# TIPSHEET 8 – PI INSURANCE: TIPS & TRAPS FOR CONSTRUCTION CONTRACTS (PART 1).

Common 'pitfalls' for construction professionals in professional services contracts and the impact on PI insurance.

## SCOPE OF SERVICES

Sometimes the scope of services described in a professional services contract 'goes beyond' the type of services or work usually performed by professionals in that industry. This area is often overlooked by clients or their lawyers when reviewing contracts.

The terms of a professional services contract and the services that a professional agrees to provide is an important factor in determining the duty of care that applies to those services[i] and the extent of any damages a person can claim for breach of contract.[ii]

The goods and services described in the contract should be consistent with the type of goods and services the insurer has agreed to insure you for. It is always a good idea to check with your broker that you are covered for particular business activities whenever you sign a contract particularly if you might be providing a new service.

If the contract doesn't fully describe the products or services you will provide then you should make sure that this is fixed and the parties have agreed precisely what will be provided under the contract. This should be detailed in the contract – it is best to avoid referring to another document or letter as this may be difficult to find in the future if there is a dispute.

Sometimes the type of service you have agreed to provide may be excluded by the terms of your policy – always check with your broker.

*EXAMPLE: A professional services contract may require the Consultant to "warrant that any designs will conform to a cost plan provided by the Principal (as amended at the time the relevant design work is carried out)". Many PI policies exclude claims relating to an estimate of construction cost or a failure to meet a construction budget.*

The contract may need to be re-drafted to ensure that any claims for breach of this obligation do not trigger the policy exclusion. If you want to offer a service that does not come within the 'professional services' description in the policy, your broker needs to seek an endorsement to amend the 'professional services' description.

*EXAMPLE: Generally, an architect coordinates their work with other consultants. Unless the contract is a 'design and construct' contract, an architect does not usually have a 'project management' role. If the architect wants to provide project management services (whether under a 'design and construct' contract or otherwise), the professional services description*

*in their policy should be reviewed and if necessary extended to include "project management services".*

## DUTY OF CARE / ACTING AS AN EXPERT

Over time nearly all professionals develop areas of specialisation or expertise. If they make representations to clients about their expertise, the client can rely on those representations in a way that alters the professional's 'duty of care'. The duty of care is the legal standard at which the professional is expected to provide their services (ie to "use reasonable care, skill and diligence" in the performance of the work they undertake).[iii] This applies unless a different duty is agreed by the parties.

Most PI policies exclude claims for liability which is assumed by the professional that is different to their liability at law. If a professional agrees to assume the standard of an 'expert' or represents in the contract that the services will be provided as an 'expert', it can trigger this exclusion and a claim for failure to meet the 'expert' standard may be declined by the insurer.

Take care when making oral or written representations about having particular expert skills (whether in the contract or elsewhere).

*EXAMPLE: An architect tells a client that he is an expert in a particular field of architecture (eg heritage architecture) and the contract states "the Consultant shall perform the services with the degree of professional skill, care and diligence expected of an expert professional in heritage architecture". A claim involving breach of contract for failure to expertly provide the services could be denied by the insurer because this liability was 'assumed' under the contract. It required the architect to do more than exercise the reasonable care and skill of a reasonably qualified and competent architect.*

## RELIANCE ON THE WORK OF OTHERS

On a major project, any number of consultants may work together, (eg consulting surveyors, engineers, architects, specialist designers, quantity surveyors and other consultants) who collaborate on a project in their particular discipline.

Logically each of them will rely on the particular expertise, skill and experience of the others when working in this way. However this approach may be different to what is actually contained in a professional services contract.

Often contracts for large projects state that the consultant cannot rely on the documents or materials that are supplied by the principal or developer because that person does not want to guarantee the accuracy of those materials. Quite often the consultant will have to satisfy itself that the documents or materials (including drawings, specifications, reports, surveys etc.) can be relied upon and that there are no errors or inadequacies in the materials and documents.

There is no different treatment for documents and materials that have been prepared by another consultant. Imagine asking an architect to check that the engineer's work is sound before using it in their design! If an architect or surveyor can do this, what is the role of the engineer!

A PI policy won't respond to claims arising out of these clauses if they extend the duty of care beyond the reasonable professional expertise of the insured for their professional business. The "assumed or contractual liability" exclusion and the professional services description may be used by an insurer to deny cover.
*EXAMPLE: A surveyors' services contract states: "You must not rely upon or use (or allow any*

*other person to rely upon or use) the information and documents the Principal and any other Contractor supplies to you for or in connection with the provision of your Services until you have satisfied yourself as to the accuracy, completeness and adequacy of the information, or until we have otherwise notified you that the information may be so relied upon or used."*

*The effect of this clause is that:*

- *the surveyor's duty to satisfy itself as to the accuracy, completeness and adequacy is not limited to "matters within the reasonable professional skill and expertise of a qualified and competent surveyor"; and*
- *the surveyor is not permitted to rely on the professionalism of other consultants who have prepared the documents and information.*

*If a claim arose involving the surveyor's reliance on the drawings or specifications of an engineer working on the project, the surveyor could be liable (for breach of contract) for failing to detect an inaccuracy in those drawings even though a reasonable surveyor would not know that the inaccuracy existed because it was a matter outside their professional expertise or discipline.*

## CERTIFICATION OF WORK

Certification is often given by construction professionals (including architects, builders, engineers and surveyors) when building work has been completed.

Builders must guarantee their construction work and they often give a certification that the building has been constructed in a good and workman-like manner or the building is structurally sound or free of defects and/or safe and suitable to be taken into service.

Other professionals can only give a certification as to the conformance of the building with the design, documents and specifications they prepared for the project. They cannot certify the same things that a builder can because they haven't constructed the building. Likewise a certification as to quality of fixtures, fittings and finishes used in construction should not be given unless those things have been designed and manufactured by or at the direction of the construction professional.

Check if the contract requires the professional to certify the building. Certification should be confined to:

- Things that are actually known, or could reasonably be known, to the professional after making reasonable enquiries or conducting a reasonable inspection.
- Things that are within the professional's area of expertise or their professional discipline.

These things will differ depending on the scope of the services but in most cases should be limited to conformance of the building to the design, drawings and specifications prepared by the professional or to the extent of the professional's information, knowledge and belief after making reasonable inquiries/inspection. Certificates given on completion are often included in the schedule to a professional services contract and they should be reviewed carefully before the contract is signed in case they extend the professional's duty or fall outside the 'professional business' definition in a PI Policy.

Some PI policies exclude claims relating to the quality of the construction, erection or installation of the built works. If so, the

professional cannot give a broad certification and still be covered by their PI policy.

*EXAMPLE: The following clause could trigger a number of exclusions in a PI policy:*
*"The Consultant shall certify that any building work, structure, plant, equipment and/or services installed by any Builder as a result of any design, drawing, specification or other document prepared by the Consultant as part of or in connection with the Services is structurally sound, safe for use for the purposes described in the Brief and at practical completion is free from patent defects."*

## SUB-CONSULTANTS

PI policies do not usually insure the work of sub-consultants engaged by the professional unless they are 'named insureds' under the policy. In most cases, the policy covers the "vicarious liability" of the professional for the sub-consultant's work but not any direct liability that the sub-consultant may have.

Instead of naming sub-consultants under the professional's PI policy, it is usually better to ask sub-consultants to maintain their own insurance. It may be necessary to modify the professional services contract so that the professional agrees to obtain a certificate of currency from each of the sub-consultants as a condition of their appointment and on request by the principal.

## SET OFF CLAUSES

Set off clauses allow a principal to deduct any costs they incur from the consultant's fees, if there is a failure to perform the services to the standard required under the contract. These clauses can have a big impact on PI insurance. The main issue is whether the consultant can access their PI policy to meet the costs. Often the answer is "No" because the clause allows the principal to automatically deduct their losses without making a claim for compensation.

If there is no "civil liability claim" made against the consultant (ie a legal claim or demand made by the principal) and the principal has deducted the costs from the consultant's fees, there may be no basis for the consultant to make a claim under the PI policy (even though the reason for deducting the fee was due to a professional failure by the consultant).

Set off clauses allow the principal to avoid making a damages claim altogether and the consultant can be left "out-of-pocket" if they can't be indemnified by the policy for their loss.

*EXAMPLE: An engineer's professional services contract, contains a clause which states: "If, as a result of the Consultant's failure to perform its obligations in accordance with this Contract, the Principal requires the performance of additional services or incurs any other costs or expenses, then the losses incurred by the Principal as a result of such failure may be deducted from the Consultant's fee."*

*The engineer has made an error in the drawings and specifications for construction of the building. The principal has engaged a new engineer and has deducted the cost of some of their work from the fees payable to the engineer. No claim for professional negligence or breach of contract has been made, so the engineer cannot claim on their PI policy to recover the loss of fees even though this is due to an error or omission in the course of providing professional services.*

**If you would like a legal review of your contracts and insurance policies, contact your insurance broker for a referral.**

i *Al Mousawy v Howitt-Stevens Constructions Pty Ltd & Ors* [2010] NSWSC 12

ii *Roluke Pty Ltd & Anor v Lamaro Consultants Pty Ltd & Anor* [2008] NSWCA 323

iii *Voli v. Inglewood Shire Council* (1963) 110 CLR 74.

## CAN WE HELP YOU.

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For further assistance, contact:

**The Steadfast Contractual Liability Helpline**

T 02 8353 6607
E contracthelpline@thefoldlegal.com.au

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