

Liability for sub-consultants

The Claims Department has noted that an increasing number of claims made against construction professionals are being made in circumstances where the construction professional engaged, and is therefore responsible for, the acts and omissions of its sub-consultant. In such cases, proceedings are initially commenced against the construction professional with the sub-consultant subsequently joined as a third party, involving it in the dispute.

The result is a multi-party litigation which prolongs the duration of the dispute, increases legal costs incurred by the parties, including the construction professional and its professional indemnity insurer, and makes resolution of the dispute more difficult. Further, if the sub-consultant (a) has disappeared; (b) is insolvent; or (c) is without any, or adequate, professional indemnity insurance cover, the construction professional may ultimately bear the liability of its sub-consultant. Despite not being negligent, the construction professional will have an adverse claims record.

In a number of instances, pursuant to the dispute resolution process stipulated in the contract, the client has referred the dispute to arbitration. The consequences for the construction professional are that it has incurred significant costs in defending arbitration proceedings which it has had little prospect of successfully defending where its sub-consultant has been negligent. As the sub-consultant is not a party to the arbitration proceedings it is not bound by the arbitrator's findings therefore the construction professional has had to pursue a separate recovery action against the sub-consultant. The result is an increase in legal costs incurred by the construction professional and its professional indemnity insurer.

Construction professionals should always encourage clients to appoint consultants directly. This establishes a contractual relationship between the client and the consultant and in the event of a dispute in respect to the consultant's services:

- The client can deal with the consultant directly without the construction professional becoming involved as a party in any dispute.
- The construction professional is able to continue to give advice to the client to assist in resolution of any dispute thereby maintaining a good relationship with the client.
- The construction professional's claims record will not be adversely affected.

Limitation of liability clauses can work for you

Contracting parties are free to negotiate the terms and conditions of their relationship. Contractual terms can extend liabilities and responsibilities as well as limit them. Limitation of liability clauses in engineering consultancy agreements have been popular for years. With the release last year of the Australian Institute of Architects' new client/architect agreement which also contains a limitation clause, it is important to understand how such clauses work and what you have to do to make sure that they work for you.

Limitation of liability clauses (sometimes called exemption clauses) inserted into consultancy agreements are designed to operate as defences to claims for breaches of contract and negligence. So in simple terms, if a client proves that there has been a breach of contract and/or negligence then you, the consultant, can plead the limitation clause to hopefully exclude or limit your client's rights.

As you may be aware the Association of Consulting Engineers of Australia (ACEA) and the New Zealand Institute of Architects standard consultancy agreements contain limitation of liability clauses. The Australian Standard 4122:2000 General Conditions of Contract includes an optional limitation clause which is sometimes used.

If you are not using a standard form agreement that includes a limitation clause, you might want to contact solicitors to draft one for you. You can limit your liability to:

- a fixed dollar amount;
- the total amount of your professional fees under the agreement;
- a percentage of your professional fees under the agreement;
- an amount of your professional fees under the agreement or a fixed dollar amount, whichever is the greater;
- an amount recoverable under an insurance policy;
- a fixed period of time; or
- a fixed dollar amount and a fixed period of time.

Be aware however that the courts will construe a limitation clause against the party seeking to rely on it and will fully investigate the background facts, the conduct and relationship of the parties, the negotiations and the supporting documentation. So don't always assume that your clause will protect you.

Adele Monaco
National Claims Manager

Case Study¹

An architect engaged an engineer to carry out redevelopment work which included a new area of pavement. The engineer’s engagement included the standard ACEA limitation of liability clauses, one of which discharged it from liability after a year. The clause reads as follows:

“The Consulting Engineer shall be deemed to have been discharged from all liability in respect of the services whether under the law of contract, tort or otherwise at the expiration of the period specified in item 10 of the schedule or if no date is specified on the expiration of one year from the completion of the Services, and the Client (and persons claiming through or under the Client) shall not be entitled to commence any action or claim whatsoever against the Consulting Engineer (or any employees of the Consulting Engineer) in respect of the services after that date.”

Following the engagement, the architect advised the engineer of the load capacity required for the pavement. A year later the client advised the architect of the need to increase the load capacity of the pavement, but the architect did not make the new load requirements known to the engineer. The construction of the pavement was therefore based on the original instructions and design. The pavement collapsed after 4 years and legal proceedings were issued soon after.

At first instance the client successfully sued the engineer and the architect. Liability was apportioned between them on a 50/50 basis. The engineer successfully appealed against this decision on the basis that its terms of engagement contained a limitation of liability clause, which prevented an action being brought against it more than one year after the provision of the services.

Interestingly the engineer’s appeal was successful notwithstanding that the engineer did not actually forward the relevant conditions containing the limitation to the client or architect. The success of the appeal was instead due to the fact that there was no dispute that the client knew that the standard conditions contained a limitation clause and that the engagement of the engineer incorporated the conditions. Further, that the client had accepted the limitation by allowing the engineer to provide its services.

On appeal, judgment was entered against the architect for total costs of rectifying the defective paving.

Things to Consider

Notwithstanding the finding in the above case, it would nevertheless be prudent, in order to be able to rely on your limitation clause to consider the following tips:

- Make sure your limitation clause is clearly written to avoid ambiguity regarding its interpretation. Seek legal advice on the specific wording relevant to your practice. Alternatively, use an industry based consultancy agreement which contains a limitation clause that has been tested in court if possible.
- Provide your client with the written agreement containing the limitation and make sure that the agreement is signed and dated. Your client’s signature on the document is evidence of their agreement to allow you to limit your liability and saves you having to prove your client’s knowledge of the clause and their agreement to it.

- If you intend to incorporate industry standard documents that contain limitation of liability clauses into your consultancy agreement, it would be prudent to make sure the document is referred to, that you provide your client with a copy and can prove receipt and acceptance of it too.
- Complete all information in the agreement and attached schedules relevant to the limitation of liability clause – so that it is clear how you intend to limit your liability. Don’t leave blank spaces or rely on oral evidence or having to imply an amount or time based on industry practice.

When engaging other consultants either “for and on behalf” of your client or for yourself, also consider the following:

- If you are engaging a consultant “for and on behalf” of your client, make sure that you have your client’s written authority to engage a consultant that wants to limit its liability.
- If a consultant you are engaging “for and on behalf” of your client wants to limit its liability make sure you draw this fact to your client’s attention and suggest that they seek legal advice regarding its implications. It would be prudent to have documentary evidence (file note, email, letter, etc.) to be able to prove that your client was aware of the limitation.
- If you are engaging your own sub-consultants, refuse to allow them to limit their liability, as limitation of liability clauses in sub consultancy agreements activate the waiver of rights exclusion² in your professional indemnity insurance policy which will lead to uninsured liability for the amount exceeding the limitation.
- If one of your sub-consultants wishes to be engaged by referring to industry standard conditions, make sure that you request a copy and take legal and insurance advice on any limitation clause that may be contained in the terms.

Summary

There are two schools of thought:

- Limitation of liability clauses make commercial sense as they provide the contracting parties with greater certainty as to what losses can be recovered.
- Limitation of liability clauses should be prohibited as they allow a party who has been reckless and negligent to limit the time proceedings can be brought against them and the amount recoverable from them.

Appreciate therefore that these conflicting views exist when negotiating limitation clauses into your own agreements and out of other consultants’ agreements!

Further Reading

We refer you to our Risk Rules on Limitation of Liability Clauses and Liability for Sub Consultants, for further commentary.

Helen Johannsen
Risk Manager – Queensland and Northern Territory

¹Hyder Consulting (Australia) P/L v Wilh Wilhelmsen Agency P/L (2001) NSWCA 331
²Be aware that not all professional indemnity insurance policies contain a waiver of rights exclusion clause.

Project Specific Professional Indemnity Insurance

Most practices have one professional indemnity insurance policy that covers all types and sizes of projects. However practices engaged in medium to large projects have another option open to them regarding cover for the professional indemnity risks associated with a specific project.

Stand alone project specific policies may be arranged if a practice does not wish to include a project under its current professional indemnity insurance policy. A stand alone project specific policy is a totally separate professional indemnity policy and can be arranged on an annual or a multi-year basis. The benefits of such a policy are as follows:

- The project is isolated from the practice’s professional indemnity insurance policy. A separate premium is charged and the fees earned from the project do not have to be disclosed at renewal of the practice’s annual policy. This ensures that a double premium is not charged. Any claims that arise from the project will be paid out by the project specific policy.
- The premium payable is for the specific project only so the practice may be able to negotiate a contribution from the client.
- The project specific policy can be arranged with a higher limit of indemnity than carried by the practice and that limit is not shared with any other projects undertaken by the practice.
- A multi-year policy, usually arranged between five and ten years, provides additional levels of certainty and comfort. The full premium is paid upfront and the policy set up for a specific period. The policy is thereafter not subject to any annual review by insurers and therefore there are no premium increases in the event of a claim or a change in underwriting markets. The risk of a practice being unable to maintain cover on a commercially viable basis is therefore eliminated. Furthermore if the client agrees to contribute to the costs of the policy, the practice does not have to approach the client each year for the contribution.
- If the project is being carried out as a joint venture, more than one practice can be named as insured parties on the policy and the premium shared.

When considering whether a project specific policy may be appropriate it is important to note that:

- Insurers will generally only offer such insurance for significant projects.
- The annual premium payable for a project specific policy may be greater than the extra premium payable by the practice to include the project under its current professional indemnity policy.
- Multi-year policies are generally not renewable. If you require cover for the project to continue after the project specific policy expires, a new project specific policy would have to be taken out or the project noted under the practice’s current annual policy.
- The premium payable may result in it not being commercially viable for the practice to take out a project specific policy.

If you wish to discuss project specific insurance in more detail, please contact your Account Manager.

*Laurence Gottlieb
State Manager- Victoria*

Good Novations

In 2009, I helped develop “Guiding Principles for Balanced and Insurable Novation Deeds” for the Australian Institute of Architects.

Conceived out of discussions at the Victorian Large Practices Forum and with input from several national practices as well as the Institute, the document identifies some common pitfalls and necessary protections in the novation process. Its purpose is to support architects in their negotiations with clients and to educate clients who come to novation without the benefit of experience.

It is free to subscribers to the Institute’s “Acumen” service and can also be purchased as part of the 2005 document “Guiding Principles for Balanced and Insurable Client/Architect Agreements” from Knowledge Services at the Institute.

Covering similar subject matter and available at any time is our “Novation” Risk Rule, which is exclusively available to our insured practices. Contact your Account Manager for a copy.

*Wendy Poulton
Risk Manager – Victoria, South Australia and Tasmania*

New and updated Risk Rules

Our Risk Managers have been busy writing and updating the Risk Rules. The following Risk Rules are new for 2010:

- Continuity of Cover
- Public Liability Insurance
- The A to Z of Professional Indemnity Insurance

Our “Indemnities” Risk Rule has also had a major overhaul and the following Risk Rules have been updated to address emerging issues:

- Safe Design
- Electronic Documents Checklist
- Scope of Services

Please contact your Account Manager if you would like to receive any of the above Risk Rules.

Staff Updates

The NSW Branch is pleased to announce that Samantha Neilson, Contracts Advisor, NSW is due to give birth to her second child any time now.

Natalie Sullivan, Risk Manager – NSW/ACT/WA, has returned from her maternity leave and is now working 4 days a week providing contract reviews and risk management seminars to clients.

Don't forget to tell your insurers.....

A business can see many changes in a 12 month period. It is surprising how many insurance renewal reviews we complete with our clients where the end result is quite different to the previous year's cover. Whilst it is important to review and update your cover each year, you must remember to advise your insurer during the insurance period if any significant changes occur. The following list represents the more common changes we find businesses forget to advise their insurers of.

| Type of Insurance | Change |
|--|--|
| Business | Opening a new office location, change of address, purchase of new equipment (especially IT equipment), moving archive storage locations, upgrading office fit out, purchase of expensive art collections, change in the business description |
| General Property | Purchasing new laptops or portable phones and equipment |
| Travel | Booking unscheduled flights, travelling to countries where 'do not' travel warnings have been issued |
| Group Accident | Changes to insured staff members. (NB: Group accident policies cover listed employees only) |
| Landlords - Commercial | Changes to your tenants' occupation |
| Public Liability | Any new corporate entities, specific requirements by landlords or clients to be noted or other contractual requirements |
| Machinery | Installing new equipment e.g. Air conditioning (Have you signed a new lease that requires you to insure the air-conditioners?) |
| Professional Indemnity, Directors and Officers, Management Liability | Change in directors or principals, change in activities undertaken, new joint ventures, change in business name, mergers or acquisitions |
| Expatriate | Change in staff members and their families based overseas. (NB: Expatriate policies cover listed employees only.) |
| Business Interruption | Change in revenue figures |

It is not an exhaustive list, although our concern is that most changes potentially leave the business uninsured or underinsured which can be a major problem should a claim occur.

It is important to remember that your insurance policy is covering your business for the specific information detailed in the policy schedule. If any of this information changes during the insurance period and you don't notify your insurer then you leave yourself open to uninsured losses. If in doubt, call us and we can advise whether your insurer needs to be notified.

Vanessa Collins
Compliance Manager

STOP PRESS

A draft new edition of the Australian Standard Consultancy Agreement AS 4122 has just been released for public comment, to replace the current AS4122-2000. Comments can be made until 26 April 2010.

A copy of the document can be downloaded at:
<http://infostore.saiglobal.com/store/Details.aspx?ProductID=1390422>.



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