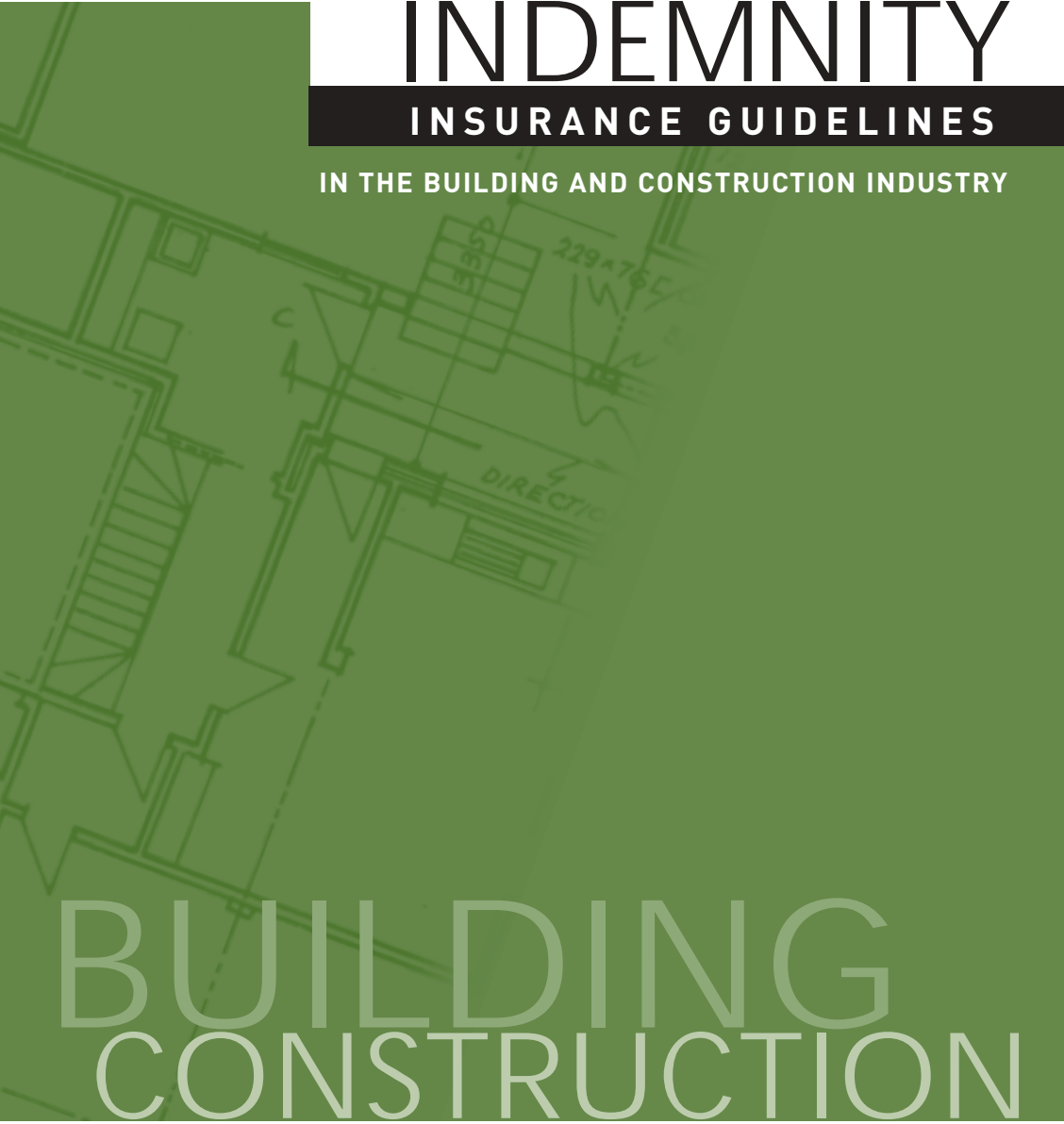




PROFESSIONAL INDEMNITY

INSURANCE GUIDELINES

IN THE BUILDING AND CONSTRUCTION INDUSTRY



BUILDING CONSTRUCTION

Australian Procurement and Construction Council Inc

PROFESSIONAL INDEMNITY INSURANCE GUIDELINES IN THE BUILDING AND CONSTRUCTION INDUSTRY

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PROFESSIONAL INDEMNITY INSURANCE GUIDELINES



INTRODUCTION

These Guidelines have been prepared by the Australian Procurement and Construction Council (APCC) to assist Australian, State and Territory government agencies to determine the level of Professional Indemnity Insurance (PII) which may be appropriate to the services they require from consultants in the building and construction industry.

The availability and affordability of Professional Indemnity Insurance to support project procurement is no longer guaranteed given the condition of insurance markets around the world. Insurance therefore needs to be regarded as a limited resource. These Guidelines are intended to assist Government clients (principals) to identify an appropriate level of insurance to be held by consultants (refer Sections 1 and 2).

The Professional Indemnity Insurance Guidelines

- Are intended to guide government agencies and public organisations involved in the procurement of hospitals, schools, custodial facilities, design services, non-construction, project management, etc, however this does not preclude them from being used in the private sector;
- Relate to Professional Indemnity Insurance only and do not refer to other liability issues;
- Recognise that for particular activities (e.g. asbestos, toxic mould and terrorism) insurance may not be available and that Government clients may need to accept some of the risk; and
- Recognise that some special cases may require other arrangements.

- ***These guidelines only deal with Professional Indemnity Insurance and have not attempted to address some of the broader issues such as: Principal Controlled Professional Indemnity Insurance, Professional Standards Legislation and Limit of Liability.***

- ***The guidelines will be reviewed in twelve months.***

DISCLAIMER These guidelines are subject to the impact of the proposed Professional Standards Legislation to be enacted nationally and may require review in relation to any schemes administered there-under.



1. THE LEVEL OF COVER

Two approaches are presented to indicate the suggested level of cover:

- A Simplified Method; and
- A Risk Assessment Based Method

The Simplified Method is considered appropriate for simple, non-construction related consultation and all projects under \$1million. More complex projects due to the type of construction, technology or environment in which they are constructed may warrant the use of the Risk Assessment Based Method.

1.1 Simplified Method

This method is considered appropriate for projects that agencies consider *conventional non-construction* consultancies and for all conventional projects, (including all projects up to \$1 million) undertaken in the civil engineering and building industries.

It is suggested that the amount of Professional Indemnity Insurance (PI Insurance) per event and in the aggregate, to be provided for typical projects by the consultant to the principal should be the greater of \$1 million or ten times the fee.

1.2 Risk Assessment Based Method

This approach addresses particular risks associated with both the project type and the nature of the professional services being provided. The process suggested is as follows:

- Use the Project Risk Assessment to identify overall project risk (refer section 1.2.1)
- Use the Professional Service Risk Assessment to identify service risk (refer section 1.2.2)

The methodology outlined in the Australian and New Zealand Standard AS/NZS 4360: 1999 Risk Management, provides guidance on these issues. Using Appendix E of AS4360 as a guide, a risk may be categorised in the following terms: extreme, high, moderate and low. On complex or large projects, it is recommended that the risk assessment be carried out in accordance with the Australian and New Zealand Standard.



1. THE LEVEL OF COVER

1.2.1 Project Risk

Projects need to be assessed to identify the overall project risk and may be thought of in the following terms. The risk descriptor may vary by project depending on the level of complexity and criticality to the project, e.g. acoustic design¹. See Addendum A for a comprehensive list.

Risk Descriptor	Definition	Examples
Extreme (E)	Immediate action required	Repair of collapsed bridge, pollution clean up, contamination, asbestos removal, oil or gas fire
High (H)	Senior management attention needed	Tunnels, marine works, mining, nuclear reactors, temporary structures, certain design services
Moderate (M)	Management responsibility must be specified	Pipelines, regulatory codes & requirements, road & rail infrastructure, bridges, demolition (M/H) , project management, design e.g. hospitals
Low (L)	Managed by routine procedures	Non-construction, conventional structures, training manuals, interior & landscape design, planning studies

In carrying out a risk identification and analysis in accordance with the AS/NZ 4360 Risk Management Standard to identify the risk inherent in a project, each risk may be considered and defined in terms of consequences. Each agency will have a different view on the nature of risk associated with projects. Some examples are as follows:

	Extreme	High	Moderate	Low
Site	Unstable	Significant settlement	Minor settlement	Innocuous, stable
Natural Environment	Threatened	Very sensitive	Managed co-existence	Innocuous, unmanaged
Technology	Experimental	Innovative or new	Innovative application	Routine application
Function	Essential for life	Essential with <12 hr	1 Week interruption	Non essential
Reliance	>100,000 people per day	20,001 to 100,000 people per day	1,000 to 20,000 people per day	>1,000 people per day

¹Please note for building and construction projects, terms are defined in Appendix E Table E3 in the AS/NZ 4360:1999



1. THE LEVEL OF COVER

1.2.2 Service Risk

The principal is also exposed to risks associated with the service provided by consultants. It is suggested that an analysis of the service risk be undertaken in a similar manner as for the project risk recognising that services risk may vary amongst agencies.

In looking at a particular project, the risk associated with each consulting service may be analysed and the risk profile identified. An example follows:

Risk Descriptor	Activity	Service Type
Extreme	Fire protection engineers, Water treatment	Due Diligence Work
High	Geotech & Mining engineers, Cost Estimating (L/H) (<i>refer footnote</i>)	Cost Estimating, Construction Management
Moderate	Civil, Structural & Mechanical engineers, Design, Building surveying (M/H)	Design & documentation, construction planning, Fabrication Schedule, QA
Low	Architecture, Planning, Project management (L/M)	Studies, Concept Design, Asset Management

Footnote: Level of risk to be determined on a case-by-case basis, for example availability of time and information and the cost risk manager. Cost management is a high risk activity and related services are provided by a range of professionals including Quantity Surveyors. Quantity Surveyors provide a low risk methodology to manage cost risks.

On major projects it is suggested that a more detailed assessment of the risk in the delivery of the service be made part of the principal's procurement and selection procedure of the consultants. In considering the various issues relating to the service or role to be undertaken by the consultant, a principal might identify the risks as follows:

	Extreme	High	Moderate	Low
Client Staff Expertise & Resources				
Consultant's Skills				
Consultant's Experience				
Consultant's Resources				
Consultant's Systems				
Technology				
Cost				
Program				
Building Project Delivery				
Infrastructure Project Delivery				

See Addendum A



1. THE LEVEL OF COVER

Based on this assessment it is suggested that principals form a view as to the risk profile of each service they wish to procure. See Addendum A for examples.

1.3 Amount of Cover

Having identified the project and service risk, the use of the tables in Addendum B will determine the amount of PI Insurance cover required for the project, exclusive of legal cost.

The tables will indicate an amount in a range of \$1 million to \$10 million (exclusive of legal cost) with intermediate amounts of \$2 million and \$5 million in line with industry practice.



2. POLICY TERMS

A Professional Indemnity Insurance policy is what is called a '*claims made*' policy, which means that, generally speaking, it covers claims made or deemed to be made during the currency of the policy. The claims can relate to circumstances or events that occurred during or before the period of currency of the policy. However, some policies may limit the retroactive operation of the policy.

A claims made policy is to be contrasted with an event occurrence policy such as a Public Liability policy that covers claims no matter when they are made in respect of events that occur during the currency of the policy.

PI Insurance is usually purchased as an annually renewable policy covering the consultant's operations as a whole as distinct from a specific project.

The guidelines below on excess, duration, exclusions etc. apply to normal annually renewable policies.

Single project PI Insurance is available in limited circumstances and needs to be negotiated individually in all aspects including excess, duration, exclusions etc.

2.1 Excess

It is suggested that the maximum excess be stated as the higher of \$50,000 or 2% of the consultant's gross fee turnover.

There should also be scope for a consultant to negotiate a higher excess where acceptable self-insurance arrangements are in place, for example, appropriate captive insurance arrangements for example, a captive insurance facility that satisfies regulatory and reporting requirements in the relevant jurisdiction.

2.2 Duration of Cover

Because PI Insurance is purchased as an Annual Policy, renewal has never been guaranteed.

In the past, consultants attempted to qualify any contractual requirement to maintain PI Insurance for more than 12 months by stating they would maintain the PI Insurance for the stated period of time as long as the insurance continues to be available at a reasonable cost. Government clients increasingly reject this qualification.



2. POLICY TERMS

It is suggested that government contracts nominate a period following completion of the services under the contract as the default period for which consultants contract to maintain the specified level of PI Insurance for any engagement, for as long as that insurance is available to consultants in the market on reasonable terms. These terms are to take account of the future market for insurance including factors such as the cost and availability of insurance for certain services.

2.3 Cover and Exclusions

An acceptable PI policy must indemnify the consultant against any liability for breach of professional duty and provide general cover for liability arising out of the conduct of the professional business under the Commonwealth Trade Practices Act and the relevant State or Territory Fair Trading Acts. The scope of the cover should include property damage, economic loss and death or bodily injury arising out of the conduct of professional business.

In relation to exclusions, each consultant should be required to declare:

- Any activities forming part of the engagement that are not covered by the policy e.g. asbestos removal; and
- Whether there are any and what liabilities are created by the proposed terms of engagement that are excluded or are not covered by the consultant's Professional Indemnity Insurance.

These matters are to be set out by the consultant as appropriate and notification given by the consultant to the client.

2.4 Evidence of Insurance

Acceptable evidence of Professional Indemnity Insurance is a current certificate of currency presented by the consultant as issued by an underwriter or insurance broker.

The certificate should specify:

- Name of the insured
- Policy number
- Expiry date
- Name of the insurer
- Level of cover in the aggregate (exclusive of legal cost)
- Policy excess
- Summary of the cover provided
- Jurisdictional and territorial limits



3. PRINCIPAL CONTROLLED

PROFESSIONAL INDEMNITY INSURANCE

Recognising the limit in availability and lack of certainty for principals in relation to the insurance contract terms of the consultants, the principal may wish to consider initiating insurance policies themselves. These policies may cover either all consultants involved in an individual project or those involved in a program of projects. In these models, the principal has control over the determination of the scope, excess, etc of the insurance policy.

Such a system may relieve the principal from the requirement to check the currency and policy cover of individual consultants except where a basic level of insurance is provided by the consultant.

As public sector principals are believed to have a lower level of events leading to claims on consultants' PI policies compared with commercial sector clients, this should be reflected over time in the premium cost for such policies. The lower level of events reflects the other risk management processes that public sector contract principals have in place such as pre-qualification of suppliers and well established contract procedures.

The ability to obtain such insurance will vary with the insurance market and be very much dependant on the insurance program structure. It is understood that Principal Controlled Professional Indemnity Insurance for large projects may be currently obtainable and as the demand for such policies gathers momentum, program or program periodic should become available.

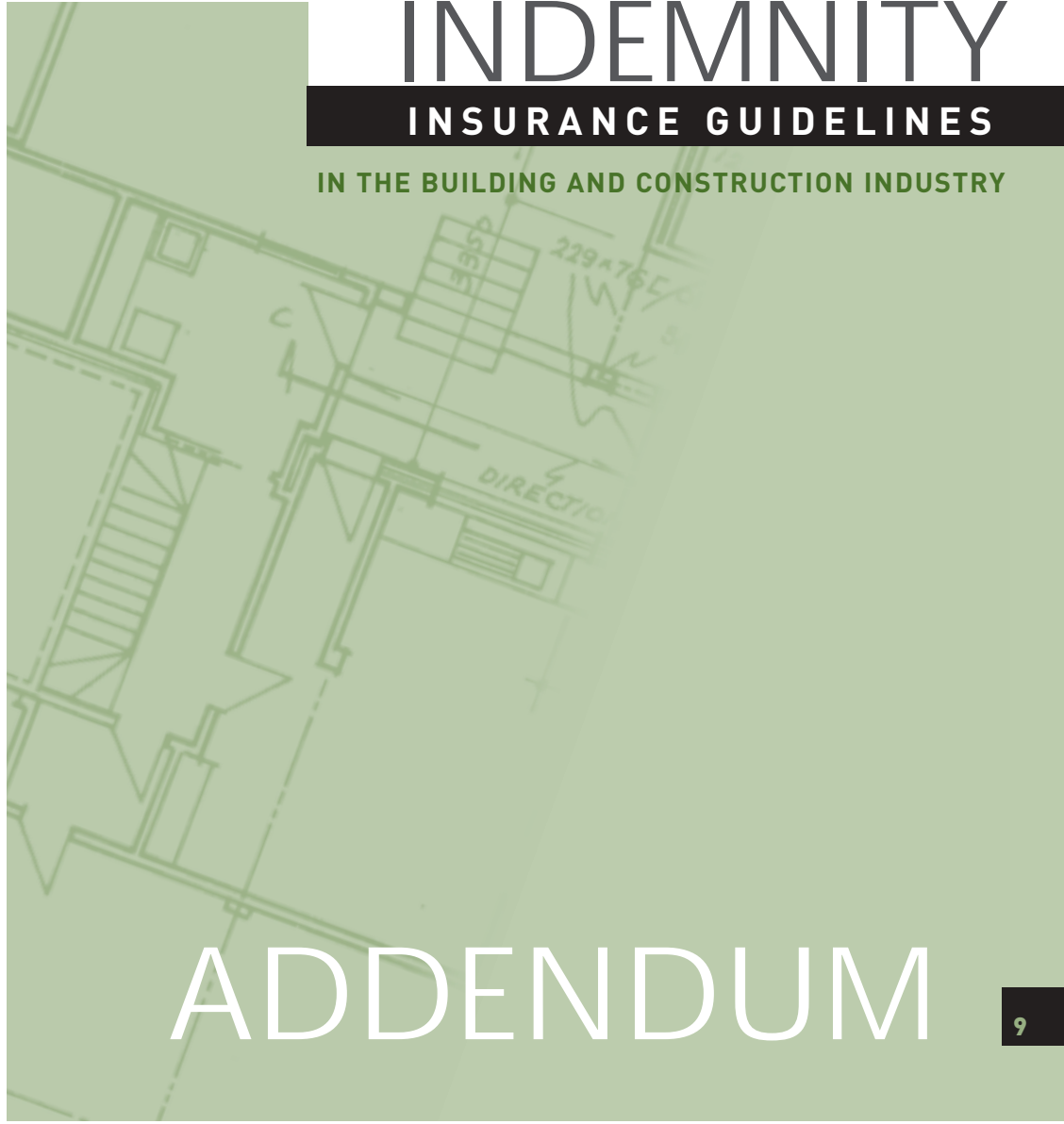
The APCC proposes to further investigate the viability of Principal Controlled Professional Indemnity Insurance schemes for Governments.



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ADDENDUM



ADDENDUM A

Project Risk Assessment Guide

Risk Descriptor	Definition	Examples
Extreme (E)	Immediate action required	Repair of collapsed bridge, pollution clean up, contamination, asbestos removal, oil or gas fire suppression
High (H)	Senior management attention needed	Tunnels on unstable sites, marine works, mining, nuclear reactors, temporary structures, hazardous chemical design services
Moderate (M)	Management responsibility must be specified	Pipelines, regulatory codes & requirements, road & rail infrastructure, bridges, demolition (M/H), project management, design e.g. hospitals, schools, housing, temporary structures
Low (L)	Managed by routine procedures	Non-construction, conventional building structures, training manuals, interior & landscape design, planning studies, maintenance & cleaning contract, asset management, concept design, acoustic design (L/H project dependent)

ADDENDUM A

Professional Service Risk Assessment Guide for Major projects

	Extreme	High	Moderate	Low
Client Staff Expertise & Resources	None	General expertise and limited resources	High level expertise and limited resources	High level of expertise & adequate resources
Consultant's Skills	Does not usually operate in the field	General skills in the field	Recognised skills in the field	Recognised leader in the field
Consultant's Experience	None in last 5 years	Experience in related fields in last 5 years	Relevant experience in last 5 years in single projects for multiple clients	Recent and current relevant experience in multiple projects for multiple clients
Consultant's Resources	Project requires 100% of company's resources	>20% of company's corporate resources & >50% local resources	>10% of company's resources & >20% local resources	<10% of company's resources & <20% local resources
Consultant's Systems	New systems to be developed to manage services of the type to be provided	Multiple systems to be integrated into a new system to manage services of the type to be provided	Existing proven systems to be tailored to manage services of the type to be provided	Existing systems proven on numerous projects to manage services of the type to be provided
Technology	Experimental Analysis & Design Methods	Application of New Design & Analysis Methods	Innovative Application of Known Design & Analysis Methods	Routine Application of Known Design & Analysis Methods
Cost	Lump sum fees dramatically under authority budget	Lump sum significantly under authority budget	Time plus expense basis fees to upper limit or Lump sum fees >75% of authority budget	Time plus expense basis fee
Program	Delays in consultant's service could jeopardise project	Delays in consultant's service could cost more than 20% of project budget	Delays in consultant's service cost more than 5% of project budget	Delays in consultant's service cost less than 5% of project budget
Building Project Delivery	Alliance	Guaranteed Maximum Price	Design & Construct	Traditional Delivery or Construction Management
Infrastructure Project Delivery	Build, Own Operate & Transfer	Design, Construct & Maintain or Design & Construct	Traditional Delivery	Construction Management



Risk Assessment Based Model

Suggested amount of Professional Indemnity Insurance Cover for range of Project Risks and Service Risks:

Project Risk Low					Project Risk Moderate				
Project Value	Service Risk				Project Value	Service Risk			
	Low	Moderate	High	Extreme		Low	Moderate	High	Extreme
\$0-\$5m	\$1m	\$1m	\$2m	\$2m	\$0-\$5m	\$1m	\$2m	\$2m	\$5m
\$5-\$10m	\$2m	\$2m	\$2m	\$5m	\$5-\$10m	\$2m	\$2m	\$5m	\$5m
\$10-\$50m	\$2m	\$5m	\$5m	\$5m	\$10-\$50m	\$5m	\$5m	\$5m	\$10m
Over \$50m	\$5m	\$5m	\$10m	\$10m	Over \$50m	\$10m	\$10m	\$10m	\$10m

Project Risk High					Project Risk Extreme				
Project Value	Service Risk				Project Value	Service Risk			
	Low	Moderate	High	Extreme		Low	Moderate	High	Extreme
\$0-\$5m	\$2m	\$2m	\$5m	\$5m	\$0-\$5m	\$2m	\$5m	\$5m	\$10m
\$5-\$10m	\$2m	\$5m	\$5m	\$5m	\$5-\$10m	\$5m	\$5m	\$10m	\$10m
\$10-\$50m	\$5m	\$5m	\$10m	\$10m	\$10-\$50m	\$10m	\$10m	\$10m	\$10m
Over \$50m	\$10m	\$10m	\$10m	\$10m	Over \$50m	\$10m	\$10m	\$10m	\$10m

The level of cover suggested is based on several factors including:

- Levels accepted or recommended by some government agencies;
- Recognising the finite amount of insurance availability and the need to allocate it responsibly; and
- The balance between the cost of insurance and the required level of insurance for each project.