MARSH

FINPRO Practice

PROJECT PROFESSIONAL INDEMNITY INSURANCE

The demand for project professional indemnity (PI) is growing as construction project owners often insist a Project PI policy is in place, particularly for the larger, prestigious projects. Project owners value the benefits of certainty in the current economic climate and in response, Marsh has launched a Project PI facility.

BENEFITS OF COVER

The facility is aimed at major construction projects anywhere in the world, excluding projects domiciled in the USA, and can provide limits of liability of up to £20m for periods of insurance of up to 10 years.

The facility is designed to cover all project participants with responsibility for professional services rendered in connection with the construction process. This includes contractors and consultants alike, whether working individually or in joint ventures or consortia.

The facility is suitable for projects with an estimated construction value in excess of £25m and provides:

- Non-cancellable limits of liability that are dedicated to the project.
- Certainty of coverage for the project with periods of insurance of up to 10 years (with the possibility of further periods being available after completion of the construction process, in order to comply with contractual obligations).
- Certainty of cost for the PI insurance.
- Indemnity to owners in circumstances where the owners are claimed against by third parties due to professional errors or omissions committed by the construction parties.
- Wrap-up coverage for all construction parties engaged in the provision of professional services.
- The facility can also be utilised by project owners by way of Owner Controlled Insurance Programmes (OCIP) whereby the owner arranges project PI insurance on behalf of the construction parties thereby ensuring total transparency of cost.

WHY SINGLE PROJECT PROFESSIONAL INDEMNITY?

FROM AN OWNER'S PERSPECTIVE

Project PI premiums are often viewed as being somewhat expensive, yet when one analyses this pre-concept it is not difficult for an owner to form a somewhat different view for the following reasons:

- The premium affords certainty of coverage over a number of years in terms of the available limit of liability and the scope of coverage; the total premium should therefore be broken down over the whole policy period.
- If contractors' and consultants' own annual practice PI policies are utilised the owner is likely to still end up funding the premium. However, the cost will be unknown and hidden as the construction parties each add the cost of maintaining PI for the required period to their contract prices. This unknown cost could potentially be higher than the cost of purchasing a project PI policy.
- Following completion of the project, the owner has very little control over whether or not the contractors and consultants renew their PI policies.
- Any one of the contractors' or consultants' own annual practice PI policies could potentially fall into default during the period that they are required to maintain cover. This may be because the available limit of indemnity for a certain party has already been eroded by another claim on another project (see note below), breach of a policy term or condition, or insurer insolvency.
- If reliance is placed on annual PI policies of contractors and consultants, additional costs and delays may be incurred arising out of the need to prove liability against 'the guilty party'. Potential disputes may also arise when agreeing apportionment of blame and with differing approaches to the settlement of a claim by the various PI insurers involved.
- It is becoming increasingly common for contractors and consultants to insist on liability caps limiting an owner's recourse against such contractors and consultants in the event of a professional indemnity claim. Contractual language can be used to allow the contractors and consultants to cap their liability to a set limit under their own PI insurances yet allow for additional liability to be covered by way of an OCIP.

Note. PI policies operate on a 'claims made' basis. This means that the policy of response is the policy in force when a claim is first made against the insured party. PI claims can take many years to reach settlement. It is therefore not difficult to contemplate the following situation:

- An owner diligently checks and ensures that the design/build contractor he has engaged to carry out a project on his behalf continues to renew and maintain adequate PI insurance as required under the contract.
- A professional error is committed by the contractor resulting in a defect in the project.
- This leads to a dispute over the costs of rectifying the defect and the owner is subsequently forced to make a claim against the contractor and the contractor's PI policy.
- Successful prosecution of the claim (whether through the courts, mediation or negotiated settlement) is not achieved until three years after the original claim was made.
- In the meantime another unrelated PI claim against the contractor on the same policy year has already been settled exhausting the available PI limit for that year leaving the owner with an uninsured loss.

An owner will, therefore, often prefer to purchase a single project PI policy covering the professional acts, errors or omissions of the various parties employed on the project.

The owner then has control over the scope of cover, the policy duration and limit. They also know the cost from the outset, removing unknown additional costs from contractors and consultants.

In summary the benefits of an owner arranged Project PI policy include:

- Cost of coverage is known from the outset.
- Avoidance of disputes between the various contractors and sub-contractors.
- Avoidance of additional costs involved with each construction professional defending its own position.
- The scope of coverage for all contractors and consultants is consistent.
- The project limit remains in force irrespective of the erosion of the individual contractors'/consultants' own annual PI limits.
- Assured policy response for an agreed discovery period after the completion of the project.

FROM A CONTRACTOR'S OR CONSULTANT'S PERSPECTIVE

JOINT VENTURES

If a contractor or consultant has a suitable annually renewable practice PI policy then project PI is unlikely to be a consideration.

However, when contractors and/or consultants form joint ventures consideration may well be given to a project PI policy.

Joint ventures are an effective way for contractors and consultants to pool resources and expertise on large projects.

The respective joint venture parties may have differing levels of annual PI coverage, excesses and limits. In some cases members of a joint venture may have no PI insurance at all.

If joint venture members were to rely solely on their separate annual policies each joint venture member would have to seek indemnity from its individual insurers. The various insurers may take differing stances on how the claim should be dealt with, or how the claim should be paid. This can create problems, delays in settlement and potentially additional costs to insurers, the insured and the owner.

An annual contractor's PI policy often does not provide full cover for joint ventures and an insured is unlikely to want their annual policy impacted by claims from another member of the joint venture.

Where a joint venture operates on an integrated basis it may be impossible to determine which member of a joint venture is responsible for an error.

A Project PI policy helps avoid these problems by providing a separate wrap-up policy for the joint venture members with a specific, dedicated limit and for a specific period of time.

The benefits of a Project PI policy where the contract is being undertaken by a joint venture include:

- Avoidance of disputes between the joint venture members.
- Consistent scope of coverage for all joint venture members.
- Claims experience of the joint venture is less likely to impact the individual joint venture members' own annual PI policy.
- The project limit remains in force irrespective of erosion of the individual members' own annual PI limits.
- Coverage for an agreed discovery period after the completion of the project, providing both the joint venture members and the owner with certainty of policy response.
- The total cost of the PI coverage for the project can be budgeted for and charged to the project.

FROM A PROJECT FINANCIER'S PERSPECTIVE

Financiers of a project may require the owner to take out a dedicated single project policy. This is to protect the financier's interests and investment, irrespective of any of the consultants' or contractors' own annual PI arrangements. The benefits for this are the same as those outlined for project owners.

ENQUIRY TO FIRM ORDER

STAGE ONE – THE ENQUIRY

The proposer completes the simple Short Form Project Questionnaire (SFQ) and submits it to Marsh Ltd.

STAGE TWO – THE INDICATION

Marsh provides the proposer with non-binding indications of premiums. The project indication sheets are designed to be as user friendly as possible and use plain English without complicated insurance terms and jargon.

STAGE THREE – THE SINGLE PROJECT FULL PROPOSAL FORM

This stage is normally reached once the contract for the project is awarded to the proposer, the initial insurance indications have been provisionally accepted and firm quotations are required. It is at this stage that Marsh will request a full underwriting submission from the proposer. The quality of the underwriting submission is critical to the quotation process. It can have a positive or negative effect on the final terms depending on its content. For this reason Marsh has designed a comprehensive single project full proposal form (SPFPF) to ensure that insurers have the benefit of full and comprehensive information on the project. This form is designed to be easily understood by people who are not necessarily well versed in insurance terminology. At all stages of the information gathering process Marsh remains on hand ready to assist.

STAGE FOUR – THE FIRM QUOTATION

Upon receipt of the fully completed and signed SPFPF Marsh presents the information to insurers together with premium and coverage recommendations for approval. Marsh then provides the firm quotation to the proposer.

STAGE FIVE – BINDING THE ORDER AND POLICY DOCUMENTATION

If the firm quotation is accepted by the proposer, coverage is bound with insurers by Marsh from the agreed inception date. Marsh processes and administer the placement on behalf of the insured.

STAGE SIX – PREMIUM ADJUSTMENT

The project PI policy will normally have a minimum and deposit premium, which will be adjustable on the final contract value or the final fees dependent on the nature of the contract. The adjustment is due within 90 days after the issuance of the partial acceptance certificate (or similar).

To download a short form questionnaire please visit

http://www.marsh.co.uk/risk/professionalliability/documents/Marsh_Project_PI_Short_Form_Questionnaire.doc

The operation of the facility is headed up by Martin Stubbs, a Senior Vice President at Marsh's FINPRO Practice in London, who has been responsible for the placement of over 100 project PI policies throughout the world.

FOR FURTHER INFORMATION, CONTACT

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