CONSTRUCTION LIABILITY INSURANCE—READ THE POLICY CAREFULLY!

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INTRODUCTION

A construction liability insurance policy commonly provides indemnity with respect to third party claims brought against project participants, but will not generally operate to afford indemnity with respect to claims brought by project participants against each other with respect to damage caused to the work under the contract.

This can be contrasted with the operation of a contract works insurance policy, which, while being a policy of property insurance, often extends the benefit of cover to project participants who do not necessarily have an interest in the property which is damaged. The courts have emphasised the notion of such parties having a 'pervasive interest in the whole of the works' due to the 'common venture' nature of a construction project and the commercial convenience of having project participants insured under the one policy.

The exclusion from cover of such claims in construction liability policies, is usually sought to be achieved by an exclusion in relation to any claims arising out of damage to property that comprises the insured project (subject to 'carve outs', for example in relation to damage to existing structures and the like).

Notwithstanding this, the issue continues to arise from time to time as to the applicability of construction (or broadform) liability insurance with respect to claims arising out of damage to insured property brought by other project participants. It is accordingly worthwhile revisiting a comparatively recent decision in New South Wales (NSW) which highlights the need to closely examine the wording of insurance policy exclusions, in order to ensure that the cover provided accords with the parties' intentions.

The decision is the case of *Transfield Pty Ltd v National Vulcan Engineering Insurance Group Ltd*[1] and the reasoning applied by the Judge at first instance and subsequently by the NSW Court of Appeal accords with the decisions in *Re FAI General Insurance Co Ltd & Fletcher*[2] and *Speno Rail Maintenance Australia Pty Ltd v Hamersley Iron Pty Ltd*,[3] in which it was considered (in the context of so called 'worker to worker' exclusions) that where a policy included similar clauses as found in those cases, each party comprising 'the insured' would be considered as a separate legal entity and that expression would apply to each party as if a separate policy had been issued to each.

AT FIRST INSTANCE

Transfield was the principal contractor for the construction of a section of the New Southern Railway, being 158m of reinforced concrete tunnel. For the purpose of the project Transfield engaged four subcontractors. On two separate occasions sections of the works collapsed causing damage to plant and equipment belonging to two of the subcontractors. As a result, proceedings were brought by the two subcontractors.

Transfield also commenced proceedings against the two contractors for property damage it had suffered.

Prior to the incidents, Transfield had taken out a contractor's floater policy. The policy extended cover to Transfield,

... and their subcontractors and all principals as they may appear and all other interested parties as may be required, for their respective rights, interests and liabilities.

The policy was, however, subject to an exclusion 'for damage to property owned by the insured'.

The primary issue was whether the policy responded to indemnify the subcontractors against the claim made by Transfield, all of whom were insureds under the policy. This involved the determination of whether the meaning to be given to the term 'the insured' in the exclusion clause was a reference to any insured or to the separate insured seeking policy indemnity in respect of the claim made against it.

The policy included a clause deeming subcontractors to be included in the name of the insured, waiver of subrogation and particularly a cross–liability clause that provided:

Each of the persons comprising the insured shall for the purposes of this policy be considered as a separate and distinct unit and the words 'the insured' shall be considered as applying to each of such persons in the same manner as if a separate policy had been issued to each of them in his name alone ...

The insurer argued that the property that failed was owned by Transfield and the policy did not extend to liability 'for damage to property owned by the insured'. Furthermore, the insurer submitted that the expression 'the insured' as identified in the deeming provision—

In respect of operations performed by subcontractors ... such subcontractors shall be deemed to be included in the name of insured

—when used in the exclusion was to be construed as meaning all of the insureds under the policy.

In rejecting the insurer's arguments, McClellan J found that the policy was clearly intended to insure each insured (including subcontractors as deemed insureds) for their respective rights, interests and liabilities. Informed by the cross–liability clause,

each party was to be considered a separate entity 'in the same manner as if a separate policy had been issued to each of them'.

Accordingly, the exclusions needed to be interpreted in the same light.

Therefore as the claim for indemnity by the subcontractors relating to their liability for damage to Transfield's property was not for damage to their property the exclusion was inapplicable and indemnity was available under the policy.

ON APPEAL

The case went on appeal to the NSW Court of Appeal.[4] The central question was whether the policy responded to a claim by one insured in respect of property damage it had sustained as the result of the assumed negligence of another, or whether the exclusion applied.

The critical part of Santow JA's reasoning (with whom Ipp JA and Young CJ in Eq agreed) was—

42. ... 'When in clause 1 of section C the insurers commit 'to pay on behalf of the insured all sums which the insured shall become legally obligated to pay' as well as defending any claim or suit against the insured to recover damage, one would expect the words 'the insured' to have the same meaning in section C when it comes to stating exclusions, namely the insured who claims under the policy. Indeed clause

3(a) also logically must operate on that basis when it excluded 'bodily or personal injuries sustained by any person ... in the course of his employment by the insured'. Here, there is no need for any

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stretch of the imagination to envisage circumstances where employees of the insured would claim under the policy but for the exclusion in clause 3(a).

43. Thus as each of the exclusions 3(a) and (b) operate as an exception to the cover provided by section C, each must be construed in the same manner ...

44. Similarly, the 'liability' in relation to which exclusions 3(a) and 3(b) operates is and can only be the liability of the particular insured entity which makes a claim under section C.

45. Further, to construe 'the insured' in Exclusion 3 (b) as meaning 'any of the insured entities' is inconsistent with:

(a) the use of the definite article;

(b) the use elsewhere in the policy of different language where it is intended to refer to insured entities generally or any one or all insured entities.

...

49. Furthermore, construing Exclusion 3(b) as referring only to the insured entity which makes the particular claim is expressly reinforced by [the cross–liability clause].[5] His Honour rejected a submission by the insurer that his interpretation would render the exclusion redundant. He pointed out that it would apply to claims in respect of property in which a third party had a partial proprietary interest, and so exclude claims by one joint owner against another, or a mortgagee or lessee against an owner.

While the policy considered in National Vulcan, expressly insured the parties 'for their respective rights, interests and liabilities' and it contained a cross–liability clause, those features did not appear to be essential to Santow JA's reasoning.[6]

Santow JA considered that the exclusion in National Vulcan could operate logically only if 'the insured' referred to was the insured making the claim. Although a contrary conclusion had been reached by Wilson J of the Supreme Court of Queensland in *WorkCover Queensland v Royal & Sun Alliance Insurance Australia Ltd*,[7] Santow JA specifically declined to follow Wilson J.[8]

CONCLUSION

The result of this decision would appear to be that, at least in circumstances where a policy contains a cross–liability clause, (and possibly even in the absence of such clause) the meaning of 'the Insured', subject to an express intention to the contrary, should be considered in the context of the insured that is seeking coverage under the policy for the particular claim. This may have the effect therefore, of extending the operation of the policy to claims between insureds. For the exclusion to have operated as suggested by the insurer in Transfield, the policy wording ought to adopt language clearly reflecting the intent. McClellan J suggested that to achieve this intention the exclusion would have to read either 'any insured' or 'an insured' rather than 'the insured'.

REFERENCES

1. (2003) 12 ANZ Ins Cas 61–489

2. *Re FAI General Insurance Co Ltd & Fletcher* (1998) 10 ANZ Ins Cas 61–403

3. (2003) 23 WAR 291, 19 December 2000

4. *National Vulcan Engineering Insurance Group Ltd & Ors v Transfield Pty Ltd* (2004) 13 ANZ Ins Cas 61–595

5. at pp 77,074–5

6. at [42]–[45]

7. (2001) 11 ANZ Ins Cas 61–489

8. (see *National Vulcan* at [60])

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