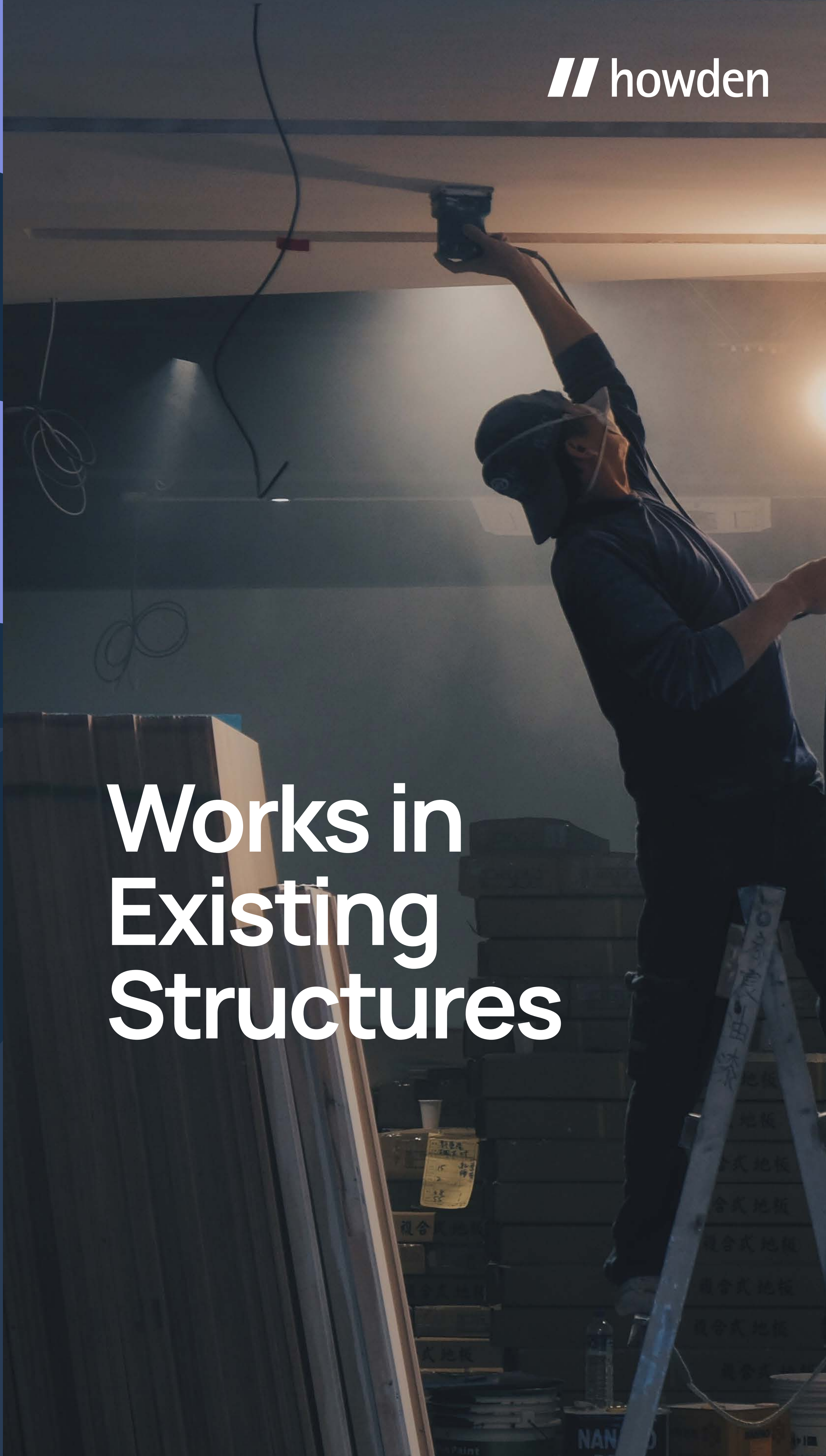

Works in Existing Structures

Undertaking construction works where an existing structure is involved adds another element of risk that needs to be considered at an early stage.

However, before we explore this further it is probably worth recapping on the three main insuring options under a JCT contract:

- **Option A** is intended for new build projects where the requirement is for the contractor to be responsible for the insurance of the works in "Joint Names" with the employer;
- **Option B** is also intended for new build projects where the requirement is for the employer to be responsible for the insurance of the works in "Joint Names" with the contractor;
- **Option C** is to be used where the work consists of refurbishment of, modifications to, or extensions of an existing structure. In this situation it is traditionally the employer that is responsible for insurance of the works and the existing structure (for Specified Perils) in "Joint Names" with the contractor.

As you will see, the first and second options deal with insurance of the works for new build projects and are quite straightforward in that either the contractor or the employer takes responsibility for insuring the works (Construction "All Risks" Insurance). However, the third option includes the existing structure which adds another area of complication and one that has been an issue for many years (the author was contacted circa 10 years ago for advice on possible solutions). The issue is that the contractor is unable to adequately insure the existing structure as it is not their building and often the employer will not be willing or able to include the contractor as an insured. Reasons for this attitude include:

- Employer's risk management philosophy;
- Property insurer reluctance to take on construction-related risks;
- The employer is a tenant and does not control the property insurance.

It is for this reason that the JCT introduced a new option known as the "C.1 Replacement Schedule" in their 2016 suite of contracts though slightly unhelpfully (though understandably) this just leaves it blank for the parties to insert the alternative insuring option to be used.

What are the solutions?

Luckily, for an experienced construction/real estate broker this is relatively simple to fix as there are generally three alternative options for covering the existing structure:

1. **The landlord agrees to include the contractor as an insured (or waive subrogation rights) on the existing property insurance.** This is the most straightforward solution but is often not possible as the landlord and/or their insurers will not want to expose their policy to claims arising from the works and will want to retain subrogation rights against the contractor. However, even if it is possible to include the contractor as an insured, it may not be best suited where structural alterations are involved, as operational property policies always exclude collapse, other than where such damage itself results from a defined peril;
2. **The landlord agrees for the tenant to take over insuring responsibility for the existing structure for the duration of the works and as such the tenant can add the contractor as a named insured**. This is quite rare and only really occurs on major refurbishments where the tenant is the sole occupier of the building (i.e. it does not work for multi-tenanted buildings);
3. **The risk of damage to the existing structure arising from construction activities is passed to the contractor as a third party liability risk.** This is the most common solution and often a contractor will take out a specific Third Party (Public) Liability (TPL) policy to the value of the existing structure to ring-fence this risk away from their annual liability policy. This can however have its challenges due to the cost of this cover. As such, a compromise may be considered where the contractor is held liable for a reasonable primary limit, with a release of liability in excess, in accordance with unamended JCT Option C. The advantage of this approach is that it helps reduce cost and provides comfort to the landlord's property insurer that it has rights of recourse up to the agreed limit.

   A variation of the above could be the employer taking out this TPL policy and include the contractor on this cover; there are various scenarios where this is the most sensible solution. Care should however be taken as it is not uncommon for standard contractor or employer public liability policies to exclude damage to existing structures as insurers deemed this not to be third party property.

   In recent years the cost of these TPL policies has increased significantly primarily as a result of various fire and escape of water claims such as the Glasgow School of Art, London Mandarin Oriental Hotel, Primark Belfast (all in 2018) and Koko Camden (2020). To help mitigate these pricing increases, as well as the solutions identified above, there are various other mechanisms that can be put in place (both from a contractor's and employer's point of view) to reduce these premiums and we would be happy advising on these if this is of interest.

Whichever option is chosen, the JCT drafting is likely to need amending and in particular care should be taken on Clauses 6.3, 6.9 and Schedule 3 to ensure that these correctly reflect the final agreed insurance position.

Revenue Cover

Another nuance for work within an existing structure that is worth briefly flagging is that where an asset is going to be revenue generating post completion of the works (e.g. office, student/residential accommodation, hotel) and this revenue stream is insured then great care needs to be taken on how this cover is structured. For example:

- For a new build project you would generally set the indemnity period (maximum period insurers would pay out for if there was a delay) at the original construction period plus circa 10%. However, if an existing structure is involved this is not the correct way of calculating the indemnity period as the presence of the existing structure can completely change the length of the potential delay;
- The relationship between the construction revenue cover and any property business interruption cover needs to be considered, as well as how the existing structure itself is actually insured.

For works that do not have a structural component and where areas of the building remain partially operational, investigations should be explored under the landlord's policy to insure its anticipated loss of rent receivable. Premiums may be more cost effectively sourced this way, rather than through a construction placement.

This is a very complex area and one that we have seen numerous large brokers fall foul of in the past so early consultation with suitably experienced broker is strongly recommended.

Though construction can be complex, Howden's view is that insurance should never be a barrier and a solution can usually be found. The key is to make sure you engage at an early stage with a specialist construction broker who will be able to offer advice and assistance to guide you to the most equitable solution and more importantly, ensure that the insurance responds in the unfortunate event of a loss.

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