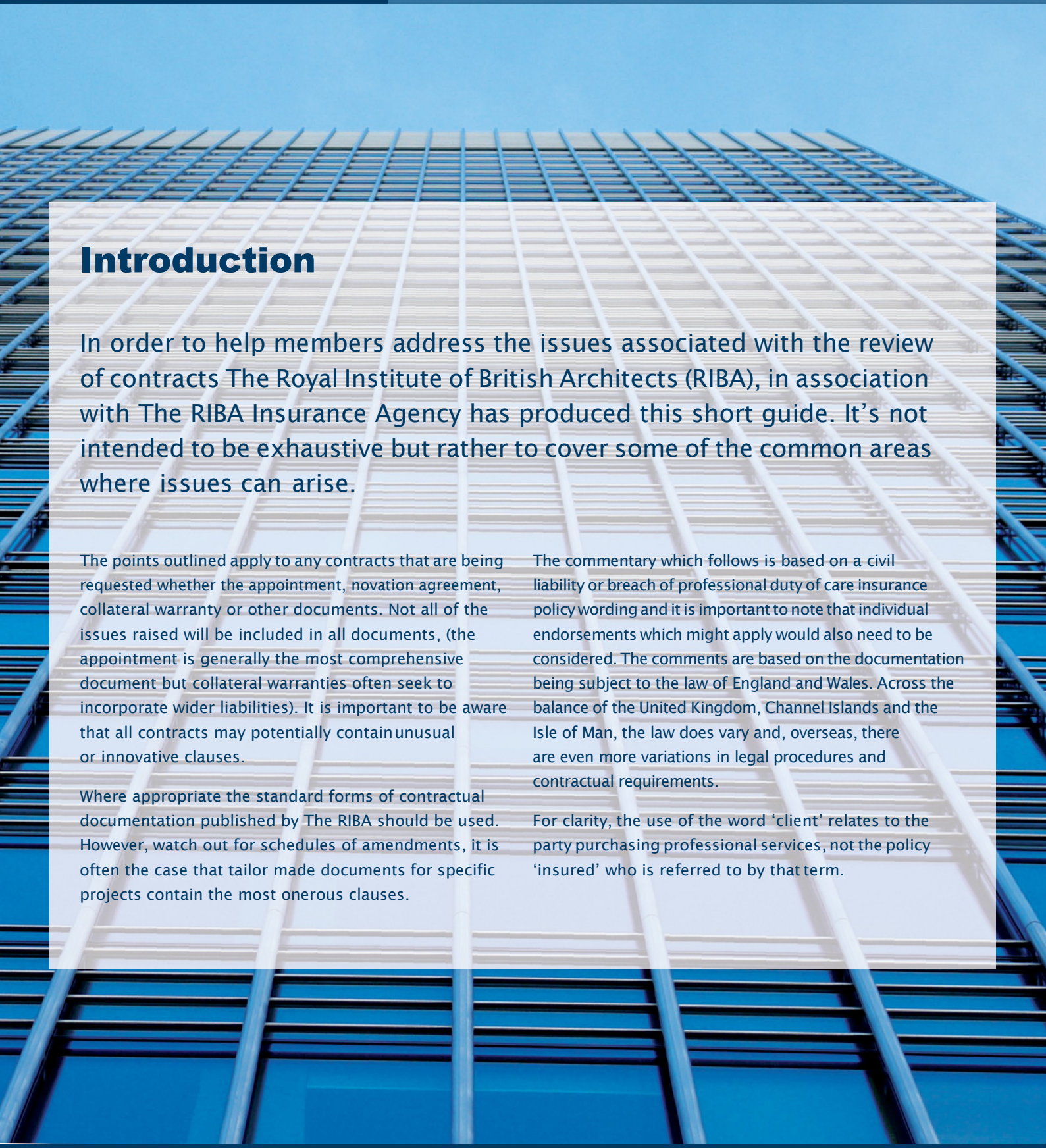
RIBA
INSURANCE AGENCY

Guide to Reviewing Contract Documentation



Introduction

In order to help members address the issues associated with the review of contracts The Royal Institute of British Architects (RIBA), in association with The RIBA Insurance Agency has produced this short guide. It's not intended to be exhaustive but rather to cover some of the common areas where issues can arise.

The points outlined apply to any contracts that are being requested whether the appointment, novation agreement, collateral warranty or other documents. Not all of the issues raised will be included in all documents, (the appointment is generally the most comprehensive document but collateral warranties often seek to incorporate wider liabilities). It is important to be aware that all contracts may potentially contain unusual or innovative clauses.

Where appropriate the standard forms of contractual documentation published by The RIBA should be used. However, watch out for schedules of amendments, it is often the case that tailor made documents for specific projects contain the most onerous clauses.

The commentary which follows is based on a civil liability or breach of professional duty of care insurance policy wording and it is important to note that individual endorsements which might apply would also need to be considered. The comments are based on the documentation being subject to the law of England and Wales. Across the balance of the United Kingdom, Channel Islands and the Isle of Man, the law does vary and, overseas, there are even more variations in legal procedures and contractual requirements.

For clarity, the use of the word 'client' relates to the party purchasing professional services, not the policy 'insured' who is referred to by that term.

General Issues

It may sound obvious but it is important to ensure that the contract is in writing and clearly defines the services to be provided. However, this is an area which is often the source of disputes, especially with clients that are not experienced in procuring professional services. In these circumstances, in the absence of written parameters, clients may expect to receive more than they are actually paying for.

You should also be satisfied that you are only undertaking to provide services which you are capable of delivering, in terms of both expertise and resources, or where you are sub-contracting the delivery of a service (or services) to specialist sub-contractor(s) or sub-consultant(s), that you have taken appropriate steps to ensure their competence. We return to this issue later in this guide.

It is also important to check that the parties signing the document are those that you expect. If a client suddenly changes its name, is there a reason and is the new organisation going to be responsible for paying any outstanding fees?

Specific Clauses

The order and title will vary between documents however the following are the most common forms.

1. Operative / duty of care clause

- This should require that the services are undertaken exercising the reasonable skill and care required in conformity with the normal standards of the insured's profession.
- The wording may extend to include 'reasonable skill, care and diligence'.

Watch out for wordings demanding higher levels of skill such as requests for 'professional' or 'expert' skill. Both can create a degree of liability that is higher than would otherwise be the case and a court is likely to view these as representing the 'highest standards of the profession' rather than those of a 'normal competent practitioner'.

Another danger is that this clause can seek to impose upon the insured the same responsibility as the contractor has, especially in design and build situations, which can lead to problems with fitness for purpose and other performance guarantees.

2. Authority levels

Make sure that the extent of your authority to act on behalf of the client is agreed. Include a statement, if appropriate, that the client's authority will be obtained before moving on to the next stage. Ensure that you adhere to the contractual agreement.

3. Appointment of other consultants

This is often an area that can cause problems. Ideally all appointments should be direct from the client but if this is not possible then you should ensure adequate due diligence is undertaken before you engage any consultant. Ideally this should include financial health checks, evidence of adequate professional indemnity insurance and relevant experience/expertise to undertake the required services.

Where you are appointing other consultants, their appointment must also be in writing and you must pass on the same obligations to the consultants as are required from you. This should be achieved by using an appointment such as the RIBA Sub consultant Professional Services Contract that provides back-to-back terms.

Consultants must also be required to sign collateral warranties and other supporting documents and we would recommend that they additionally sign a collateral warranty with the client to create a direct contractual link.

4. Materials clause

The 'deleterious materials clause', should only place an obligation on you to use reasonable skill and care not to specify for use in the project materials known to be deleterious at the date of specification. Ideally this should be in the form of an agreed list, or specified document such as 'Good Practice in the Selection of Construction Materials' issued by The British Council for Offices

An obligation, that may be included, is one of advising if you become aware of the use of materials that are deleterious. Here it is important to ensure that the obligation does not extend your site responsibility or require you to monitor the use of materials that are outside your usual professional expertise, if a material is specified in good faith, then you should have no liability either.

One further danger is that the clause might refer to materials specified that are known to be deleterious at the time of use. This is impossible to comply with even with an obligation to advise if materials change their status during a project.

Be vigilant for absolute clauses that could breach the performance warranty clause of your professional liability policy.

5. Cyber Liability

Professional indemnity insurance is generally not intended to respond to 3rd party liabilities that could arise from the transmission of computer viruses or similar technology based issues such as cyber-attacks. There has been a recent push by insurers to apply specific cyber exclusions. This has been triggered by concerns that some professional indemnity policies were taking on board cyber losses without really intending to cover these risks. Stand-alone Cyber cover should certainly be considered to mitigate such exposures.

6. Copyright / license to use documentation

You should take steps to ensure that you retain the copyright in all designs and documents that you prepare. Commonly, a license is included for to enable the use of the documentation for the intended purposes relating to the project but not for other sites or for the purposes of an extension to the development.

There may, however, be projects for organisations such as government bodies, where copyright is transferred for security reasons.

Keep watch for licenses that may be freely assigned, especially in collateral warranties.

Try to link any copyright license to the payment of the fees due to you.

7. Fees

Whilst fees are not directly a professional indemnity issue, disputes over fees often lead, in turn, to counter claims alleging that payment has been withheld because of a failure on your part.

In general, your fees need to be agreed within the contract which should also set out whether they are to be paid as a lump sum or on an instalment basis.

8. Professional indemnity insurance

This clause should include the provision that you will maintain professional indemnity insurance at an agreed specific limit of indemnity and for an agreed period, which should be either six or twelve years depending on how the contract is executed. The period should run from the date of practical completion of the development or the completion of your services whichever is the earlier.

Watch out for clauses that simply state that the limit should be 'adequate to meet the obligations under the contract' or similar, open-ended terms as, until a claim is quantified and ultimately settled, it is impossible to say that the limit is adequate.

Sometimes the clause will require that the limit is index linked. This is not a particular problem during periods of low inflation but longer term there could be issues if the rate of inflation increases.

The maintenance of insurance must be on the basis of it remaining at commercially reasonable rates and on typical terms and conditions prevailing in the insurance market to firms of a similar size/risk profile.

You should seek to define 'commercially reasonable rates' in your appointment and link it to the premium levels charged when you take the contract on. The definition should not state that increases caused by your claims record will be deemed as commercially reasonable.

The excess level is also sometimes defined. This can be an issue if a low level of excess is specified. If the subject is to be mentioned, then perhaps it should only be on the basis that you will maintain an affordable level of excess and pay it promptly when required by the policy terms and conditions.

Some contracts will seek to ensure that insurance is maintained either by the client having the right to take out cover and to recover the cost from you, or that the client will pay for the increased cost over the commercially reasonable level. In practical terms these are likely to be very difficult to obtain.

Another issue to watch for is a requirement that the client has a veto over any agreement you and your insurer wish to enter into regarding your policy. You must not allow any 3rd party to interference as to do so could compromise coverage in the event of a claim.

9. Liability periods

In the majority of cases in England and Wales, the liability under contract is either for a six or twelve year period depending on how the contract is executed.

Contracts entered into 'under hand', simple, signed contracts have a six year lifespan.

Traditionally, contracts entered into as a deed, were required to be executed 'under seal', however, with the decline in the use of company seals, deeds can now be signed.

One point to watch out for is that any collateral warranties or similar third party rights documents do not have a longer lifespan than the appointment as most professional indemnity policies exclude liability under collateral warranties which is longer (or wider) than the appointment.

10. Fitness for purpose / performance warranties

There can be serious problems where you accept specific liability for clauses which extend your liability to the level of giving guarantees. Typically a clause will be included in the policy excluding liability:

"…arising out of performance warranties, penalty clauses or liquidated damages clauses unless the liability of the insured to the claimant would have existed in the absence of such warranties or clauses."

Professional indemnity policies exclude claims arising from performance warranties (which include fitness for purpose clauses), penalty clauses and liquidated damages clauses unless your liability to the claimant would have existed in the absence of the clause.

11. Collateral warranties

Where appointments require these documents to be issued, the form they take must be agreed in principle before the commitment to enter into them is accepted. Otherwise, a commitment to enter into a warranty could lead to an onerous document being produced.

You should try to limit the number of warranties that may be required. A common way of doing this is by limiting them to the first purchaser, tenant or funder. The nature of the project should also be considered, especially in the case of residential developments.

Ensure that the collateral warranty includes a clause to make it clear that there is no greater liability under the collateral warranty than to the original client under the appointment. The RIBA recommends that members seek legal advice before entering into any form of collateral warranty.

12. Assignment or novation

Any transfer of any contract should be subject to prior consent and ideally, include a limit on the number of assignments and their purposes.

Appointments should only be assigned to a party which is taking over the project to see it through to completion, typically the contractor by novation, or to the funders by way of security.

Collateral warranties should only be assigned on a limited number of occasions. There is often a limit in the collateral warranty extension on the number of assignments – two is the most common figure.

Particularly in the case of the novation of your appointment, ensure that provision is made to make sure that all your fees are paid, either by the novation stating that it can only take place if all the fees due to date have been paid to you, or that the party to whom the contract is being novated accepts written responsibility for paying you all the fees that are outstanding at the date of the novation. Novation agreements of the ab initio type should be avoided, and the RIBA recommends that you seek legal advice before entering into any novation agreement. The CIC Novation Agreement, published by the Construction Industry Council, is a switch type novation agreement, and is the standard novation form recommended by the RIBA.

13. Economic and consequential loss

Ideally these should be excluded from collateral warranties or the extent of loss covered limit. The British Property Federation standard forms seek to restrict consequential loss.

14. Joint and several liability

Joint ventures and consortiums are generally excluded from cover unless they are specifically endorsed into the policy. The key concern surrounding any form of joint and several liability clause is that in such arrangements you might end up in a position where, as the only party still trading, you have to bear another parties liability.

15. Net contributions clause / liability cap

This is a way to limit liability and should be included in all contracts and collateral warranties. The aim is to restrict your liability to the proportion of the loss for which you are responsible and on the basis that all the other parties with design responsibility have been deemed to have paid their proportion as well. Some clients, especially commercial developers and their banks, will not agree to the inclusion of a net contributions clause.

A liability cap should be included in all documents whenever possible to restrict your liability to an agreed amount. Usually this is set at the same level as the insurance limit.

16. Jurisdiction clause

This clause must make it clear that the Law will govern the contract and the processes that will be followed. There should be some relevance between the Law applying to the contract and the details of the project. Commonly this will relate to the location of the project, the residence of the client or of the insured.

It is important to watch out for overseas jurisdictions. These may impose significantly higher obligations and also fall outside the scope of your policy cover. The USA, with its legal system, is of particular concern but there are also countries where there may be local insurance requirements.

17. CDM regulations

Watch out for clauses where you are asked to accept the client's responsibility. Under this legislation, this must remain with the legally required party.

18. Adjudication

The danger with this process is its speed and the possibility that the parties will not accept the adjudicator's decision. Professional indemnity policies require that the right of appeal is retained otherwise the decision of the adjudicator may fall outside the scope of the insurance.

It is also important to check your policy for the notification requirements relating to adjudication as these may not be in line with your contractual obligations.

19. Contracts (Rights of Third Parties) Act 1999

The recommendation is that the application of this Act should be deleted from all contractual documentation. The additional liability which it imposes is significant, with rights granted to third parties to enforce the contract and to use it in the event of a dispute.

If the Act applies, then collateral warranties should not be signed. These documents were the construction industry's answer to the problem created by the erosion of the Law of Tort, especially that of Negligence.

The Act allows parties to 'contract out' of it and all standard forms of contract include such a provision.

20. Pollution liability

Many insurance policies will include a restriction to an annual, aggregate basis or may have a sub-limit. Look out for pollution liability that extends your liability on this issue. Within this aspect, look carefully at any requirements relating to asbestos. This is generally a stand-alone clause in policies and is often excluded.

21. Policy exclusions

There are other exclusions which may affect the content of documents and all of these should be considered for particular contracts. These can include:

- War and terrorism. This is only a problem if the client is asking for an undertaking that you are taking such risks into account.
- Nuclear risks. These will be excluded under the policy. There is specific insurance available through a pooled insurance arrangement and such risks must not be passed on in the contract as they will not be covered under professional indemnity policies.
- Supply of products. Even if you are only undertaking the design you will also need to have a products liability for the physical aspects involved.
- Matters covered under other policies such as public and employer's liability.
- Acting as a contractor. Such projects will commonly be excluded, or indemnity limited, to avoid conflict of interest. The same is true of acting on the insured's own property.
- Fire Safety and Cladding – Since the fire at Grenfell and several other high profile fires, there has been a move by PI insurers to restrict or exclude fire safety and cladding from professional indemnity insurance policies. You should always bear in mind any limitations that apply to your policy when considering the contractual terms and conditions, and seek to exclude as far as possible liability that falls outside the scope of your policy. In the current insurance market conditions it may be advisable to recommend to your client that they directly appoint a fire engineer for all fire related aspects of the project.

Important note:

The above is intended as a guide to the more common areas where issues can arise that may lead to claims which might not be indemnified or cover restricted. The RIBA Insurance Agency wishes to make it clear that our advice is given in our role as insurance brokers and that legal advice should also be obtained.

For the avoidance of any doubt, the professional indemnity policy conditions will always take precedence so in the unfortunate event that liability arises, the applicability of cover will be determined by the policy terms, conditions, exclusions and limitations in force at the time of notification to insurers.

The RIBA & RIBA Insurance Agency welcome your feedback and would welcome your views on how this guidance might be improved and expanded. The RIBA Insurance Agency provides advice on contractual matters and publishes articles on its website: www.architectspi.com

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