



CONTRACT REVIEW TRAINING SERIES

PART 3

Risk, Indemnities and Consequential Loss



Presented by Greg Henry
Principal, Turtons Lawyers

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WHAT COULD GO WRONG?

WHAT COULD YOU BE LIABLE FOR?

LIABILITY FOR ECONOMIC LOSS

HOW TO QUANTIFY YOUR EXPOSURE TO UNINSURED LOSS

HOW TO FORMULATE A STRATEGY

NEXT STEPS

What could go wrong?

- The works do not function as intended.
- The works are damaged during construction.
- Other property is damaged during construction.
- Someone is injured during construction.
- The project is late.
- Something else bad happens.



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Repair Costs

Medical bills

Economic losses
(loss of use, loss of production, loss of profit, etc)



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**Contractors are most concerned about liability
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**Contractors are most concerned about liability
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When can you be liable for economic loss?

What types of loss are covered by your insurance?



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**When can you be liable for
economic loss?**

Normal loss

The kind of loss that every person in a like situation will suffer.

Special loss

Anything other than the normal loss if the loss 'may reasonably be supposed to have been in the contemplation of both parties, at the time they made the contract, as the probable result of the breach of it', including any special circumstances made known at the time of entering the contract.

Hadley v Baxendale (1854) 156 ER 145;

Environmental Systems Pty Ltd v Peerless Holdings Pty Ltd (2008) 19 VR 358.



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Scenario 1


A contractor is engaged to install a new item of major plant to replace an existing one.


The new plant will have lower running costs than the existing one.


The plant is defective.




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WHAT COULD GO WRONG?	<h2>Scenario 1</h2> <p>The client claims:</p> <ul style="list-style-type: none"> (a) the cost of labour deployed to try to fix the problem; and (b) the costs of having to use the old plant until the defects were rectified. <h3>What can the client claim?</h3> <p>(Assume there is no consequential loss exclusion.)</p>
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WHAT COULD GO WRONG?	<h2>Scenario 1 Answer:</h2> <h3>(d) Both (without an exclusion clause).</h3> <p><i>Peerless Holdings Pty Ltd v Environmental Systems Pty Ltd [2006] VSC 194</i></p>
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WHAT COULD GO WRONG?	<h2>Scenario 2</h2> <p>A head contractor is appointed to roll out home insulation under Government scheme.</p> <p>It subcontracts part of the works.</p> <p>The subcontractor causes a fire.</p> <p>The head contractor's contract is cancelled and it sues the subcontractor for loss of profit.</p>
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WHAT COULD GO WRONG?	<h2>Scenario 2</h2> <p>Can the head contractor claim for loss of profit?</p>
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Scenario 2 Answer:

(b) No.

Stuart Pty Ltd v Condor Commercial Insulation Pty Ltd [2006] NSWCA 334


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Because the principles are so general, it's difficult to predict how the rules will be applied.


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Talking in abstract terms doesn't help.

'Normal loss', 'Consequential loss', 'indirect loss', 'special loss', 'the second limb of Hadley & Baxendale' etc.

Talking about specific risks and examples makes things easier.

What happens 'if we're late', 'if the works are damaged', 'if we damage other property', etc.


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The risk of claims for economic loss is highest on 'one of a kind' projects where a default can have immediate economic consequences.

Production facility for a commercial enterprise
v
Recreational landscaping works for a Council


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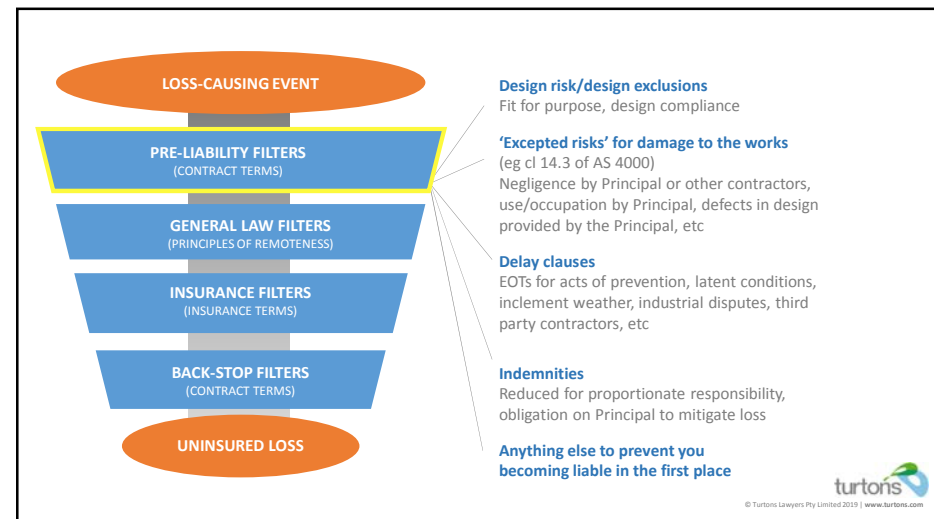
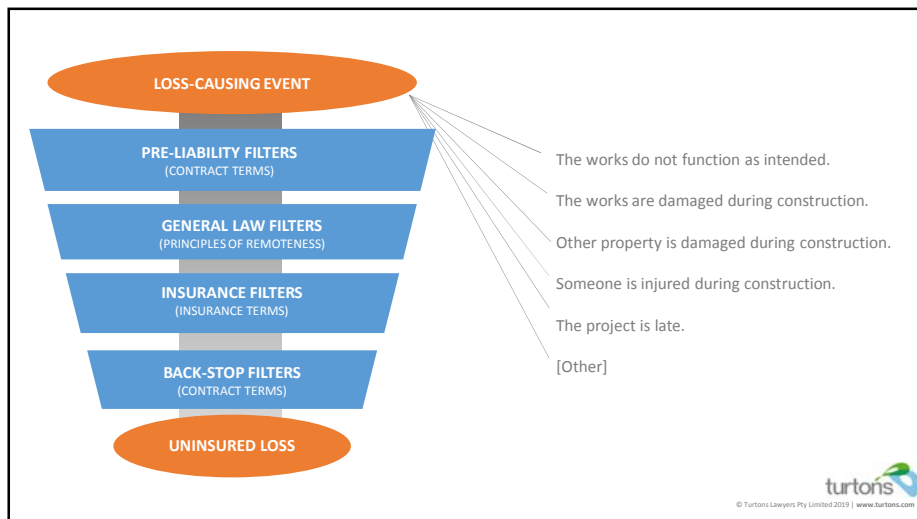
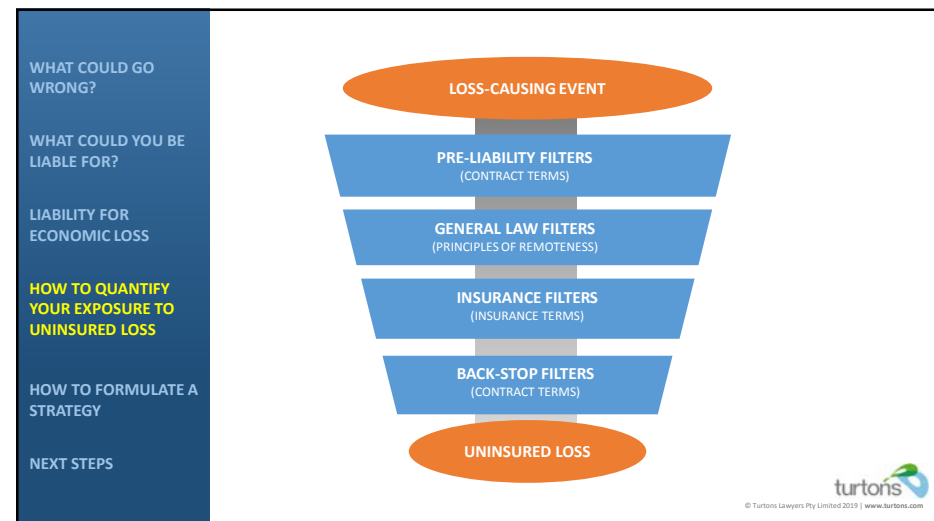
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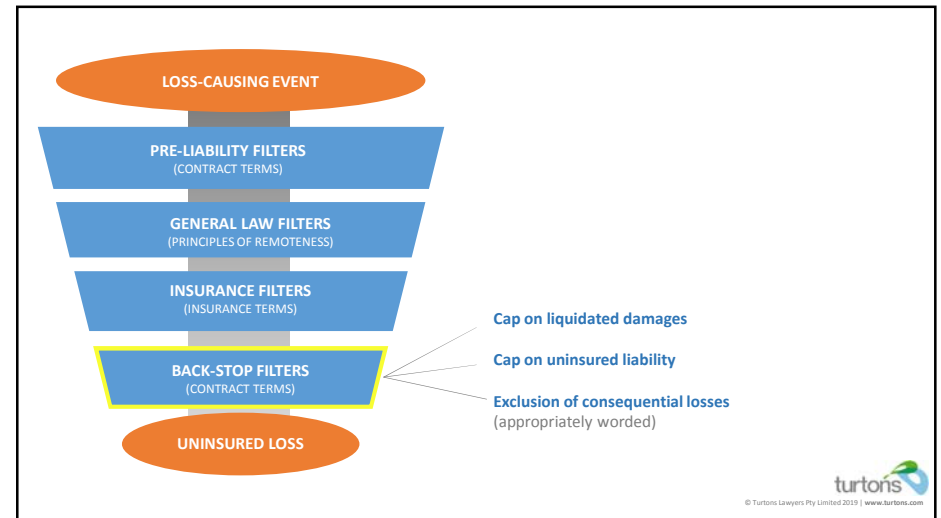
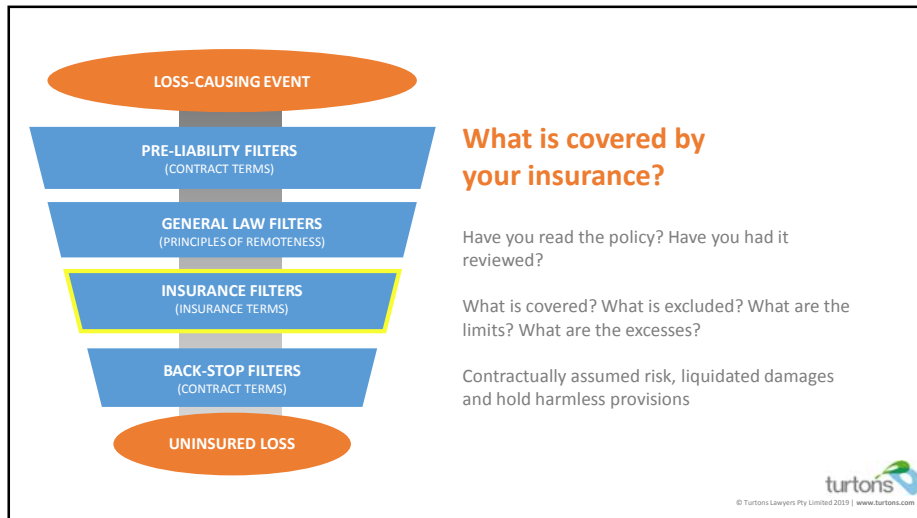
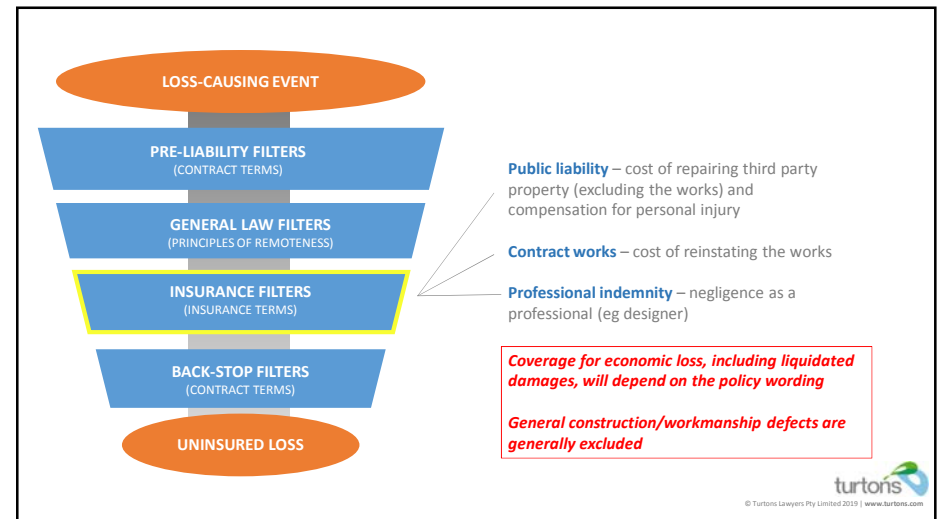
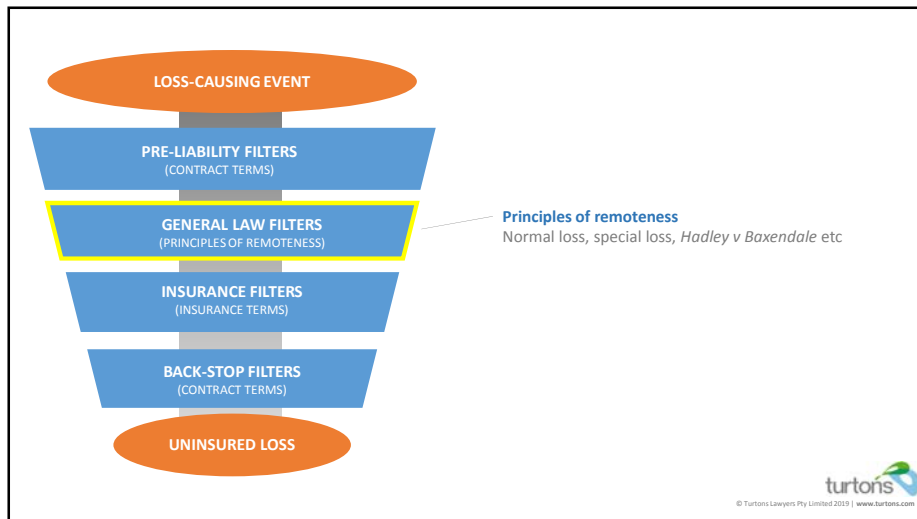
NEXT STEPS

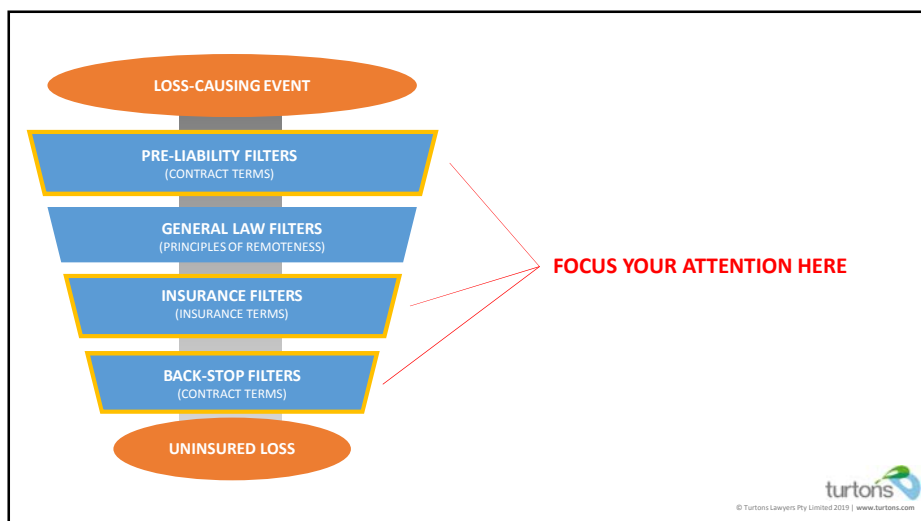
The best way to regulate your liability is through a structured approach.



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Sample Risk Matrix

What could go wrong?	The works do not function as intended	The works are damaged during construction	Other property is damaged during construction	Someone is injured during construction	The project is late	Other
What's our potential exposure	Repair Costs Economic Losses	Repair Costs Economic Losses	Repair Costs Economic Losses	Medical Costs Economic Losses	Repair Costs Economic Losses	Other Costs Economic Losses
Pre-liability filters <small>Contract Terms</small>	Exclude fit for purpose/ design risk	'Excepted risks'	Indemnities, excepted risks	Indemnities, excepted risks	Qualifying causes of delay	?
General law filters <small>Principles of Remoteness</small>	[No Action Required]					
Insurances filter <small>Insurance Terms</small>	PI insurance	Contract works insurance	Public liability insurance	Public liability insurance	(See left)	?
Back-stop filters <small>Contract Terms</small>	Caps & Exclusions	Caps & Exclusions	Caps & Exclusions	Caps & Exclusions	Caps & Exclusions	?
What's our residual, uninsured exposure?	?	?	?	?	?	?

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The Ideal Contractual Approach

1. You can claim additional money and/or time for anything outside your control.
2. You're not exposed to liability for any loss caused by someone else.
3. You're not exposed to any risk that could potentially destroy your company.

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For example...


1. There is reasonable relief for delays (EOTs).
2. All indemnities, risk and care of works provisions are qualified and the usual list of 'excepted risks' applies.
3. There is otherwise no liability for anything outside your control.
4. Liquidated damages are capped.
5. 'Consequential loss' (appropriately worded) is excluded (eg loss of profit, loss of production, loss of use, pure economic loss etc).
6. Your aggregate, uninsured liability is capped.

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The ideal contractual approach may not always be commercially viable.


Not winning contracts has its own risks.


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How do you deal with one-sided contracts and/or unsophisticated clients?

1. Make sure you understand the issues yourself.
2. Be ready to explain the issues in simple terms.
3. Take a tailored approach to tender assessments – focus on what’s most important.
4. Be selective about your tender qualifications.
5. Pay close attention to how you qualify your tenders.
6. Seek help if you’re not sure about your approach.


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If the ideal approach isn’t viable, focus on what’s most important.

What could go wrong?	The works do not function as intended	The works are damaged during construction	Other property is damaged during construction	Someone is injured during construction	The project is late	Other
What’s our potential exposure	Repair Costs Economic Losses	Repair Costs Economic Losses	Repair Costs Economic Losses	Medical Costs Economic Losses	Repair Costs Economic Losses	Other Costs Economic Losses
Pre-liability filters <small>Contract Terms</small>	Exclude fit for purpose/ design risk	“Excepted risks”	Indemnities, excepted risks	Indemnities, excepted risks	Qualifying causes of delay	?
General law filters <small>Principles of Reasonableness</small>	[No Action Required]					
Insurance filter <small>Insurance Terms</small>	PI insurance	Contract works insurance	Public liability insurance	Public liability insurance	(See left)	?
Back-stop filters <small>Contract Terms</small>	Caps & Exclusions	Caps & Exclusions	Caps & Exclusions	Caps & Exclusions	Caps & Exclusions	?
What’s our residual, uninsured exposure?	?	?	?	?	?	?


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Key Takeaways/Next steps

Take the time to map out what could go wrong.


Make sure you understand your insurance.

Set an internal policy around your contractual approach to economic loss.

Use checklists or forms to implement your policy.

Make sure the contracts you sign reflect your policy.

Seek help if you’re in doubt.


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