

## LILLEHAMMER: 'COVERAGE INTENT' PANEL, 7<sup>th</sup> MARCH 2013 – GARY SWINNERTON

### **“What do I believe the Contractor has bought?”**

The Contractor has bought an intangible product recommended by a Broker and underwritten by an Insurer promising to pay claims as per the agreed contract terms and conditions.

There are many stakeholders relying on the insurance cover purchased by the Contractor – for example, at a construction stage there is the Client, Fabrication Yard, Suppliers, Contractor and possibly Lenders.

### **“What does a successful claim look like?”**

The Insurer indemnifies the Contractor in a timely manner and meets their joint expectations.

### **“What are the ingredients for a successful claim?” 3C's**

(1) CLARITY - what is the policy covering?

(2) CERTAINTY - how does the policy respond?

and, if I may add, beyond the specific topic of 'coverage intent' itself

(3) CONSENT - “Treating Customers Fairly” approach with a smooth/speedy claims process.

With Broker support a Contractor has to adequately demonstrate a loss to be caused by an insured peril and costs/expenses to be reasonably incurred – all to the satisfaction of the Insurer (in consultation with his Underwriter) and following recommendation by a nominated Loss Adjuster, together with possible input from other experts.

### **Corrosion**

Corrosion is an inherent vice and will occur gradually under normal conditions. Accordingly a Contractor safeguards as best as he reasonably can:

- At a design stage a Contractor aims to protect against or allow for corrosion, examples being epoxy-based coatings; sacrificial anodes or impressed current cathodic protection; appropriate materials selection; plus material thickness adequacy and consistency.
- At an operational stage a Contractor aims to prevent and detect/monitor corrosion through a robust programme, examples being ROV inspection, thickness gauging, painting, coupons analysis – all done regularly as per industry standards (as a minimum).

In completing his work a Contractor strives to exercise due diligence, comply with legal requirements and perform according to a QA/QC system. Accidents do happen though and this is one of the reasons why a Contractor purchases insurance in the first place:

eg, incorrect installation/application or failure of equipment/processes can bring on the early onset or acceleration of corrosion.

A Contractor wants to insure against fortuity and its consequences. Equally, an Insurer does not want to insure inevitability. So, how do these expectations translate in policy wordings?

### **Coverage Intent**

1. WELCAR 2001 'Exclusion' - “costs of repairing/correcting/rectifying ... rust and oxidisation”
2. WELCAR Revised 'Exclusion' - broader, reference to *gradual* causes “rusting, oxidisation”
3. Institute Clauses for Builders' Risk 1988 – no reference (latent defect cover)
4. Norwegian Plan - Chapters 12/18 Inadequate Maintenance “costs in renewing/repairing part(s) in a defective condition as a result of wear and tear, **corrosion** etc”
5. Institute Time Clauses Hulls 1983/87 with Additional Perils Clauses – no reference: (Latent defect cover). Part causing loss or damage to Vessel and loss or damage to Vessel caused by negligence, incompetence or error of judgement.
6. Marine Insurance Act 1906 Section 55 refers to ordinary wear and tear, inherent vice etc. being excluded.

## *Ways Forward*

Referring back to the opening comments:

### Insured Peril

Contractor is to 'adequately demonstrate' (i.e. on the balance of probabilities) operation of an insured peril. [Conversely, the Insurer is to prove the exclusion]. Corrosion can be viewed here as the effect, not the cause.

- **Why not use the word 'corrosion' and, if an Insurer already does, then qualify it?**

eg, Exclusion: 'ordinary or gradual corrosion of any kind'

Insured Peril: 'accidental', 'unintended', 'unexpected', 'extraordinary' or 'accelerated' corrosion

Evidence of specific text within the policy wording is useful to understand the extent of cover and to help manage expectations of the various interested parties.

### Clarity / Certainty on Cover

- **Cover for 'other physical damage' consequences? Yes**

Eg, cover for collapse on unit/vessel, other than corroded items causing the collapse.

- Is 'defective part' restricted to the corroded item per se?

(Impact on common/concurrent repair costs split for corroded items & rest of unit/vessel).

Does the policy cover damage in the nature of corrosion arising from an insured peril eg, crew negligence allowing salt water into a heat exchanger?

- **How does Defective Part Exclusion Buy Back cover apply in relation to corrosion?**

Cover for defective parts is subject to the same policy conditions as other physical assets.

- **If there is doubt here, is it appropriate to consider a LEG 1/2/3 equivalent?**

1 out-right defects exclusion / 2 consequences-style wording / 3 wider 'full defects' style.

### Consent

- **'indemnify in a timely manner'**

Is it feasible to jointly appoint a common expert with agreed terms of reference [eg, root cause / differentiation between ordinary and accelerated corrosion] at the outset if we all know that such claims are likely to be problematic?