant to determining such matters as:
1. whether and, if so, how the risk should be laid off;
2. pricing a contract and allowing in the pricing for the potential cost of identified risks;
3. even in assisting the realisation that the job is not one which should be attempted.

All parties need to be alert to these issues in both the negotiation of any contractual
arrangements which allocate or apportion the risk and in assessing the costs
consequences of both apportioned and allocated risks and unanticipated risks. The cost
consequences will be one of the critical concerns in assessing and weighing both the
exposure of that party if the anticipated risks do occur and the capacity of that party to
absorb the cost within the estimated project profit. In short, in assessing the viability of that
party's participation in the project.

The assessment will also be critical in determining, to the extent that risk cannot be
absorbed, whether that risk should be, if possible, laid off, shared and/or insured against.

It is also important to have a basic understanding as to what other parties will perceive as
their risks and how they may seek to absorb or allocate their risks. Such an understanding
can better assist negotiations relating to risk.

2.2 Controlling/managing risk

Risk can be controlled in a number of ways, including:

• it can be assumed, ie risk taking;
• it can be priced, ie built into a tender price;
• it can be laid off - back to back conditions in contracts;
  - insured against;
• it can be refused, ie declining a job;
• it can be shared, ie by contract, by alliancing or partnering arrangements.

Latham Quote – Risk cannot be ignored.

2.3 Risk arising in the course of bringing a project to conclusion

(a) Documented risk

As each stage or element of the relationship between the parties to the project is
documented, there is new or additional allocation of risk. Different stages at which
risk may be documented include:

• financing or loan documentation;
• any agreement between the bid team;
• in the tender documentation and tender submission;
• in contracts let to carry out the works;
• in contracts between contractor and consultants relevant to the works;
• in contracts with sub-contractors retained by the contractor;
• in the operating consortium arrangements;
• in operating agreements relevant to operation of the project upon completion;
• in ongoing maintenance contracts.
• Insurance contracts.

(b) Circumstance or occurrence risk

Risk is not limited to documentation and can also arise, other than by allocation and assumption through project documents, from events or occurrences which take place in the course of designing, executing and operating the project. Some such risk can be anticipated, on other occasions it will be unexpected or unanticipated and can include such things as:

• insolvency events;
• failures by parties to perform as expected or as contractually required;
• unexpected site conditions or events external to contracts entered into, eg strikes, war, force majeure.

2.4 Timing

The potential risks need to be assessed at the outset of any Project. The risk managers, insurance brokers and legal advisors can all assist with this process. The appropriate risk management strategies need to be discussed, consulted and applied as each risk is identified.

Once agreements have been signed, it is inevitably too late to undo what has been done with the real prospect that risk may have been assumed in a way that was not intended, or without appropriate risk control risk minimisation procedures being put in place because risk has not been:

• understood or appreciated; or
• properly transferred or shared; or
• properly avoided or insured.

The decision is *Skanska v Egger*¹ – is a good example of the problems that can be caused if the interrelationship between the construction contract and the insurance contracts are not properly defined.

Skanska was appointed under a design and construct contract for a wood chipboard factory in Scotland. The Contract required the Principal to insure the works, in joint names for:

¹ [2002] BLR 236
all loss or damage from whatever cause arising, for which the Contractor is responsible under the terms of the Contract.

The insurance obtained obtained by the Principal excluded loss or damage caused by defects, errors or omissions in the design, workmanship, material plan or specification.

There were defects in the floor slab. Skanska sued the Principal for failing to provide sufficient insurance pursuant to its obligations under the insuring clause to cover the cost of rectifying the floor slab defects.

The Court of Appeal held that the obligations to insure had to be read in the light of the care of the works provision and in any event the obligation was to insure against loss or damage and this did not include ‘defects’. Consequently the Principal was not found to be in breach of contract.

Although presumably the courts correctly identified the parties’ intentions, this litigation could have been avoided if the Principal’s obligation to insure was limited to the terms of a draft insurance policy, which was attached to the construction contract. The Contractor would also have a benefit in knowing what risks were insured. This is the approach which the AS Standard Contracts take.

It can often be cost effective for Principals to take out the Contract Works Insurance, particularly if the Works forms part of a larger infrastructure project (AS4000 and 4902 have options which allow for this (Clause 16 Alternative 2). However there are a number of smaller issues which the standard contracts do not address well if at all, including:

(a) who pays deductibles?
(b) what happens if the insurer is unable to pay/is insolvent?
(c) what is the relationship between the indemnity given by the Contractor in respect of damage to the Works and the indemnity provided by Insurers. There have been some recent cases on this issue and John will speak about those later.

It is also important to know at the time that risk is identified, that risk management strategies you have in place or intend, can in fact be implemented before the risk is assumed or allocated.

If risk is to be assumed, it will be important:

(a) identify an appropriate insurer; and
(b) identify the extent of what is being offered matches the risks that are being assumed and attempt to negotiate policy terms and conditions if they do not; ideally before the execution of the other Project agreements.

The interactions referred to above, with employees at the coalface, brokers and lawyers, will also assist in the obtaining of a range of beneficial outcomes including:

- the widest possible assessment of risk;
- identification of risks that are insurable and those that are uninsurable;
- identification of policies available in the market that are relevant to identified risks;
• identification of gaps in insurance cover for which cover might be obtained on negotiation of policy extensions or new policies;
• exploration of the possibility of obtaining policies, including the cost of such policies, to cover identified but uninsured risk;
• ascertaining premiums that would be payable and the cost consequences of premiums for the project as a whole in the event of insurance cover being obtained for identified risks;
• identification of risks which should be laid off by means other than insurance, eg for reasons of cost of insurance or uninsurability;
• assisting in the costing of tender and construction risks in a more effective and reliable manner;
• identification of variations that should be sought in tender/contract documents on issues relating to risk and the allocation of risk;
• identification of variations that might be required in contract documents to ensure that available policies of insurance will have the widest possible application, alternatively to ensure that contract documents meet specific requirements of insurers;
• having regard to insurance available and underwriters’ requirements as expressed in negotiation or in insurance policies available, identification of that party best able to take out insurance policies for the benefit of the project and other parties to the project as a whole.

Ideally all parties should be undertaking the early assessment process in conjunction with their negotiation of the agreements to identify those areas where insurance is required and to provide co-ordinated approach to the obtaining of appropriate policies of insurance. This will:
• maximise the prospect of identification of appropriate policies of insurance to apply throughout the project;
• maximise the prospect that policies of insurance obtained will be co-ordinated and consistent;
• maximise the prospect that by co-ordinated approach to underwriters, duplication in policy cover will be avoided and cost savings obtained;
• maximise the prospect of reduced premiums and cost savings;
• lessen the prospects for costly and disruptive disputes between the parties and between the parties and their insurers.

2.5 Risk Allocation

There have been in-depth investigations of risk allocation within the construction industry. In Australia, we have the No Disputes report, the Latham Report² in England and the report

by Henry Tang in Hong Kong provide examples. All have had a common theme which is
that a realisation that a misallocation of risk results in hidden costs particularly litigation
costs.

There is a growing realisation that it is often in the Principal’s interest to ensure that the
Project risks are not simply passed down the chain but instead there is some degree of
‘risk optimisation’ or efficiency in risk allocation. The best known attempt to laying down an
acceptable formula was carried out by Prof Max Abrahamson. He said that:

[A] party should bear a construction risk where:

1. It is in his control, ie, if it comes about it will be due to wilful misconduct or lack of
   reasonable efficiency or care; or

2. He can transfer the risk by insurance and allow for the premium in settling his
   charges to the other party ... and it is most economically beneficial and practical for
   the risk to be dealt with in that way; or

3. The preponderant economic benefit of running the risk accrues to him; or

4. To place the risk on him is in the interests of efficiency (which includes planning,
   incentive, innovation) and the long term health of the construction industry on which
   that depends; or

5. If the risk eventuates, the loss falls on him in the first instance, and it is not
   practicable or there is no reason under the above four principles to cause expense
   and uncertainty, and possibly make mistakes in trying to transfer the loss to another.

The job of trying to balance the five principles in practice is the hard one ... But at least it is
best to work from declared principles rather than undeclared and perhaps unconscious
prejudices.\(^3\)

In the context of PPP Projects, the Abrahamson Principles should be not considered a
panacea. In fact one seasoned commentator considered that they had no application to
the complexities of a PPP Project.\(^4\) Although that may be overstating the difficulties
involved in risk allocation, the Abrahamson Principles should only be considered as a
useful starting point.

2.6 Who is at risk?

All parties involved in the construction industry must confront risk in one guise or another;
some risks will be peculiar to one party and some shared with other parties.

For example:

(a) Principals

Risks faced by principals include:

(i) that a job will be completed late, inadequately or increased cost exposure;

(ii) land acquisition risk; and


(iii) Government principals – social or political cost.

(b) The Consortium

The consortium's objective is to manage and maintain the completed project, for the period allocated to the operator, to the required standard or within the required cost parameters in a way which gives the operator sufficient funds to return a profit after operating and finance costs.

Risks facing the consortium may include:

- late delivery of the project;
- increases in operating costs, eg increased labour costs;
- design and construction defects impacting upon the operation of the completed project;
- deficiencies in other infrastructure or services upon which the successful operation of the project depends, eg feeder roads are not constructed or urban development does not proceed as anticipated;
- market risk, eg switch by potential users to public transport, reducing reliance on the tollway;
- political risk, eg change in priorities of governments and lack of ongoing political support necessary to promote the success of the project.

(c) Contractors

Risks which the contractor will have to consider, allocate, assume or lay off can arise at all stages from negotiation of the consortium or bid agreement through to the construction or design and construct contract and possibly any follow up maintenance contract.

Risks which the contractor will have to consider will include:

- Design risk - laid off to consultants
  - laid off to insurers;
  - is PI adequate?
- what site conditions might be encountered, and the consequences of unanticipated conditions;
- are there planning, site contamination, native title issues to be addressed;
- what are his obligations to carry insurance and, if so, what types of insurance;
- construction risk – defects supervision;
- what responsibilities he may have for the works of sub-contractors (particularly bearing in mind that default by a sub-contractor can have consequences for the project as a whole far beyond the value of the work being carried out or performed by a sub-contractor);
- the capacity to lay off risk to sub-contractors;
• what are specified, defect and warranty obligations in respect of the works.
• exposure to damages, penalties and costs in the event of delays in completion of the works to:
  ➢ the principal;
  ➢ consortium partners;
  ➢ the subsequent operator; and
  ➢ financiers
• management/administration risk – monitoring compliance with the insurance contracts or even obtaining copies of policies or evidence that insurance had been taken out and monitoring ongoing compliance. Often after weeks of negotiation, the contract can be put away and forgotten about.

For example – a contractor was involved in a design and construct bridge project. The Contractor subcontracted the design obligations to a subsidiary of an American design consultant. Under the consultancy agreement, the subsidiary was obliged to effect PI Insurance for up to $20 million. In fact the subsidiary was a shell company and the design work was carried out by staff specifically brought in for the Project.

The subsidiary gave negligent advice at tender stage, which exposed the Contractor to significantly more cost than it had anticipated and had budgeted for. After the bridge was complete, the Contractor sued. However, during this whole process, the tender stage, the design and construction stage and even during submission of pleadings in the litigation, no one had obtained a copy of the PI insurance policy from the designer. When the designer was finally asked for it, half way through the proceedings, it naturally said no. Faced with the uncertainty of litigation against a potentially uninsured shell company, the Contractor settled at a fraction of its claim.\(^5\) This is of course an example of the effects of litigation risk.

• the consequences of the default, or failure of a consortium partner;
• ability to rectify defects after completion.

(d) Consultants

An obvious and insurable risk for professional consultants is that their design, drawings, or advice may prove inadequate and/or negligent.

(e) Financiers

The principal concerns of the financiers will be:

• the economic viability of the project; and
• the continuity of cashflow from the project (required to service debt).

These concerns will be driven by the risk of loss of funding or inadequate return if the project is unsuccessful or incurs major problems.

Risks which financiers are exposed to include:

- delays, costs overruns, etc which may cause cashflow problems;
- insolvency of major parties to the project;
- claims against the contractor in the course of construction; and
- claims against the operator in the course of operation.

If the project sponsor/operator is, as is frequently the case, a special purpose company with limited assets set up specifically for the purpose of the project, then financiers will also seek an allocation of risk (and recourse) to those who are designing and constructing the project works as one means of laying off the risk that the security provided may prove inadequate.

Risk can be assumed and costed in the form of terms of lending, interest rates, etc, that is by allowing for more than adequate returns on the successful completion of the construction phase.

Financiers will want to explore loss of profits insurance against the risk of late delivery of the project or other delay in cashflow from the project. It may be more difficult to obtain insurance cover which specifically protects financiers’ exposure during the construction phase.

To the extent that insurance is not available to financiers to protect the risk to finance funding, then financiers may also pressure the project sponsor or those parties directly involved in design and construction to carry insurance which might then operate as a secondary recourse in the event of problems arising during the construction phase which impact on financiers’ risk.

3. **The Role of Insurance**

3.1 **Overview**

As mentioned above, insurance is not the only means by which risks associated with construction and infrastructure projects may be addressed. However, it is one of the principal means by which parties to major projects treat risk.

In considering whether or not insurance should be looked at as the answer to a particular identified risk, the following questions need to be considered:

(a) is the risk insurable - can a policy be procured which specifically covers the risk;
(b) is the cover adequate - if a policy is procured, will it respond to the risk which you have identified and to the fullest extent of that risk;
(c) does the cost outweigh the risk - what is the cost of the policy;
(d) what is the nature of the policy - how long will the policy operate to provide cover;
(e) can the policy be tailored or negotiated;
(f) is the insurer here for the long haul – to what extent can the parties have confidence that the insurer is solvent and able to honour its contractual obligations if called upon.

3.2 Policy risk
In negotiating a policy of insurance, you need to understand:

- what the risk is against which you are seeking insurance protection;
- the policy itself, how the policy operates and what obligations you may have to the insurer under the policy, eg notifications, conduct, no assumption of additional risk, etc;
- what the limitations to the policy cover are and to what exclusions the policy is subject;
- whether the policy is effective to provide cover in respect of the particular risks which you have identified and in respect of which you have sought cover, ie do the policy clauses clearly and without limitation apply to the identified risk.

Policies of insurance should also be subject to periodic review against the totality of risks insured to ensure that there are no gaps in policy coverage through which the proverbial truck may be driven.

3.3 Procedural risks
Having obtained policies of insurance which on their face provide protection, you should also be aware that until such time as the policy is tested, you cannot necessarily be certain that protection will be provided. At this time, further issues may arise which may result in a denial of insurance protection. For example, there may be issues as to:

- the policy wording – does it apply to cover the event which has occurred?
- compliance – has appropriate notice been given, has there been non-compliance with the terms and conditions of the policy which acts to preclude cover?
- interpretive issues - as to the meaning and extent of cover provided by the policy, eg is the event in respect of which cover is sought one occurrence or multiple occurrences cf arguments in respect of the World Trade Centre?
- are there issues of waiver, subrogation, etc which might be argued against you?

The claim for indemnity may trip up on any one of these issues and again leave you uninsured, alternatively involved in lengthy and expensive court proceedings which waste resources and divert management time, to determine whether or not insurance does apply.

3.4 Quantum risk
Insurance policies will have a deductible excess, ie uninsured element. An assessment has to be made by weighing premium costs against the amount of uninsured risk which you will carry before insurance cover kicks in.

Equally, you may have determined that policy cover of, say, $50 million, is adequate to protect against identified risks, whereas the consequence of catastrophic failure may see claims emerge well in excess of the insurance cover. Again, you are exposed in respect of that excess.
Contracts requiring insurance almost invariably set a limit of indemnity, but less often a deductible.

4. Types of Insurance

We discuss below issues which may arise in relation to the key classes of insurance commonly required in construction and infrastructure projects.

The following is by no means a definitive list of the types of insurance which may be required for a particular project.

4.1 Contract Works

Contract Works insurance is often provided as a combined material damage and legal liability policy.

The first part of the policy usually insures against physical damage to:

- the works under construction
- materials for the project stored on site and off-site
- temporary structures
- hired plant and equipment
- contractor's plant and equipment (although in some cases this is insured separately under Contractor's Constructional Plant insurance)

The second part of the policy insures against damage to property or personal injury to third parties arising from construction activities on and off the site.

Contract Works policies will usually contain exclusions for, amongst other things, faulty workmanship and design. They do not cover all risks associated with the building works and most importantly, where design is an issue, must be supported by professional indemnity cover.

This type of insurance is usually taken out by the contractor but can be taken out on a principal controlled or project manager controlled basis and in such case should name the principal, project manager, contractors and subcontractors as insureds under that policy.

A construction program is usually put to the insurers (such as we are going to develop an underground mine which will go down to a certain number of levels and construct a treatment plant and this is going to take 18 months) and the contract works insurers agree to cover the principal and the contractors for that period. At the completion of the construction phase the ISR insurer will then take over. Sometimes however there is a phased handover from the contract works policy to the ISR policy and this is because it is a cheaper option but it can get very complicated. What that means is the contract works policy will apply to various stages of the project and as each stage is completed that stage is taken out of the contract works policy and covered under the ISR policy. So for example you might find that you have a pipeline which has been built and is completed and the pipeline may be used to run off water while part of the mine is developed. Once the pipeline has been completed it can be taken out of the contract works policy and put into
the ISR policy. However if it is being used for construction purposes it may be considered to still fall under the contract works policy but it may also fall under the ISR policy because it itself has been completed. You may end up with disputes between insurers, for example, the ISR insurer may say that the pipelines are not covered by the ISR policy because they are being used as part of the construction process but the contract works insurer may argue that the pipeline is not covered because it has been completed and is no longer itself under construction.

Similar complications can arise where the works involve extensions or refurbishment to existing structures. The interface between the works and the existing structure must be clearly defined to avoid a stand-off between insurers.

Another means of minimising such insurance disputes is for the Contract Works and ISR policies to be placed with the same insurer. However, this can give rise to other issues. All we can recommend is that you have sophisticated brokers to advise on these issues.

4.2 Industrial Special Risk (or 'ISR')

This insurance is sometimes referred to as ‘Property Damage and Business Interruption’ insurance.

Like Contract Works insurance, an ISR policy normally has two components. The first of these is property damage, under which cover is provided for the physical loss, destruction or damage to all tangible property belonging to the insured, or for which it has assumed responsibility to insure. If a loss occurs, the policy allows for reinstatement or replacement of the damaged property. The policy has, as most policies do, a number of exclusions and these usually include war, radiation, wear and tear, faulty materials or faulty workmanship, error in design, theft, fraudulent acts, erosion, earthquakes, flood, kidnapping and bombing.

The second part of the ISR policy is what is called a business interruption section under which cover is provided for consequential or pure economic losses resulting from an interruption to or interference with business following damage to an asset insured under the first part of the policy. For example, it would say something like:

> If any building or other property used by the insured at the premises for the purposes of the business is lost, destroyed or damaged, and the business carried on by the insured in consequence thereof is interrupted or interfered with, the insurers will pay the amount of the loss suffered as a result of that interruption or interference.

Of course as you would expect there is a formula set out as to how the insured's loss is calculated along with a number of exclusions. The policy will usually cover either the reduction in gross earnings or the loss of gross profit and in some policies the insured can elect which formula to adopt.

Calculating the loss of profits claim under the business interruption section of an industrial special risks policy is very complicated and it is necessary to use either very experienced loss adjusters and some accountancy firms have expertise in this area. It is not usually the sort of matter that an ordinary accountant would be able to do.

Furthermore, as referred to above, it is critical to manage the interface between the works and existing structures and the transition of particular items under construction from cover under the Contract Works policy to cover under the principal's ISR policy, to ensure there
are no gaps in cover, having regard to the fact that a principal will usually elect for its ISR cover to commence only at the same time as commencement of commercial operations.

4.3 Professional indemnity

As its name suggests, this insurance indemnifies an insured for amounts which the insured becomes legally liable to pay as a result of any actual or alleged negligent act, error or omission in the conduct of its business or profession. Costs and expenses incurred to investigate, defend or settle any claim are also included, sometimes in addition to the policy limit.

PI insurance is a 'claims made' insurance. This means that the policy only responds to claims first made against the organisation during the policy period, irrespective of when the act of negligence actually occurred. This is an important point of distinction to other policies, such as Public and Product Liability, where coverage is provided for occurrences when the policy is in force even if the claim is made after expiry of the policy.

It is common for a principal to require a contractor to have PI insurance where the contractor is to provide engineering, design, project management or other professional advisory services relied upon by the principal. A principal will also usually endeavour to ensure that the contractor maintains such insurance for a number of years after completion of the contractor's work.

Sometimes the principal will assume responsibility for PI insurance of its consultants subject to a nominated excess, and then require the contractors to maintain their own PI insurance for claims up to value of the excess under the principal procured policy. The rationale behind such an approach might be as follows:

- the particular project would give rise to PI issues for a number of consultants;
- the consultants are likely to pass on to the principal the cost of obtaining the PI insurance required by the principal and the principal would be at risk of a claim being made by another principal to which the consultant has provided services that would remove or reduce the coverage available for claims by the principal; and
- a principal controlled, project specific PI policy can be tailored to the particular circumstances of the project, would maximise the prospects of recovery by the principal and would avoid the need for the principal to review its consultants' PI insurance for several years after the completion of their work.

4.4 Public and Product Liability

This insurance is sometimes referred to as 'Combined Liability' or 'General Liability' insurance. Again, there are usually two components to this policy:

- Public Liability: Legal liability to pay compensation to third parties arising in connection with the business activities of the insured. This part is limited to a maximum amount for any one occurrence or event (or series of claims from the one incident), but generally unlimited in the number of events it will respond to in any one policy year.
- Product Liability: Legal liability to pay compensation to third parties arising in connection with the insured's products. This section is limited to a maximum amount for any one term and for all claims in any one policy year. Most insurers now accept that insureds have a products exposure, even if they do not manufacture or produce anything in a tangible sense (eg food and beverages supplied at the insured's cafeteria).

In large infrastructure projects, it is common for the principal to require a contractor to procure Public and Product Liability insurance immediately upon the commencement of the operational phase of the project. This insurance then takes over from any liability cover provided under the Contract Works insurance.

4.5 Workers’ Compensation

All states and territories have statutory requirements for employers to effect workers’ compensation insurance for the benefit of their employees. While there are variations from State to State, this insurance effectively covers all liabilities, whether arising under statute or at common law, in relation to the death of, or injury to, employees or persons deemed to be employees.

It is common for a principal to require a contractor to maintain the necessary workers’ compensation insurance in respect of all employees engaged in performing the contract. The principal may also seek endorsements on the contractor's workers' compensation policy, in the case of a contract for a project with specific recognised hazards eg the construction of processing facilities for a mine, endorsements may be sought to extend cover to industrial diseases and to include employees working underground.

A principal will usually seek to be named and insured as a principal under the contractor's workers compensation policy. This is to cover claims by contractors' employees who assert that the principal is a deemed employer.

4.6 Compulsory Third Party Motor Vehicle

Each state and territory in Australia has legislation making it compulsory to arrange insurance for third party injury liability arising out of the use of a motor vehicle. Like the workers’ compensation legislation, administration of the CTP scheme, premiums levied and the extent of cover provided vary from jurisdiction to jurisdiction.

Principals often require the inclusion of a provision requiring the contractor to take out all necessary CTP insurance as required by statute in the relevant jurisdiction for vehicles used in connection with work under the contract.

4.7 Marine Cargo or Transit

This insurance covers the risk of loss or damage to cargo being transported from one country to another by sea, road, rail or air and is required, for example, where a significant item of plant or equipment needs to be transported from the country of its manufacture to the project site. Equipment being transported domestically is usually covered by the Contract Works policy.
It is common for the principal to take out Marine Cargo insurance, at least where the principal has assumed title and risk in relation to the product at a place other than where the product is required.

4.8 New insurance products

New insurance products evolve as the insurance market develops new approaches to address risk.

Of potential importance for construction/infrastructure projects, one insurance product new to the Australian market is transactional insurance.

Transactional insurance is directed at protecting parties from risk-related contingencies or disagreements which might otherwise block the completion of a business transaction. For example, transactional insurance may be used to replace more traditional forms of risk treatment such as indemnities or representations and warranties in the project documentation, letters of credit, a party accepting reduced financial benefit or retaining financial liability following a deal. Risks which may be addressed by transactional insurance include one party's withdrawal from the transaction, unfavourable regulatory changes and decisions, unfavourable tax treatment, environmental liabilities and loss associated with existing litigation.

Obviously, the precise terms of a policy within the above ‘classes’ of insurance will vary from insurer to insurer and be affected by the prevailing market conditions and the circumstances of the project to be insured.

5. Examples of risk allocation and insurance clauses

Many construction contracts in general use contain provisions relating to the obtaining of insurance and direct by whom insurance is to be obtained.

Frequently, project documentation will be based upon the industry standard contracts, for example, Australian Standards contracts AS4300 (‘General Conditions of Contract for Design and Construct’) and AS2124 (‘General Conditions of Contract’).

However, it is important that insurance provisions are not treated as ‘boilerplate’. Careful thought does need to be given to the allocation of insurance responsibilities; simply accepting allocations in standard form contracts may not be the best solution. The risks associated with a particular project should be carefully identified and assessed and then the insurance provisions can be negotiated in the context of the allocation of those risks (and, of course, the insurance cover available). By way of example, Annexure 1 to this paper contains extracts of insurance related provisions from a major infrastructure project.

6. Current issues in relation to negotiating insurance clauses

The following section discusses a few topical issues relevant to the negotiation of insurance clauses.
6.1 **Who is the insured?**

One decision which has to be made in the process of obtaining insurance cover is who is the appropriate party to seek insurance.

Again, collective review at the outset of risk and risk allocation issues together with insurance requirements and insurance issues will prove a useful tool in assisting decisions on not only what insurance cover is required, but also who is the appropriate party, or who are the appropriate parties, to apply for and carry that insurance.

*Should the principal take out insurance?*

There may be certain benefits for the principal to take out cover for the project naming the contractor, consultants and contractor’s sub-contractors as insured parties. For example:

- comfort to the principal that insurance is in place, rather than reliance upon others to effect insurance;
- if the principal is a large enterprise and is able to use economies of scale, then the principal may also be able to obtain cost savings in premiums on any policy obtained;
- control over renewal and form of policy, in particular there is no need to be checking on a regular basis that other parties have obtained required policies and have maintained those policies current;
- if the policy is one which is best suited to a principal, eg project-specific insurance or a construction management contract;
- a principal initiated policy naming all parties may reduce or prevent subrogation and cross-claims, particularly in circumstances where there may be a number of contractors working on different aspects of the project and where their works interface, eg a rail project where you may have one contractor building the station and another laying the track.

On the other hand, a number of practical difficulties may arise where the principal takes out insurance including:

- who makes the claim, pays the deductible and signs a release in respect of building claims where care of the works is imposed on the contractor;
- what happens if the principal settles a claim with insurers for less than the contractor believes the damage has cost;
- what happens if the care of the works provisions require the contractor to accept greater risks than those insured by the principal, ie can the principal in fact obtain coverage which adequately protects the interests of all the parties named as insured.

Careful drafting should be able to overcome the above issues but it is important to keep them in mind.

*Should the contractor take out the policies?*
Similar issues arise for consideration to those issues which the principal must consider. From the contractor's perspective, it might prefer to have the certainty of having affected insurance given that, in most instances, it will have care of the works. However, there is the burden that attaches to organising the insurance and satisfying the principal of the existence and adequacy of the insurance, to consider.

*Should all parties take out their own policies?*

Issues then arise in relation to the co-ordination and checking of policies. Do they provide complete cover or have gaps arisen where there is uninsured risk? Who will undertake the process of co-ordinating and reviewing the policies to be satisfied that policies taken out by individual parties provide seamless cover in sufficient amount for all the work to be performed in relation to the various phases of the project?

Quality control or management issues arise in relation to ensuring that policies are obtained, premiums paid and policies renewed not only for the duration of the project, but for any identified or appropriate period subsequent to completion of the project.

We would usually not recommend all parties taking out their own policies.

The benefits of a supervening coverage arranged by one party were acknowledged by Lloyd J in *Petrofina (UK) Ltd & Ors v Magnaload Ltd & Anor* [1984] 1 QB 127 at 136, where his Honour stated:

…there can be no doubt about the convenience from everybody's point of view, including, I would think, insurers, of allowing the head contractor to take out a single policy covering the whole risk, that is to say covering all contractors and sub-contractors in respect of loss of or damage to the entire contract works. Otherwise each sub-contractor would be compelled to take out his own separate policy. This would mean, at the very least, extra paperwork; at worst it could lead to overlapping claims and cross-claims in the event of an accident. Furthermore,…the cost of insuring his liability might, in the case of a small sub-contractor, be uneconomic. The premium might be out of all proportion to the value of the sub-contract.

### 6.2 Double Insurance

Generally speaking, double insurance exists when the same insured is covered by more than one contract of insurance in respect to the same loss.

A detailed paper on double insurance and contribution was presented as part of last year's Insurance Breakfast Seminars. For the purposes of today's presentation, we simply wish to flag the problems which can arise where, despite a clear contractual intention in the project documents that the responsibility for insuring the project lies with the principal, the underwriters of the principal controlled cover may seek recovery from the underwriter of the contractor's policy on the basis of double insurance.

Given that the insured has a right to claim against any of the liable insurers, and included 'other insurance' clauses which excluded cover in the event of another policy covering the same risk, the onus is then on the insurer who indemnifies the insured to seek contribution from the other insurers, double insurance is generally an issue for insurers as opposed to insureds. However, this can give rise to cost implications for insureds (eg it may impact on future premiums where a claim is made against a policy which was not intended by the named or primary insured to respond to such claims).
The problem essentially arises due to s45 and s76 of the *Insurance Contracts Act*.

The effect of s45 of the *Insurance Contracts Act* is to render ‘other insurance’ clauses ineffective except in the permitted circumstances of compulsory insurance or where the other cover is appropriately specified.

**Section 45 of the Insurance Contracts Act** provides:

1. Where a provision included in a contract of general insurance has the effect of limiting or excluding the liability of the insurer under the contract by reason that the insured has entered into some other contract of insurance, not being a contract required to be effected by or under a law, including a law of a State or Territory, the provision is void.

2. Subsection (1) does not apply in relation to a contract that provides insurance cover in respect of some or all of so much of a loss as is not covered by a contract of insurance that is specified in the first-mentioned contract.

**Section 76 of the Insurance Contracts Act** complements s45 in that it allows an insurer who has paid out a claim which was subject to double insurance to obtain contribution from any other insurer liable in respect of the same cost.

One ambiguity which arises is the degree of ‘specificity’ required by s45(2) to avoid the operation of s45(1). There is very little case law on this issue. Some guidance was recently given by the NSW Court of Appeal in *HIH Casualty and General Insurance Ltd v Pluim Constructions*.

In this case, Pluim Constructions (Constructions) was doing building work at a recreation club (the Club). Related companies Pluim Detail Joinery Pty Ltd (Joinery) and Pluim Commercial Landscapes Pty Ltd (Landscapes) were also involved with the job.

Constructions had public liability insurance with the appellant (HIH). Pursuant to requirements in the building contract, the Club also had relevant public liability insurance for Constructions with Commercial Union Assurance Company of Australia Ltd (CU).

Mr Knight, a Landscapes' employee, was asked to assist Constructions by removing debris from the site using vehicles belonging to Landscapes, and in the course of doing so, sustained a knee injury from glass shards. There was not meant to be glass in the relevant debris.

Knight sued Constructions and Joinery in the District Court. Constructions was found to have breached its duty of care to Knight and damages were assessed against it. Constructions had filed third party notices in respect of claims for contribution or indemnity under various insurance policies and against the Club for damages for breach of the building contract.

CU denied liability to indemnify Constructions, relying upon various exclusions in its policy (in particular, Exclusion 6 which excluded certain claims arising from the operation of a motor vehicle).
HIH argued that it should be allowed to escape liability because of Exclusion 4 of the policy (an exclusion which was again with respect to liability arising from operation of motor vehicle).

Alternatively, HIH relied on Condition 7 of its policy, which was essentially an ‘other insurance’ clause, to argue it had no liability (because the CU policy applied). Condition 7 of the HIH policy stated:

**PRINCIPAL-ARRANGED INSURANCE**

In the event of the named Insured entering into an agreement with any other party (who for the purpose of this clause is called “the Principal”) pursuant to which the Principal has agreed to provide a policy of insurance which is intended to indemnify the named Insured for any liability arising out of the performance of the Works, then the Company(ies) will (subject to the terms and conditions of this Policy) only indemnify the named Insured for such liability not covered by the policy of insurance provided by the Principal.

Alternatively, HIH argued that if Exclusion 4(a) and Condition 7 did not apply, it was entitled to contribution from CU.

In short, the case involved consideration of 3 issues:

- whether CU could rely on Exclusion 6 of its policy to decline Constructions’ claim;
- whether HIH could rely on Exclusion 4(a) of its policy to decline Constructions’ claim;
- assuming neither exclusion was applicable and both HIH and CU were prima facie liable to indemnify Constructions, what was the effect of Condition 7 of the HIH policy.

At first instance, the trial judge held that the CU policy did not respond, but that the HIH policy did respond. While it was unnecessary for the trial judge to make a decision on Condition 7 of the HIH policy, he held that the language of Condition 7 was too general and not of sufficient specificity to satisfy s45(2) of the Insurance Contracts Act.

HIH appealed.

On appeal, the NSW Court of Appeal held:

- By a 2:1 majority (with Mason P dissenting), Exclusion 6 of the CU policy did not apply, and therefore the CU policy did respond and CU was liable to indemnify Constructions.
- By agreement, Exclusion 4(a) of the HIH policy did not apply and therefore HIH was prima facie liable to indemnify Constructions under the HIH policy.
- By agreement, Condition 7 of the HIH policy failed to adequately specify the CU policy for the purposes of s45(2). Accordingly, Condition 7 was rendered void pursuant to s45(1).

The discussion of the interpretation to be given to s45(2) is contained in the judgment by Mason P. It should be noted that Mason P gave the dissenting judgment which found that the CU policy did not respond to Constructions’ claim. As such, Mason P found that it was unnecessary to address the issue of the operation of Condition 7, but since it was fully
argued, he did “address some remarks to the topic”. Mason P’s comments on Condition 7 and the operation of s45(2) were accepted by Handley JA and Foster AJA in their joint judgment.

Mason P considered that the issue was whether the words ‘the policy of insurance provided by the Principal’ in Condition 7 were sufficient to specify the CU Policy within the meaning of s45(2).

In his deliberations, Mason P noted that s45 originated from the recommendations of the ALRC’s Report on Insurance Contracts (discussed above) and that the explanatory memorandum explaining clause 45 of the Bill identified the mischief addressed in clause 45 in terms broadly similar to the ALRC Report.

Mason P found that the policy of s45(1) suggested that the exception in s45(2) should be construed narrowly. In this case, Mason P considered:

… there was no identification of any particular policy with any particular insurer. The type of insurance which the proprietor was obliged to take out was described in the building contract in terms of the broadest generality and with no reference to conditions or exclusions. The HIH Policy is not in form or substance, a type of layered insurance or excess insurance. The fact that “a policy of insurance” would be “principal-arranged” only emphasises its futurity, contingency and the lack of relevant specificity. In the context of condition 7, “a policy of insurance” means any policy of insurance. This is the antithesis of “a … specified contract” within s45(2).

Further, Mason P noted:

It may be that a contract of insurance need not actually have been formed and/or commenced before it is capable of being specified within s45(2). And it is possible that a clearly defined class of insurance, such as “X’s Standard Construction Policy with an excess of Y” would suffice. I prefer to reserve my position on these possibilities. They are far removed from the present situation.

In view of the above, unless a policy covers an insured’s excess liability, it is likely that s45 will render void an “other insurance” or notification clause. In these circumstances, if an insurer wants to reduce the possibility of being caught in a double insurance situation, this can only really be solved by ensuring that what an underwriter intends to cover is reflected in what the policy wording says.

6.3 Indemnity vs insurance

Most construction contracts contain an indemnity granted by the contractor in favour of the principal for damage to the works and/or for claims for injury, death or third party property damage to the extent the principal is not responsible for that loss or damage (or to the extent not otherwise accepted). By way of example, AS4300-1995 contains the following indemnity provision:

…

The Contractor shall indemnify the Principal against:

(a) loss of or damage to property of the Principal, including existing property in or upon which the work under the Contract is being carried out; and
(b) claims by any person against the Principal in respect of personal injury or death or loss of, or damage to, any property,

arising out of or as a consequence of the carrying out by the Contractor of the work under the Contract, but the Contractor’s liability to indemnify shall be reduced proportionally to the extent that the act or omission of the Principal, the Superintendent, or the employees or agents of the Principal contributed to the loss, damage, death or injury....

The relationship between indemnity and insurance provisions in a services agreement was considered in some detail by the Full Court of the Supreme Court of Western Australia in the *Speno* case⁷. In that case, Speno had contracted to provide rail grinding services and to operate the principal's rail grinding machine. An employee of Speno was injured when travelling to the rail grinder in the principal's Landcruiser which had been modified to travel along the railway line. The vehicle was derailed due to the negligent switching of points at a siding by an employee of the principal. The case contains a number of findings. However, the most important part of the decision for present purposes was the response of the Full Court to the contractor's argument that a clause requiring the contractor to take out workers' compensation insurance indorsed to indemnify the principal resulted in the contractual indemnity not applying. The court found in favour of the principal on this point. Reference was made to the decision of Phillips J in the Buller Ski Lifts case, in which his Honour said:

> the need for insurance cover [in addition to an indemnity] recognises, I think, the commercial possibility of insolvency or some other obstacle standing in the way of the [insured party] meeting the call for an indemnity, when made.

In her judgement in the *Speno* case, Wheeler J suggested that:

> where, as [in the *Speno* case] there is a contract for services which contains within itself an indemnity provision, together with insurance which may also cover the events the subject of the indemnity, it is generally appropriate to regard the insurance as a secondary rather than a co-ordinate obligation.

The message to be taken away from the *Speno* case, which is of particular importance to contractors, is that one should not assume that a principal will not be able to enforce an indemnity provision against a contractor simply because the contract obliges the contractor to procure insurance that may cover the same events as are covered by the indemnity.

### 6.4 Limitation of liability

There is a growing tendency for contractors under design, construction, procurement and related contracts to seek to introduce a cap on their liability under the contract. The cap sought is usually expressed in very broad terms so as to make even the indemnity clause subject to the cap on liability. The size of the cap might be an identified monetary amount or the contractor’s estimate of the profit it will derive from performing work under the contract.

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⁷ *Speno Rail Maintenance Australia v Hamersley Iron Pty Ltd* [2000] WASCA 408
The benefit to a contractor of a cap on liability is self evident. It quantifies and caps the maximum prospective liability of the contractor to the principal if things go wrong in the performance of the contract. This has obvious benefits for financial management, risk management, claims management, external financing, and perhaps even shareholder relations.

From the perspective of the principal, a cap on the contractor’s liability needs to be approached with caution. In addition to the effect of a cap on liability on a contractual indemnity, it can also impact on the principal’s rights to recover under its own or the contractor’s insurance policies.

Where a principal considers that it is reasonable or commercially necessary to accept a cap on the contractor’s liability, it should consider a number of matters:

1. Is the size of the cap sought by the contractor appropriate in the circumstances of the particular contract or is there a more appropriate figure?

2. Some of the principal’s own insurance policies will prevent the principal from limiting its rights of recovery against third parties and, to the extent the principal does so, its insurer may refuse coverage if the insurer’s ability to recover against third parties is prejudiced by the limitation of liability. Alternatively, where a principal takes out a PI policy on behalf of all consultants and engineers involved in a project and a consultant has negotiated a limitation on its liability to the principal in its services agreement, where the principal makes a claim against the consultant to which the insurance policy responds, the insurers will argue that they have the benefit of the contractual limitation of liability conferred on the consultant.

Accordingly, care should be taken when drafting the cap on liability to ensure that the cap is in addition to amounts recoverable under insurance policies.

6.5 Insurance placed with reputable insurer

A number of standard form contracts impose an obligation on contractors to take out the prescribed categories of insurance with a reputable insurer having a credit rating of not less than a prescribed rating of a recognised ratings agency, such as Standard & Poors. The reasons for introducing such a requirement are obvious in light of the collapse of HIH.

Given the current state of the insurance market, many large contractors are now self-insuring for all or part of their exposure. If a contractor proposes self-insurance, then consequential amendments will obviously need to be made to the standard provisions and thought given to what proof a self-insured contractor should provide of its ability to meet any claim made.

6.6 Insurance obligations – an ongoing issue

Most construction contracts contain a provision along the following lines:

Proof of insurance

Before the Contractor commences [work under the Contract] and whenever requested in writing by the other party, a party liable to insure shall provide satisfactory evidence of such insurance effected and maintained.
Some construction contracts run for several years. Some insurance provisions require a party to keep in place a particular type of insurance for a period of time after completion of work or for there to be a 'run-off' period allowing claims to be made after the completion of the work but in respect of the relevant work. There is therefore good reason to include a clause along these lines.

However, if appropriate contract administration practices are not in place, there is a risk that a party required to maintain prescribed insurance under the contract may fail to comply with that obligation and an event occurs to which insurance would have responded had it been in place. In these circumstances, a party might have a claim in contract against the other but the party in default may not have the financial resources available to satisfy the claim.

Careful thought should therefore be given to developing an appropriate set of contract administration procedures and a checklist of material obligations and there should be frequent reference to those documents by an appropriate person within the relevant organisation and even diary entries to operate as reminders for the necessary periodic compliance checks.

Further, as a result of the current insurance climate, it may be that insurance which was available say 5 years ago, may no longer be readily available or may not be available on terms satisfactory to the party required to obtain the insurance. We are seeing an increasing number of matters where failure by one party to comply with insurance obligations (due to a change in the insurance market conditions) is being used as a means to either terminate a contract or reopen negotiations on allocation of risks under the contract.

6.7 Terrorism cover

Pursuant to recent terrorism insurance legislation enacted by the Commonwealth Government, terrorism exclusion clauses in non-residential property and business interruption policies covering Australian interests will not operate if there is a declared terrorist incident in Australia.

The relevant legislation is the Terrorism Insurance Act 2003 (which commenced on 1 July 2003) and the Terrorism Insurance Regulations (which were gazetted on 26 June 2003). This development is discussed in AAR's July publication of 'Focus On – Insurance' which is available on the AAR website.

In summary, the key aspects of this legislation include:

- For eligible insurance contracts in force at 1 July 2003, or which begin after that date, if there is a terrorist incident (as declared by the relevant Minister), then any terrorism exclusion is rendered inoperative and cover is provided for eligible terrorism losses in accordance with the other terms and conditions of the policy.
- The legislation applies to policies irrespective of whether they are issued by Australian or overseas insurers.
- The Terrorism Insurance Regulations prescribe a large number of contracts which are excluded from this coverage including home building and home contents policies;
various types of liability cover such as professional indemnity, directors' and officers' liability, trade credit and trade indemnity; motor vehicles policies; and marine and aviation insurance.

Insurers affected by this legislation are fully indemnified for claims and claims settlement costs arising from policies in force on 1 July 2003, or incepted between 1 July and prior to 1 October 2003. On or after 1 October 2003, insurers can reinsure with the Australian Reinsurance Pool Corporation, or alternatively, they will need to have made a decision to take the liability on their own balance sheet or to seek other alternative reinsurance arrangements.

Insureds will need to consider which policies are covered by this legislation and which are not in order to make an assessment of their existing coverage and what coverage they may still need to obtain.

7. **Illustrative cases**

7.1 **Policy wordings and construction claims**

Each case will, of course, turn on the particular circumstances of the claim and the particular policy wording. However, the following cases provide examples of how relatively common policy wordings have been applied in the context of construction-related claims.

(a) **Transfield Pty Ltd v National Vulcan Engineering Insurance Group Ltd** [2002] NSWSC 830 per McClellan J (17 September 2002)

Transfield's case provides an example of complications in policy interpretation which can arise where a head contractor takes out an insurance policy which includes its subcontractors as insureds.

**Key Facts**

Transfield was the head contractor for the construction of a section of the New Southern Railway in NSW. Transfield took out an insurance contract described as a Contractors' Floater Policy (the *Policy*), which included its subcontractors as insureds 'for their respective rights, interests and liabilities'.

Subsequently, two incidents occurred where sheet piling on the site failed and caused damaged to property owned by Transfield and to equipment owned by two of Transfield's subcontractors.

The two subcontractors each brought a claim for compensation against Transfield and two of Transfield's consultants on the project. Transfield brought a claim against the two consultants. The two consultants each brought a claim against the other and Transfield.

This case arose from a claim for indemnity under Section C of the Policy by Transfield and the two consultants, which was declined by the insurers.

Section C of the Policy relevantly provided that the insurers agreed, subject to the limitations, terms and conditions of the Policy, to indemnify the Insured for all sums
which the Insured shall become legally obligated to pay as compensation for loss of and/or damage to and/or destruction of property and/or Loss of the Use thereof.

However, clause 3(b) of Section C provided:

This Section shall not apply to liability:

... for damage to property owned by the Insured.

The insurers argued that the expression 'the Insured' when used in this exclusion is to be construed as meaning all of the insured under the Policy or, alternatively, it should be construed as meaning:

• the 'contracting insured'; or
• all of the insured other than the one making the claim under the Policy.

The question to be determined was whether this exclusion operated so as that a party, which is insured under the Policy, and which causes damage to the property of another party, which is also insured under the Policy, cannot seek indemnity under the Policy.

Key Findings

The Court found that Section C provides that the insurer will pay all sums which the Insured shall become legally obligated to pay in the relevant circumstances. The Insured in this context must be a reference to the party which has the obligations to make the payment and will be the party which makes the claim. The exclusion clause can only operate in relation to that claim and it follows that the Insured referred to in clause 3 must be the party making the claim.

In reaching this decision, it appears that the Court was influenced by the fact that the Policy contained a 'cross liability clause' which rendered each party as a separate entity 'in the same manner as if a separate policy had been issued to each of them'.

The Court noted that for the exclusion to operate as suggested by the insurers, it would have had to read either 'any Insured' or 'an Insured' rather than 'the Insured'.

(b) Chalmers Leask Underwriting Agencies v Mayne Nickless Limited

(1983) 155 CLR 279, High Court of Australia

Relevant to this paper, this case considers the ambit of an exclusion clause in respect of loss or damage directly caused by defective workmanship, material or design.

Key Facts

Mayne Nickless Limited (Mayne Nickless) entered into a Contract to carry out drainage flood mitigation. To protect construction works it erected a coffer dam, the top of which served as a haulage road. Heavy vehicles on that road created a depression through which flood waters penetrated, scouring the dam and damaging the construction works. Mayne Nickless had a policy of insurance, issued by Chalmers Leask Underwriting Agencies (Chalmers Leask), covering the
construction works against various risks, including flooding, but containing an exclusion clause in respect of ‘loss or damage directly caused by defective workmanship, material or design’. The clause was ‘limited to the part immediately affected and shall not apply to any other part or parts lost or damaged in consequence thereof’. Mayne Nickless made a claim under the policy for damage to the works other than the damage to the dam itself. Chalmers Leask resisted the claim by arguing the loss and damage had been ‘directly caused by defective workmanship ... or design’ in the dam.

Hunt J in the Supreme Court of New South Wales held that there had been no relevant defective workmanship or design. The Court of Appeal (Hutley and Mahoney JJA, Glass JA dissenting) dismissed an appeal.

Chalmers Leask appealed to the High Court and Mayne Nickless for the first time relied upon the limiting provision in the exclusion clause.

**Key Findings**

Brennan and Deane JJ delivered a joint judgment concerning the ambit of the exclusion clause. The remaining members of the Court agreed with this joint judgment.

The exclusion clause stated:

This insurance does not cover:

... 

(iii) loss or damage directly caused by defective workmanship, material or design or wear and tear, or mechanical breakdown or normal upkeep or normal making good but so that this exclusion shall be limited to the part immediately affected and shall not apply to any other part or parts lost or damaged in consequence thereof;

...

The loss and damage that was in dispute was not the damage in respect of the coffer bank itself, but rather the loss and damage caused by the flooding waters which scoured the construction works and deposited soil and other debris in the area of the construction works. Chalmers Leask claimed that this relevant loss and damage was directly caused by defective workmanship or design. They argued that the exclusion of the loss or damage described in the exclusion clause should be viewed as being 3 independent exclusions of different types of loss or damage distinguished by reference to the cause. That is, they argued that the 3 causes of damage namely, (1) loss or damage directly caused by defective workmanship, material or design, (2) loss or damage caused directly by wear and tear, and (3) loss or damage caused by mechanical breakdown, normal upkeep or normal making good, should be treated independently as a result of the punctuation of the clause. The presence of the comma after the word 'tear' and the absence of a comma after the words 'making good' were argued to support a construction of the limiting provision confine it to loss or damage caused by the third of those groupings of causes. As such, Chalmers Leask argued that the words 'this exclusion shall be limited to the part immediately affected and shall not apply to
any other part or parts lost or damaged in consequence thereof' only applied to loss or damage caused by 'mechanical breakdown or normal upkeep or normal making good'.

Brennan and Deane JJ rejected this argument. Their Honours held that the phrase 'this exclusion' could not properly be construed as referring to one or other of the possible causes of an exclusion. Their Honours held that it referred to the exclusion itself, that is to say, it referred to the single overall exclusion of loss or damage of the type described in the clause.

Therefore, their Honours held that the limitation provision limited the exclusion to the part immediately affected which comprised the whole of the coffer bank itself, and not loss or damage to the construction works below the coffer dam that were caused by the flooding waters.

(c) **Cementation Piling & Foundations Ltd v Aegon Insurance Company Ltd and Commercial Union Insurance Company PLC**

[1995] 1 Lloyd's Rep 97, English Court of Appeal

This case again examines the application of an exclusion clause for 'defects in design, materials or workmanship' to a construction-related claim. The judgment of the English Court of Appeal provides a useful insight into the general approach courts take to interpreting exclusion clauses in insurance policies.

**Key Facts**

Cementation Piling & Foundations Ltd (Cementation) entered into a subcontract with Sir Alfred McAlpine & Sons Ltd to complete and maintain board piles and continuous diaphragm walls forming part of a series of quays to be constructed within an existing dock. The area had been reclaimed from the sea by depositing pumped sand to form a land area, or berm protruding 2.5 metres above sea level. The diaphragm walls were designed and constructed to retain the sand. Due to the method of construction of diaphragm walls, joints existed between the individual sections of the wall. Side panels were cast at the joints between the sections in such a shape as to enable the next panel to abut and provide a tight fit behind the wall in the finished dock. Upon completion of the walls the sand in the centre of the structure was dredged and seawater was permitted to enter and take its place.

In September 1985 it was discovered that quantities of sand which had been retained by the walls had escaped into the newly constructed dock. On inspection of the concrete panels it was discovered that in a number of places there were gaps and voids between adjacent panels which had permitted sand to escape. Cementation carried out works to remedy these matters. It was accepted by the parties that the need for these works arose from defects in design, materials and workmanship.

The losses suffered by Cementation fell into 3 distinct areas:

1. rectification of the gaps and/or voids in the walls;
2. removal of the sand fill from the dock bed; and
3. grouting and filling **behind** the walls of the voids from which the sandfill had escaped.

Items 2 and 3 were paid for by the insurance company under its policy on the basis that those items constituted damage to the dock and berm respectively. The issue for decision before the Judge of the High Court, and on appeal before the Court of Appeal, was whether item 1 was covered by the insurance policy.

The relevant section of the insurance policy stated:

**Interest:**

**Section 1**

The permanent and temporary works, materials, construction or plant, tools, equipment, temporary buildings ... and other things used or for use in connection with the project, the insured's own or for which they are responsible.

The policy continued:

**Section 1: Material Damage**

The insurers will indemnify the insured for an amount not exceeding the limit of indemnity in respect of physical loss of or damage to the property insured howsoever caused ... and arising from any cause whatsoever except as hereinafter mentioned ...

**Exceptions to section 1:**

The insurers shall not be liable in respect of: ...

(2) the cost of replacing or rectifying defects in design, materials or workmanship unless the property insured suffers actual loss, destruction or damage as a result of such defect. However, additional costs of introducing improvements, betterments or corrections in the rectification of the design, material or workmanship causing such loss or damage shall always be excluded.

**Key Findings**

The defendant insurers argued that the relevant peril insured against is damaged property. They argued that there must be a clear cause and effect relationship between the peril and the loss. That is, the loss must be caused by the damaged property. In this situation, the loss or expenditure caused by the damaged property was the removal of the sand from the dock bed and the grouting and filling behind the walls of the voids from which the sand fill had escaped. The damaged property did not cause the loss or expenditure in respect of rectification of the gaps and/or voids in the walls. They argued that it was the defect which caused the damage to the property and the resulting loss. As the wall was defective from the outset the insurers argued that there was no damage to it. They also argued that the provisions in exception 2 were consistent with their arguments relating to the interpretation of the insuring clause, in that the language of the exception makes it clear that what is recoverable under the policy is loss resulting from damage caused and not defects.
Sir Ralph Gibson, with whom Lord Justices Waite and Russell agreed, found the insurers' arguments strong, but nevertheless dismissed the appeal. His Lordship stated that the extent of the indemnity which Cementation could claim was controlled by the words of the policy properly construed, and that the principles of construction which the Court must apply are those applicable to any commercial document including the principle that the document shall be construed by reference to all that it contains.

His Lordship found it difficult to conclude that the cost of the rectification of the gaps and void in the wall would be recoverable by Cementation in the absence of exception 2. This followed from the wording of the indemnity being 'in respect of physical damage to the property howsoever caused'. His Lordship stated that the relevant principal was that the insured suffered loss arising from the loss of or physical damage to the property insured, and was entitled to indemnity in respect of that loss. His Lordship thought it possible to regard the cost of rectifying a defect which caused the physical damage as the cost incurred 'in respect of physical damage', notwithstanding that the defect is not itself physical damage, and that therefore the indemnity would not extend to the cost of rectifying that defect save for its connection with the physical damage. However, His Lordship also stated that it would be possible to come to the opposite conclusion.

His Lordship resolved this conflict between the two alternative constructions by reference to exception 2. He stated that it was common ground that an exception clause cannot extend the cover from which the exception is made. However, it is also common ground that the terms of an exception clause may provide material from which the Court can discern that the first possible meaning of the indemnity clause is to be preferred to another possible meaning. In such a case the wording of the whole policy shows that the contractual intention of the parties must be regarded as contained in the first possible meaning. As such, His Lordship used exception 2 to provide a context in which the meaning and extent of the words 'in respect of physical damage to the property insured' could be construed. His Lordship came to this conclusion for two reasons.

1. Exception 2 begins with the statement that:

   ... the insurers shall not be liable in respect of the cost of replacing or rectifying defects in design materials or workmanship unless the property insured suffers actual loss, destruction or damage as a result of such defect.

   His Lordship held that to argue that the insurers shall not be liable for certain costs unless a certain event has happened created a clear inference that if that event has happened the insurers are liable.

2. His Lordship also held that the additional words in exception 2, which refer to additional costs of introducing improvements, betterments or corrections in the rectification, necessarily imply that there are other costs of rectification, being the costs involved in rectifying without such improvements, which are recovered.
Therefore His Lordship held that the construction of exception 2 provided a comprehensive and conclusive answer to the argument in relation to the construction of the policy. Therefore, the appeal was dismissed and the insurers were liable to pay for the cost of rectifying the voids in the wall.

(d) **Graham Evans & Co (Qld) Pty Ltd v Vanguard Insurance Co Ltd**
(1986) 4ANZ Insurance Cases 60-689, NSWSC (20 December 1985)

This case examines the scope of the insuring clause, in particular, whether a coat of paint could be 'property' capable of being the subject of insurance. In addition, this case also reviews whether loss or damage was 'directly caused' by defective workmanship, construction or design.

**Key Facts**

Graham Evans & Co (Qld) Pty Ltd (Evans) was contracted to paint the exterior surfaces of a 26 storey block of units. Evans subcontracted the painting to Amalgamated Painting Services Limited which used the Blue Circle system to paint the building. This system involved the application of 3 distinct coats of paint. The first coat was a cement based primer intended to be applied to, and to some degree bond with, the concrete surface of the exterior walls. The second coat was intended to bond to the previous primer coat and provide a textured surface for the application of the finishing coat. The third coat was applied on top of the second and was intended to provide a rough or rippled external surface. The paint manufacturer also supplied a specification as to the manner in which the components of the paints were to be mixed and applied.

Amalgamated Painting commenced work in February/March 1983 and by November 1983 they had painted a substantial part of the outside of the building. About that time, however, the paintwork began to flake off in many areas of the building and Evans had to strip a considerable amount of the paintwork with a view to large areas being repainted.

On the evidence, it appeared that the primary cause of the failure of the exterior paintwork lay in the primer. The problem with the first coat appeared to be that it had been applied in too dilute a form to perform its required function as a primer.

As a result of the failure of the paintwork, Evans claimed under a policy of insurance issued by several insurance companies who were defendants in this case. The policy provided cover:

in respect of occurrences ... against all risks of physical loss of or damage to property of every kind and description ... owned by the insured or for which the insured may be responsible ... used or to be used in part of or incidental to the 'insured's contracting operators' ...

The defendants denied that the loss suffered by Evans fell within the cover provided by the insurance policy. Furthermore they argued that if it did, then they could rely on a provision of the policy excluding 'loss or damage directly caused by defective workmanship, construction or design', although it was provided that the
exclusion 'shall be limited to the part which is defective and shall not apply to any other part or parts lost damaged in consequence thereof'.

Two issues were raised before the Court:

- the Court needed to consider whether the policy covered the loss or damage claimed; and
- the Court needed to consider that if the policy did cover the loss or damage claimed, whether the exclusion clause applied.

Key Findings

Did the Policy cover the loss or damage claimed?

The defendant insurers sought to argue that in order for the policy to apply, loss or damage to property must be demonstrated. They contended that it was artificial to consider a coat of paint as constituting property within the meaning of the insuring clause. The defendants accepted that a tin of paint would be a chattel capable of ownership as such, but that once the material had been applied to the building it merges with the building and no longer can be described in any particular sense as an individual item of property capable of being the subject of insurance.

Foster J rejected this argument. His Honour considered the insurance policy as a commercial document to be construed beneficially. Furthermore the phrase 'property of every kind and description' is very wide and must be read with the words 'for which the insured may be responsible ...'.

Foster J held that Evans was clearly responsible for the application of the coats of paint to the building. Those coats were applied separately and their application involved the use of different materials labour in each case. Therefore, each coat was separate and severable. Therefore His Honour came to the conclusion that the coats of paint would come within the description of being 'property of every kind and description ... for which the insured may be responsible'. As such His Honour accepted Evans' submission that the rendering useless and valueless of the second and third coats of paint, and their necessary physical stripping from the building, constituted physical loss or damage to those coats considered as property.

Does the Exclusion Clause Apply?

Foster J noted that the exclusion clause contained within the policy under consideration was very similar to the one considered by the High Court in Chalmers Leask Underwriting Agencies v Mayne Nickless Limited (1983) 155 CLR 279.

The exclusion clause in the policy under consideration read:

2(c) Loss or damage directly caused by defective workmanship, construction or design or wear and tear, or mechanical breakdown or normal upkeep or normal making good but this exclusion shall be limited to the part which is defective and shall not apply to any other part or parts lost or damaged in consequence thereof;
This clause is different to the one considered by the High Court in *Chalmers Leask* in that it refers to 'part which is defective' as against the phrase in *Chalmers Leask* of 'the part immediately affected'.

Foster J felt it necessary to consider the meaning and application of the words 'directly caused', something that the High Court in *Chalmers Leask* was not required to do.

His Honour concluded that the evidence showed that the primer coat was applied in a defective manner, and that this coat suffered damage by losing both adhesion and cohesion so that it ceased to function as a primer. Therefore His Honour concluded that the damage directly caused by defective workmanship was caused to the primer coat.

Therefore, Foster J concluded that the exclusion clause did not apply to the loss or damage to the second or third coats, as their failure was not directly caused by the defective workmanship.

Therefore, Foster J held in favour of Evans that the insurance policy covered the loss or damage resulting from the failure of the second and third coats of paint.

**Graham Evans & Co (Qld) Pty Ltd v Vanguard Insurance Co Ltd**  
(1987) 4 ANZ Insurance Cases 60-772, Supreme Court of Queensland, 3 March 1987

This case examines the application of the insuring clause of a policy in the context of a building construction claim arising from the incorrect laying out of grids for the location and identification of the elements of the building. In particular, the case considers the interpretation to be given to the words 'occurrence', 'loss' and 'damage' as found in the insuring clause.

**Key Facts**

Graham Evans & Co (Qld) Pty Ltd (*Evans*) was contracted to construct a building. It retained a surveyor to lay out the grids on the site to be used for the location and identification of the elements of the building. By the time the building had been constructed to the 5th level, however, it contained a number of significant errors relating to the setting out of the grids. As a result, the building was 'skewed' with columns, internal walls and lift shafts being wrongly located. Evans sought indemnity under a policy of insurance with the defendant Vanguard Insurance Company Limited (*Vanguard*).

**Key Findings**

*Did the policy cover the loss or damage claimed?*

The insurance policy indemnified Evans' business in building construction and was set out in the following terms:

This section, subject to the limitations, exclusions, terms and conditions hereinafter mentioned, is to insure, in respect of occurrences happening during the period stated in the schedule against all risks or physical loss of or damage to property of every kind and description (including the whole of the contract plant, equipment, materials and supplies up to but not exceeding the respective sums insured in the
schedule) owned by the insured or for which the insured may be responsible or, prior to any occurrence for which a claim may be made hereunder, assumed responsibility, used or to be used in part of or incidental to the ’insured's contracting operations’ detailed in the schedule ...

Dowsett J divided this clause into 4 parts namely:

1. that the loss must be in respect of occurrences happening during the period stated in the schedule;
2. that the loss must be physical loss of or damage to property;
3. that the property is owned by the insured or is property for which the insured may be responsible or for which he has assumed responsibility prior to the loss; and
4. that it is property used or to be used in part of or incidental to the insured's contracting and operations.

Dowsett J considered each of the above points in turn.

1. The policy defined the term 'occurrence' as:
   ‘... an event, or continuous or repeated exposure to conditions, which during the policy period, unexpectedly or unintentionally caused –
   (i) bodily injury or illness ...;
   (ii) loss of or damage to or destruction of property or the loss of use thereof;
   provided the insured didn't intend that such injury or loss would result ...

   As a result of this definition, His Honour had difficulty identifying the relevant occurrence. His Honour stated that it may be either the defective laying out of the building, or the construction of the building in accordance with the defective laying out, or the subsequent partial destruction of the building to rectify the defects.

2. Dowsett J's interpretation of the second point was crucial to his decision, in that the policy required physical loss of/or damage to property. His Honour held that 'loss' implied possession of property followed by a loss of possession, usually in circumstances which cannot be explained or certainly in circumstances which cannot be rectified. In addition, His Honour held that 'damage' to property involves some injury to the property. As such His Honour had difficulty in identifying any loss or damage to property as a result of the building being incorrectly set out. Furthermore, even if one were able to identify loss or damage to property, the occurrence that caused such loss or damage could hardly be unintentional in the sense required by the definition of the term 'occurrence' as it was actually brought about deliberately.

3. Dowsett J held that the builder was not responsible for the property in the building notwithstanding that it was responsible for the construction of the building.
4. Dowsett J also had difficulty in finding that the property was to be used in part of or incidental to the insured's contracting operations. If the property concerned is the building, the building was not to be used as part of or incidental to the insured's contracting operations.

Therefore, His Honour found that the policy did not cover the builder for the incorrect setting out of the building by the surveyor. As a result it was not necessary for Dowsett J to consider the exclusion clause.

7.2 Insurance clauses in project contracts

The following cases provide an example of some recent disputes which may arose in connection with contractual obligations to take out certain insurances.

(a) North Goonyella Coal Mines Pty Ltd & Ors v North Goonyella Coal Properties Pty Ltd & Anor

[2002] QSC 368

This case provides an example of the importance for a party of ensuring that insurance cover is available on acceptable terms when it is negotiating insurance clauses in a construction contract.

Key Facts

This matter concerned a dispute in relation to a mine operations contract. While the decision ultimately related to whether the dispute could be heard by the Court or whether it had to be referred to arbitration, it also considered a clause in the mine operations contract which purported to deal with the situation where the Principal was unable to effect or maintain the insurances required under the contract.

Clause 20.3 of the contract relevantly provided:

Unavailability of Insurance

If the Principal is unable to effect or maintain the insurances required [by Schedule 6 to the Contract], the Principal must:

(a) immediately notify the Contractor; and

(b) use or continue to use its best endeavours to effect or maintain the relevant insurances in accordance with the Contract; and

(c) immediately suspend the performance of the work under the Contract.

If there is a suspension of the work under the Contract...then, for the period of that suspension, the Contractor will be relieved of the performance of the work under the Contract...

Under Schedule 6 of the contract, the Principal was required to 'use its best endeavours to effect and maintain' insurance which in specific respects (eg the extent of cover for certain items and the amount of deductibles) is on terms not less favourable than a policy which was annexed to the contract.

On 10 November 2000, the parties entered into the contract. There had previously been in place an insurance policy, effective up to 20 September 2000, which was
annexed to the contract. A new insurance policy, effective from 20 September 2000, was already in operation at the time the contract was entered. However, it appears that at the time the contract was negotiated and executed, no copy of the current policy was available. Consequently, the policy for the preceding year was used as the annexure.

It was not until September 2001 that the question of any diminution in benefit from the policy's terms became the subject of discussion.

**Key Findings**

Ultimately, the Court agreed with the Principal that this was a matter which should be referred to arbitration in accordance with the contract.

While it was not necessary for the Court to make a decision on the insurance obligations in the contract, the Court did comment that the operation of clause 20.3 was not dependant on whether the Principal has made its best endeavours, but rather whether it has as a matter of fact been able to 'effect or maintain the insurances required by' the contract. This was because clause 20.3 creates an obligation in a specified circumstance ie the inability to effect or maintain the required insurance.

(1) Thiess Contractors Pty Ltd v Norcon Pty Ltd

(2001) 11 ANZ Ins Cas 61-509
Supreme Court of Western Australia, Full Court

In this case, the Court considered the following issues:

- Where a plaintiff suffers loss as a result of a defendant's negligence, but is the beneficiary of an insurance policy covering that loss, should the sum received by the plaintiff from the insurer be taken into account in awarding damages?

- When considering whether a party has lost a contractual benefit in relation to a proposed insurance policy, is it relevant to consider whether that party had insurance covering the same loss that would have been covered by that proposed policy?

**Key Facts**

A worker on a construction site injured his spine when he tripped over a piece of uncapped reinforcing steel at a construction site. He commenced proceedings against his employer, claiming damages for negligence. Thiess Contractors Pty Ltd (*Thiess*) was the occupier of the construction site and the main contractor. Norcon Pty Ltd (*Norcon*) was one of Thiess' subcontractors. Both Thiess and Norcon were joined as defendants to the action. The worker alleged that Thiess was negligent in failing to cap the reinforcing steel or to warn workers that it was uncapped. Norcon was responsible for the installation of the reinforcing steel and the worker alleged that it was also negligent.

Thiess issued a contribution notice against Norcon alleging that it was a term of the subcontract that Norcon would, at its own expense, 'procure and maintain' an
insurance policy 'covering liability in respect of ... personal injury to any person ... where the injury arises out of or is caused by the execution of the subcontract works'. Thiess alleged that Norcon was in breach of that term in failing to procure that policy. Norcon denied that it was liable in respect of the damage suffered by the plaintiff.

Thiess had in fact taken out its own public liability policy of insurance which was wide enough to cover the claim brought by the worker, however, Thiess contended that this was irrelevant to its claim against Norcon. Norcon argued in paragraph 5 of its defence that because Thiess had taken out its own public liability insurance policy which covered the injury, Thiess did not suffer any loss or liability through Norcon breaching its obligations to procure its own public liability policy.

Thiess argued that Norcon's paragraph 5 did not disclose an arguable defence, an argument that the Deputy Registrar upheld in striking out this paragraph of the Defence.

Norcon appealed to the District Court, arguing that paragraph 5 should have been found to disclose an arguable defence because Thiess, being entitled to indemnity under its policy, had not suffered any loss and could not also have obtained indemnity under the proposed policy, even if Norcon had taken out the policy. That being so, Norcon's failure to take out the proposed policy had no consequence. The District Court Judge upheld Norcon's appeal. Thiess appealed to the Western Australian Supreme Court contending that the District Court Judge erred in holding that paragraph 5 of Norcon's defence disclosed an arguable defence.

Key Findings

The leading judgment was delivered by Steytler J, with whom Murray and Templeman JJ agreed.

Is the amount received by a party under an insurance policy relevant in the calculation of damages?

Steytler J held that where a plaintiff suffers loss as a result of a defendant's negligence, but is the beneficiary of an insurance policy covering that loss, the sum received by the plaintiff from the insurer is not taken into account in a reduction of the damages. This principle follows from cases such as Bradburn v The Great Western Railway Company (1874) LR 10 Exch 1 which was adopted by the New South Wales Court of Appeal in RG&PJ Anderson Pty Ltd v Chamberlain John Deere Pty Ltd (1989) Australian Torts Reports 80-240.

Does the existence of an insurance policy mean that a party does not suffer loss as a result of another party breaching its contractual obligation to obtain insurance?

Steytler J also held that cases such as Western Sydney Regional Organisation of Councils Group Apprentices v Statrona Pty Ltd (2002) 12 ANZ Ins Cas 61-530 and Besselink Bros Pty Ltd v Citra Constructions Pty Ltd (unreported, Federal Court of Australia, 31 October 1984) supported the proposition that it is irrelevant whether a party is able to claim indemnity from its own insurer in respect of its liability to the plaintiff in considering whether that party had suffered loss through another party
failing to obtain the insurance required of it under a contract. As such His Honour held that the defence sought by Norcon in its paragraph 5 could not be supported. His Honour held that it was irrelevant that Thiess may be able to recover or avoid any expenses which would otherwise have followed from the loss of the benefit of the proposed policy by resort to a policy which it has in fact taken out. The fact is that Thiess lost the benefit of the policy proposed under its contract with Norcon.

As such the appeal was allowed and the Court ordered that paragraph 5 of Norcon's defence be struck out.
Annexure 1 – Insurance-related provisions extracted from major construction project
54. Insurance

54.1 Insurances Until End of Defects Liability Period

(a) Subject to Clause 54.1(c), the Concessionaire must, at its own cost and expense, effect and maintain or cause to be effected and maintained from the Commencement Date until the end of the period in Clause 54.1(b)(i) or Clause 54.1(b)(ii) (as applicable) with insurers approved by the [ ] acting reasonably or the following insurances on the terms set out in this Clause 54:

(i) a professional indemnity policy in the name of the Construction Contractor for an amount of not less than $[ ] per occurrence covering, among other things, claims by the [ ] or by any other person arising out of or incidental to any negligent act or omission or for any breach of duty owed by the Concessionaire or a Sub-Contractor or consultant engaged by or on behalf of the Concessionaire in connection with their professional activities and duties with respect to the Project and, without limitation, which covers claims made under the Trade Practices Act 1974 (Cth). The Concessionaire must ensure that those of its Sub-Contractors carrying out design in relation to the Project are similarly insured to the reasonable satisfaction of the [ ];

(ii) employers’ liability and workers’ compensation insurance (including common law liability) as required under applicable Law. The Concessionaire must ensure that each of its Sub-Contractors and consultants effect and maintain equivalent such insurance in respect of any period during which they provide services in relation to the Project. To the extent permitted by Law, such insurance policy or policies must be extended to indemnify the [ ] for its statutory liability to persons employed by the Concessionaire, its Sub-Contractors and consultants;

(iii) motor vehicle insurance as required under applicable Law in respect of all vehicles used in or in connection with the undertaking of the Facility Works and third party property damage and injury to persons liability insurance in respect of all vehicles used in or in connection with the undertaking of the Facility Works and for an amount of not less than $[ ] per occurrence for third party property damage and for amounts not less than required by statute for injury to persons. The Concessionaire must ensure that each of its Sub-Contractors and consultants effect and maintain equivalent such insurance in respect of any period during which they provide services in relation to the Project;

(iv) a policy of insurance in respect of such of the Licensed Area (if any) as is not the subject of contract works insurance covering the Facility Works and contract works insurance covering the Facility Works, on a full reinstatement basis (including all consultants’ fees and costs of removal of debris from the Site) for an amount not less than $[ ]; and
(v) public/products liability insurance for an amount not less than $[ ] for any one occurrence and in the aggregate in respect of products liability, which indemnifies the [ ], the Concessionaire and its Sub-Contractors for their respective rights, interests and liabilities in respect of all Liability at Law for any damage or loss occurring to any property and for injury (including death) to any person arising out of any thing done or omitted to be done in the execution or purported execution by any such party of its rights or obligations under this Agreement or any other Project Agreement and against all Claims in connection with each of them.

(b) The Concessionaire must maintain or cause to be maintained the insurances referred to in Clause 54.1(a) until:

(i) in the case of insurance under Clause 54.1(a)(i), 6 years after the end of the Defects Liability Period; and

(ii) in the case of all other insurances under Clause 54.1(a), the end of the Defects Liability Period.

(c) The [ ] must, at the request and at the cost and expense of the Concessionaire, effect and maintain or cause to be effected and maintained with the [ ] the insurances required under Clauses 54.1(a)(iv) and (v) on the same terms set out in this Clause 54.

(d) During the period of 45 days after the Commencement Date (the Interim Period), the Concessionaire will be taken to be complying with Clause 54.1(a)(iv) if it ensures that during the Interim Period the Construction Contractor maintains temporary insurance cover for the purposes of Clause 54.1(a)(iv) for an amount of not less than $[ ] in accordance with the Construction Contractor’s insurance policy with [ ], details of which were provided in writing to the [ ].

(e) The Concessionaire must ensure that it or the Construction Contractor effects the insurance required under Clause 54.1(a)(iv) on or before the expiry of the Interim Period.

(f) The [ ] will not cancel any insurance policy which it holds with [ ] in accordance with Clause 54.1(c) without first consulting with the Concessionaire and the [ ] will use its reasonable endeavours to have the interests of the Concessionaire and the Construction Contractor noted on such policy.

54.2 Insurance After the End of the Defects Liability Period

Subject to Clause 54.2A, the Concessionaire must, at its own cost and expense, effect and maintain or cause to be effected and maintained, from the end of the Defects Liability Period until the end of the Contract Term, the following insurances with insurers approved by the [ ] (acting reasonably) on the terms set out in this Clause 54:

(a) employers’ liability and workers’ compensation insurance (including common law liability) as required under any applicable Law. The Concessionaire must ensure that each of its Sub-Contractors and consultants effect and maintain equivalent such insurance in respect of any period during which they provide services in
relation to the Project. To the extent permitted by Law, such insurance policy or policies must be extended to indemnify [ ] for its statutory liability to persons employed by the Concessionaire, its Sub-Contractors and consultants;

(b) motor vehicle insurance as required under applicable Law in respect of all vehicles used in or in connection with the operating and maintaining of the Facility or performing the Services and third party property damage and injury to persons liability insurance in respect of all vehicles used in or in connection with the operating and maintaining of the Facility or performing the Services and for an amount of not less than $[ ] per occurrence for third party property damage and for amounts not less than required by statute for injury to persons (as adjusted in accordance with Clause 54.11). The Concessionaire must ensure that each of its Sub-Contractors and consultants effect and maintain equivalent such insurance in respect of any period during which they provide services in relation to the Project;

(c) public/product liability insurance for an amount of not less than $[ ] for any one occurrence and in the aggregate in respect of products liability (adjusted in accordance with Clause 54.11) which indemnifies the [ ], the Concessionaire and its Sub-Contractors for their respective rights, interests and liabilities in respect of all Liability at Law for any damage or loss occurring to any property and for injury (including death) to any person arising out of any thing done or omitted to be done in the execution or purported execution by any such party of its rights or obligations under this Agreement or any other Project Agreement and against all Claims in connection with each of them; and

(d) industrial special risks insurance in respect of the Facility (including plant and all other items comprising the Facility, such as computer and other systems) and the Lease Land:

(i) for an amount not less than the greater of:

(A) the full cost of reinstatement at the time of reinstatement (including all consultants’ fees and costs of removal of debris from the Site); and  

(B) $[ ] (Indexed);

(ii) including business interruption insurances for an amount not less than the Capital Cost Component of the Adjusted Core Services Payment for 40 months.
54.2A Changes in Insurance

(a) Not less than 90 Business Days prior to the Operations Commencement Date, the Concessionaire must, in accordance with the Insurance Principles, obtain separate quotations from 3 reputable insurance brokers in the commercial insurance market at that time, with respect to the annual premium costs of obtaining the insurances referred to in Clauses 54.2(c) and (d) for the first year of the Operating Phase on the terms and conditions set out in Clauses 54.2 to 54.11 (as applicable) (the **Relevant Insurances**).

(b) The Concessionaire must:

(i) not less than 60 Business Days prior to the Operations Commencement Date, provide the [ ] with copies of each of the quotations referred to in Clause 54.2A(a), together with such documentation or information as the [ ] reasonably requires to confirm the Concessionaire’s compliance with Clause 54.2A(a) in obtaining those quotations; and

(ii) at the same time as the copies of the quotations referred to in paragraph (i) are provided to the [ ], notify the [ ] in writing of the Concessionaire’s proposal with respect to obtaining the Relevant Insurances, including details of the Concessionaire’s preferred quotation and insurance broker (the **Concessionaire’s Notice**).

(c) Within 10 Business Days after the [ ]’s receipt of the Concessionaire’s Notice, the [ ] and the Concessionaire must meet to discuss the proposal set out in the Concessionaire’s Notice.

(d) Within the period from the date of the meeting referred to in Clause 54.2A(c) to the date which is 10 Business Days after the date of that meeting, the [ ] and the Concessionaire must use their best endeavours to agree on the approach to and the cost of obtaining the Relevant Insurances.

(e) If the [ ] and the Concessionaire fail to reach agreement on the matters referred to in Clause 54.2A(d) within 10 Business Days after the date of the meeting referred to in Clause 54.2A(c), the [ ] and the Concessionaire must refer the matters in dispute to an independent expert for resolution in accordance with Clause 55.2. If the matter is so referred, the [ ] and the Concessionaire must request the independent expert to make a determination by the date which is not less than 20 Business Days prior to the Operations Commencement Date.

(f) The annual premium cost of obtaining the Relevant Insurances as agreed in accordance with Clause 54.2A(d) or determined in accordance with Clause 54.2A(e) (as the case may be) divided by 4 (the **Insurance Cost Component**) will apply with effect from the Operations Commencement Date until such time as the Insurance Cost Component is otherwise in accordance with Clause 54.2A(l) or Clause 54.2A(q).

(g) The Concessionaire must effect the Relevant Insurances as agreed in accordance with Clause 54.2A(d) or determined in accordance with Clause 54.2A(e) (as the
case may be), and unless otherwise agreed in accordance with Clause 54.2 to 54.11 (each inclusive), with effect from the Operations Commencement Date.

(h) At any time during the Operating Phase either party may seek to demonstrate to the other party by way of written submission to that other party that:

(i) with respect to a particular Quarter, the annual premium cost of obtaining the Relevant Insurances divided by 4 is at least 30% greater or less than the Insurance Cost Component (Indexed) for that same Quarter as last determined in accordance with this Clause 54.2A;

provided that:

(ii) any increase or decrease in the cost of obtaining Relevant Insurances which is attributable to the Concessionaire's performance under the Project Agreements or the insurance history (or other relevant acts or omissions of) the Concessionaire, the Operator or the Maintenance Contractor under or in relation to any existing or previous insurance policy will be disregarded for the purposes of paragraph (i),

(the Insurance Cost Submission).

(i) Within 10 Business Days after the receipt by a party (the receiving party) of an Insurance Cost Submission from the other party (the submitting party), the receiving party must, by notice in writing to the submitting party, either:

(i) accept the submitting party’s Insurance Cost Submission; or

(ii) reject the submitting party’s Insurance Cost Submission on the basis that the receiving party disagrees with the submitting party’s assessment of one or more matters referred to in paragraphs (i) and (ii) of Clause 52.2A(h),

(the receiving party’s Notice).

(j) [Not used]

(k) If the receiving party rejects the submitting party’s Insurance Cost Submission in accordance with Clause 54.2A(i), the submitting party may refer the matters in dispute to an independent expert for resolution in accordance with Clause 55.2.

(l) The amount of the Insurance Cost Component as at the date of the receiving party’s Notice accepting the submitting party’s Insurance Cost Submission or as at the date a determination is made by the independent expert under Clause 54.2A(k) (as the case may be), will be adjusted in accordance with the submitting party’s Insurance Cost Submission accepted by the receiving party or as determined by the independent expert (as the case may be) and that adjusted quarterly Insurance Cost Component will be the Insurance Cost Component applicable from the commencement of the next Quarter after the date of the receiving party’s Notice or the date of the independent expert’s determination (as the case may be) until such time as the Insurance Cost Component is otherwise adjusted in accordance with this Clause 54.2A(l) or Clause 54.2A(q).

(m) At any time during the Operating Phase the Concessionaire may seek to demonstrate to the [ ] by way of a written submission to the [ ] that:
(i) any Relevant Insurance is not available to the Concessionaire on commercially reasonable terms in the commercial insurance market existing at that time; and

(ii) the unavailability of the Relevant Insurance as referred to in paragraph (i) is attributable to factors other than the Concessionaire’s performance under the Project Agreements or the insurance history (or other relevant acts or omissions of) the Concessionaire, the Operator or the Maintenance Contractor under or in relation to any existing or previous insurance policy, (the **Concessionaire’s Insurance Type Submission**).

(n) Within 10 Business Days after the receipt by the [ ] of the Concessionaire’s Insurance Type Submission, the [ ] must, by notice in writing to the Concessionaire, either:

(i) accept the Concessionaire’s Insurance Type Submission; or

(ii) reject the Concessionaire’s Insurance Type Submission on the basis that the [ ] is not reasonably satisfied of one or more matters referred to in paragraphs (i) and (ii) of Clause 54.2A(m), (the **[ ]’s Notice**).

(o) If the [ ] accepts the Concessionaire’s Insurance Type Submission in accordance with Clause 54.2A(n), the [ ] and the Concessionaire must meet within 5 Business Days after the date of the [ ]’s Notice to seek to agree:

(i) the amount of any change to the quarterly Insurance Cost Component resulting from the matters set out in the Concessionaire's Insurance Type Submission; and

(ii) any other changes to the Concessionaire’s rights and obligations under this Agreement arising out of the unavailability of the Relevant Insurances the subject of the Concessionaire’s Insurance Type Submission including, if a risk event (other than a risk event to which Clause 53.3 applies) occurs that but for Clause 54.2A(m) would be covered by any Relevant Insurance, provision for the payment to the Concessionaire of amounts representing the insurance proceeds that would have been payable to the Concessionaire but for the unavailability of such insurance, taking into account the Insurance Principles.

(p) If:

(i) the [ ] rejects the Concessionaire’s Insurance Type Submission in accordance with Clause 54.2A(n); or

(ii) the [ ] and the Concessionaire fail to reach agreement on the matters referred to in Clause 54.2(o) within 20 Business Days after the date of the meeting referred to in Clause 54.2(o),

either the [ ] or the Concessionaire may refer the matters in dispute to an independent expert for resolution in accordance with Clause 55.2.
(q) The amount of the quarterly Insurance Cost Component as at the date agreement is reached under Clause 54.2A(o) or a determination is made under Clause 54.2A(p) (as the case may be) will be adjusted to reflect the amount of any change to the quarterly Insurance Cost Component so agreed or determined (as the case may be) and that adjusted Insurance Cost Component will be the Insurance Cost Component applicable from the commencement of the next Quarter after the date of such agreement or determination (as the case may be) until such time as the Insurance Cost Component is otherwise adjusted in accordance with this Clause 54.2A(q) or Clause 54.2A(l).

54.3 Proof of Insurance

(a) The Concessionaire must, whenever reasonably requested in writing by the [ ], provide evidence to the [ ] of the insurances effected and maintained by the Concessionaire under Clause 54.1 and Clause 54.2.

(b) The Concessionaire must provide, or cause to be provided, to the [ ] a copy of each certificate of currency, renewal certificate and endorsement slip, as soon as practicable after receipt by or on behalf of the Concessionaire, and a copy of each insurance policy other than in respect of any insurances under Clause 54.1(a), which will be made available for inspection by the [ ] from time to time as reasonably required by the [ ] subject to the reasonable requirements of the Concessionaire as to confidentiality.

(c) The [ ] must, whenever reasonably requested in writing by the Concessionaire, provide evidence to the Concessionaire of the insurances effected and maintained by the [ ] under this Clause 54.

(d) If, after being requested in writing by the [ ] to do so, the Concessionaire fails to produce evidence of compliance with its insurance obligations under Clauses 54.1 and 54.2 to the satisfaction of the [ ], the [ ] may effect and maintain the insurance and pay the premiums for that insurance. Any amount paid by the [ ] will be a debt due from the Concessionaire to the [ ].

(e) The [ ] must keep confidential and not make or cause disclosure of any information contained in any insurance policy or endorsement slip provided by the Concessionaire to the [ ] under Clause 54.3(b) that relates to insurance effected and maintained under Clause 54.1 other than to the extent that such disclosure is for the purposes of making a claim under any such insurance policy or is disclosure within the scope of any of Clauses 59.2(a)(i),(ii) or (iv).

54.4 Notices from or to the Insurer

Except to the extent prohibited by Law, the Concessionaire must ensure that each policy of insurance required to be effected by the Concessionaire in accordance with this Agreement contains provisions acceptable to the [ ] that:

(a) require the insurer, whenever the insurer gives to or serves upon the Concessionaire or its Sub-Contractors or consultants a notice of cancellation or other notice concerning the policy, at the same time to give to the [ ] a copy of the
notice that has been given or served upon the Concessionaire or its Sub-
Contractors or consultants;

(b) provide that a notice of claim given to the insurer by the [ ], the Concessionaire or
any of the Concessionaire’s Sub-Contractors or consultants will be accepted by the
insurer as a notice of claim given by the [ ], the Concessionaire, the Sub-
Contractor and the consultant; and

(c) require the insurer, whenever the Concessionaire fails to renew the policy or to pay
a premium, to give notice in writing thereof forthwith to the [ ] and the
Concessionaire prior to the insurer giving any notice of cancellation or non-
renewal.

54.5 Notices of Potential Claims

The Concessionaire and the [ ] must, as soon as practicable, inform the other in writing of
any occurrence or incident that may give rise to a claim under a policy of insurance
required by Clauses 54.1 or 54.2 and must keep the other informed of subsequent
developments concerning that occurrence or the claim.

54.6 Settlement of Claims

Upon settlement of a claim under the insurance required by Clauses 54.1 or 54.2, where
the [ ] did not have an insurable interest, the Concessionaire must pass through to the [ ]
the benefit of the Concessionaire’s insurance where the [ ] has suffered Loss for which the
Concessionaire is liable to indemnify the [ ] under this Agreement or any other Project
Agreement.

54.7 Cross Liability

Wherever pursuant to this Agreement insurance is effected in more than one name, the
policy of such insurance must, insofar as the policy may cover more than one insured:

(a) provide that all insuring agreements and endorsements operate in the same
manner as if there were a separate policy of insurance covering each party
comprising the insured;

(b) provide that the insurer waives all rights, remedies or relief to which it might
become entitled by subrogation against any of the parties comprising the insured
and that failure by any insured to observe and fulfil the terms of the policy does not
prejudice the insurance in regard to any other insured party; and

(c) contain a non-imputation clause providing that any non-disclosure or
misrepresentation (whether fraudulent or otherwise), any breach of term or
condition of the policy, or any fraud or other act, omission or default by one insured
does not affect another insured provided that the said acts or omissions were not
made with the connivance of that other insured.

54.8 Extent of Cover

If the [ ] at any time reasonably requires the Concessionaire to:
(a) insure against a risk not specifically provided for or contemplated under Clauses 54.1 or 54.2; or

(b) increase the extent of or change the terms of an existing cover in relation to a risk, it may notify the Concessionaire accordingly and request that the Concessionaire give effect to the [ ]’s requirements as set out in the notice. The Concessionaire must promptly notify (and provide supporting evidence to) the [ ] of the amount (if any) of any additional premium payable to effect a request by the [ ] under this Clause. Within 10 Business Days after receipt of notification from the Concessionaire of that amount of additional premium (if any), the [ ] must inform the Concessionaire whether it requires the Concessionaire to effect that insurance cover. If the [ ] notifies the Concessionaire that the [ ] requires the Concessionaire to effect that insurance cover, the Concessionaire promptly must do so and the [ ] must reimburse the amount of the additional premium to the Concessionaire within 20 Business Days after the Concessionaire provides evidence satisfactory to the [ ] that the insurance cover has been so effected.

54.9 General Requirements

(a) All insurances which the Concessionaire is required to effect under this Clause 54 must:
   (i) with the exception of the insurances required by Clauses 54.1(a)(i), 54.1(a)(ii), 54.1(a)(iii), 54.2(a) and 54.2(b), be in the names of the Concessionaire and its Sub-Contractors, the [ ] and the Operators (as applicable) for their respective rights, interests and liabilities;
   (ii) contain such conditions, endorsements and exclusions as are reasonably required by the [ ];
   (iii) contain no conditions, endorsements or exclusions unless those conditions, endorsements or exclusions have been first approved in writing by the [ ], such approval not to be unreasonably withheld;
   (iv) not be materially altered by or on behalf of the Concessionaire without the prior written approval of the [ ]; and
   (v) contain a provision requiring the applicable insurer to give the [ ] at least 10 Business Days prior written notice of its intention to serve a notice of cancellation on the Concessionaire in respect of the applicable policy.

(b) The Concessionaire must not knowingly permit or suffer to be done any act, matter or thing whereby any insurance required to be effected under this Clause 54 may be vitiating or rendered void or voidable.

(c) The Concessionaire must pay or cause to be paid punctually all premiums and other moneys payable in respect of any policy of insurance required to be effected by the Concessionaire.

(d) The Concessionaire must give full, true and particular information to the relevant insurer of all matters and things the non-disclosure of which might in any way prejudice or affect any such policy or policies of insurance or the payment of any or all moneys thereunder.
(e) Before the cancellation by the Concessionaire of any insurance required to be
effected under this Clause, the Concessionaire must first obtain the consent of the
[ ] after having provided the [ ] with the reasons for the proposed cancellation and
details of the replacement insurance which is proposed to be substituted for the
policy proposed to be cancelled.

(f) Other than upon or following:
(i) the expiry or termination by the [ ] of this Agreement; or
(ii) notice from the [ ] pursuant to Clause 53.2(b),

the [ ] waives in favour of and for the benefit of the Concessionaire the [ ]’s right to
give a notice of claim to the insurer under a policy required under Clauses
54.1(a)(iv) or 54.2(d).

(g) The Concessionaire must do everything reasonably required by the [ ] or any other
person in whose name an insurance policy is effected and maintained to enable
the [ ] or other person (as the case may be) to claim, and to collect or recover
money due, under or in respect of any insurance policy.

54.10 Additional Requirements

The Concessionaire must comply, and must ensure that the Construction Contractor, the
Operator and the Maintenance Contractor each comply, with their respective obligations to
take out and maintain registration and to pay all levies required to be paid, under the
Accident Compensation Act 1995 (Vic) and the Accident Compensation (Workcover
Insurance) Act 1993 (Vic) and to take out and maintain insurances required under the
Building Act 1993 (Vic).

54.11 Indexation of amounts of cover

(a) On 1 July 2006 and each subsequent 1 July (adjustment date) until the end of the
Operating Phase, the amount of cover required for the insurance required in
accordance with Clause 54.2(b) will be adjusted in accordance with the formula set
out below and then rounded upwards or downwards to the nearest $[ ] amount:

\[
\text{Adjusted Insurance Cover} = \text{Payment Multiplier} \times \text{AIC}
\]

where:

\( \text{AIC} \) = in respect of:

(i) 1 July 2006, $[ ]; and

(ii) each subsequent adjustment date, the adjusted insurance cover applicable
immediately prior to the relevant adjustment date (disregarding rounding (if
any) applied to that cover at the previous adjustment date).

(b) On 1 July 2006 and each subsequent 1 July (adjustment date) until the end of the
Operating Phase, the amount of cover required for the insurance required in
accordance with Clause 54.2(c) will be adjusted in accordance with the formula set
out below and then rounded upwards or downwards to the nearest $[ ] amount:

\[
\text{Adjusted Insurance Cover} = \text{Payment Multiplier} \times \text{AIC}
\]
where:

$AIC = \text{in respect of:}$

(i) $1\ July\ 2006, \$[\ ]; \text{and}$

(ii) each subsequent adjustment date, the adjusted insurance cover applicable immediately prior to the relevant adjustment date (disregarding rounding (if any) applied to that cover at the previous adjustment date).