



CLLS Construction Law Committee

Foundation Level Training – Day 3



The City of London Law Society



BONDS, GUARANTEES AND PAYMENT SECURITY

15 November 2019



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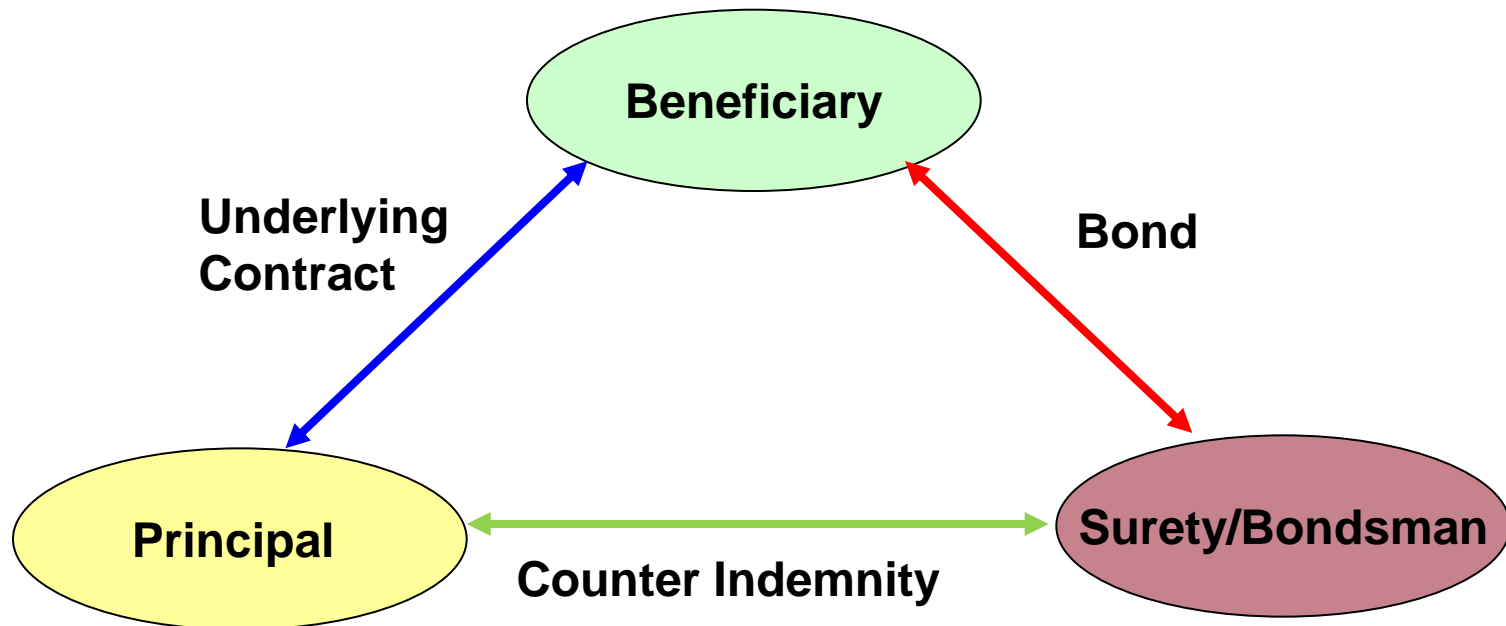
**Sir Robert
McALPINE**



TaylorWessing

Bonds

A party (the “**Surety**” or “**Bondsman**”) shall be obliged to pay another party (the “**Beneficiary**”) in the event of breach by a third party (the “**Principal**”) of that third party's obligations owed to the Beneficiary under a contract (the “**Underlying Contract**”)



- “Bond” is generic term that encapsulates potentially different types of obligations on the Surety/Bondsman:
 - a primary obligation owed by the Surety/Bondsman to the Beneficiary. The obligation is independent of obligations owed by the Principal under the Underlying Contract;

Hint: Keep in mind for "on-demand" bonds (to follow)

–a secondary obligation owed by the Surety/Bondsman to the Beneficiary which is conditional on establishing liability of the Principal to the Beneficiary.

Hint: Keep in mind for "on-default" bonds

Bonds

- A Surety's obligations can vary widely from bond to bond
- Labels used to describe bonds can be misleading. The Surety's obligations may only be determined by analysing the specific wording of the bond. In the Trafalgar House (1994) case, a bond was held to be on-default by the trial judge, on-demand on appeal by the Court of Appeal and overturned again to be on-default by the House of Lords.
- Cynically, bond forms may be in a form where performance security is illusory or compromised.
- Liability of the Surety/Bondsman is typically "all or nothing" thus potential for formal disputes
- Quantum may also be open to dispute

Binary Classification of Bonds

Bonds are labelled to describe the nature of the Surety's/
Bondsman's obligations:

- “On-Demand” or “Unconditional” Bonds.
A Surety/Bondsman is obliged to pay an amount as demanded at any time by the Beneficiary. Hint: a primary obligation.
- “On-Default” or “Conditional” Bonds
A Surety Bondsman is obliged to pay an amount to be determined under the Bond if the Principal is in breach of the Underlying Contract. Hint: a secondary obligation.

Classification of Typical Types of Bonds

- Performance Bonds: typically on-default
- Advance Payment Bonds: typically on-demand
Why? Because advance payment made but not yet earned.
Cf. *Autoridad del Canal de Panamá v Sacyr [2017]*
- Retention Bond: typically on-demand
Why? Because cash retention released
- Off-Site Materials Bonds: typically on-demand
Why? Because paid for but not yet delivered
- Bid Bond: typically on-demand
Why? Because awarding entity will suffer loss (arguably)

The JCT suite incorporates on-demand bonds: advance payment bond, retention bond and payment for off-site materials.

Bonds – policy

The use of bonds in UK public procurement was reviewed as part of a policy drive prior to the Housing Grants, Construction and Regeneration Act 1996. See HM Treasury Guidance No. 48 published in 1994

- Government should be aware of the burden that on-demand bonds can place on a contractor. Use sparingly and only for high risk projects where consequences of default are high.
- Advance payments should be avoided wherever possible; suggested on-demand form.
- Retention bonds are rare but consider costs and benefits; suggested on-demand form.

BUT

National Audit Office Investigation into Government's handling of collapse of Carillion (June 2018) for contract awards post 1st profit warning

- Lauded project requirements for performance bond
- Noted JV partners' obligations to step-in

On-default bonds – terms

- Standard Forms – ABI Model Form of Guarantee Bond is widely offered by Surety's/Bondsmen
- “1. The Guarantor guarantees ... that in the event of a breach of the Contract by the Contractor, the Guarantor shall subject to the provisions of this Guarantee Bond satisfy and discharge the damages sustained by the Employer as established and ascertained pursuant to and in accordance with the provisions of or by reference to the Contract and taking into account all sums due or to become due to the Contractor.”
- The Beneficiary’s obligation to “ascertain” damages means the due process (if any) under the Underlying Contract in relation thereto must have been gone through prior to making the call on the Bond (Paddington Churches v TGC (1999))

On-default bonds – terms

- Insolvency is not a breach Perar BV-v-General Surety and Guarantee Co Ltd (1994). Insolvency therefore will not trigger an ABI bond, when needed most. Drafting solutions required.
- Adjudication bonds provide that a Surety's liability is established on an Adjudicator's decision. Often drafted to be a hybrid; on-demand once a decision is made.
- Expiry is typically at PC but may be at end of defects liability period
- Value: Typically 10% of Contract Sum stated in the Building Contract.
- Assignment: Should be amended to allow assignment to funders etc.

On-default bonds – JCT and caselaw

Ziggurat (Claremont Place) LLP v HCC International Insurance Company [2017] 3286

- Amended ABI form for £382,519.08; contractor insolvency; additional costs claimed £621,798.38
- Amendments to deal with Perar so damages payable included monies payable under the building contract following insolvency
- Under the JCT, following insolvency termination, complete works, calculate overspend and recover as a debt. Failure to pay = breach and then triggers bond
- Takeaway 1: No bond monies until after final account of completed scheme
- Takeaway 2: Paddington Churches v TGC (1999) applies in that you have to “ascertain” damages as per final account overspend
- How useful was the bond?

On-demand Bonds – Making a Call

- Lord Denning described the nature of a Surety's obligation in Edward Owen Engineering [1978]:

“A [Surety] which gives an [on-demand Bond] must honour that [bond] according to its terms. It is not concerned in the least with the relations between the [Principal] and the [Beneficiary];...nor with the question whether the [Principal] is in default or not. The [Surety] must pay according to its [bond], on demand....without proof or conditions”

- (Almost unbelievably) the enforceability of the bond depends only upon a demand (or “call”)
- Compliance with procedural requirements is the immediate focus for the Surety/Bondsman

On-demand Bonds – Remedies

Challenging a demand:

- Fraud of which the Surety has notice (“fraud exception”) – rarely applied by the English courts. There must be “no real prospect of successfully defending the claim” *Enka Insaat case [2009]*;
- Mareva injunction: to restrain a Beneficiary from making a call by freezing assets. Injunction overturned in *Grande Cache Coal v Marubeni Corp case (2015)*; and
- A beneficiary cannot make a demand outside of time (e.g. after a certificate had been issued rendering the bond null and void) (*Simon Carves v Ensus [2011] EWHC 657*)

On-demand Bonds - Remedies

- Courts are reluctant to imply terms.
 - No implied term to make a demand in a reasonable time Scots law case *Sth Lanarkshire Council v Coface (2016)*.
 - No implied term that a demand may only be made upon breach by the Principal of the Underlying Contract *MW High Tech v Biffa* [2015]
- What happens where the amount recovered from the Surety by the Beneficiary exceeds the Beneficiary's damages sustained?
The Beneficiary has an obligation to re-pay the Surety the excess (*Cargill International v Bangladeshi Sugar [1996]* and *Tradigrain v State Trading Corporation of India [2005]*)

Counter Indemnity

Counter-indemnity from the Principal in favour of the Surety:

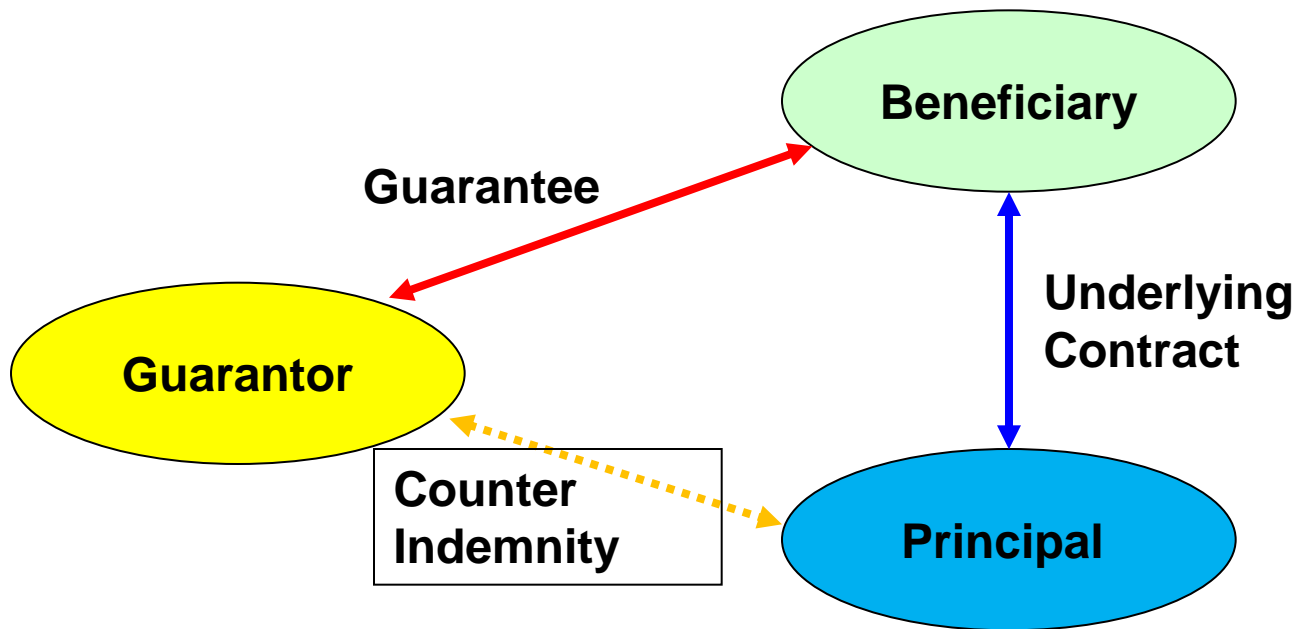
- Where the Surety becomes liable under the terms of a bond the Surety may recover that amount from the Principal under the counter-indemnity
- The effect is that the risk assumed by a Surety under a bond is limited to non-recovery under counter-indemnity (eg insolvency)
- Security (in the form of cash deposits and/or director's guarantees) may be required

Pricing of bonds

- Most contractors arrange a facility with sureties and banks to enable them to “call-off” bonds when the need arises
- Prices are dependent on Principal's track record, strength of management team, balance sheet, order book, macro-economic factors.
- On-default Bonds – 0.3 to 5% of the bonded sum p.a.
On-demand Bonds – 0.45% to 10% of the bonded sum p.a.
- Market conditions post Carillion are much tighter
- Check against new/exotic sureties, covenant strength and domicile

Guarantees

A party (the “**Guarantor**”) shall, for the benefit of another party (the “**Beneficiary**”) perform the obligations of a third party (the “**Principal**”) under a contract (the “**Underlying Contract**”) and/or pay damages where the Principal is in breach.



Guarantees

- Similarly to bonds, Guarantor's obligations vary widely and it is only by a close analysis of the terms of the Guarantee that the Guarantor's obligations can be deduced.
- There are no standard forms in the construction industry.
- Crucial to determine whether the Guarantor's obligations are:
 - as a "primary obligor", by which the Guarantor is to perform the Principal's obligations under the Underlying Contract, on default by the Principal
 - as a secondary obligation, by which the Guarantor is liable under the guarantee on default of the Principal under the Underlying Contract.

Guarantees

- Example Guarantee provisions

(see end of slides)

- Identity of the guarantor. Avoid ambiguity as to identity of the same *Liberty Merican Ltd v Cuddy [2013]*
- A guarantee is only as strong as the financial strength of the guarantor.
- Advice on need for guarantees *Football League v Hammonds* (On Digital; shareholders Carlton & Granada)

Guarantees – terms

- The Guarantee should be irrevocable and unconditional
- There should be continuing liability wording (i.e. the Guarantor is liable until all sums are paid by the Principal to the Beneficiary under the Underlying Contract) or an Expiry date on the issue of the Certificate of Practical Completion/Certificate of Making Good Defects
- The Guarantee should include saving provisions so that the Guarantor's obligations are not discharged by acts that would otherwise vitiate the Guarantee
- No greater liability for Guarantor than of Principal under the Underlying Contract? Indemnities show an intention to displace.

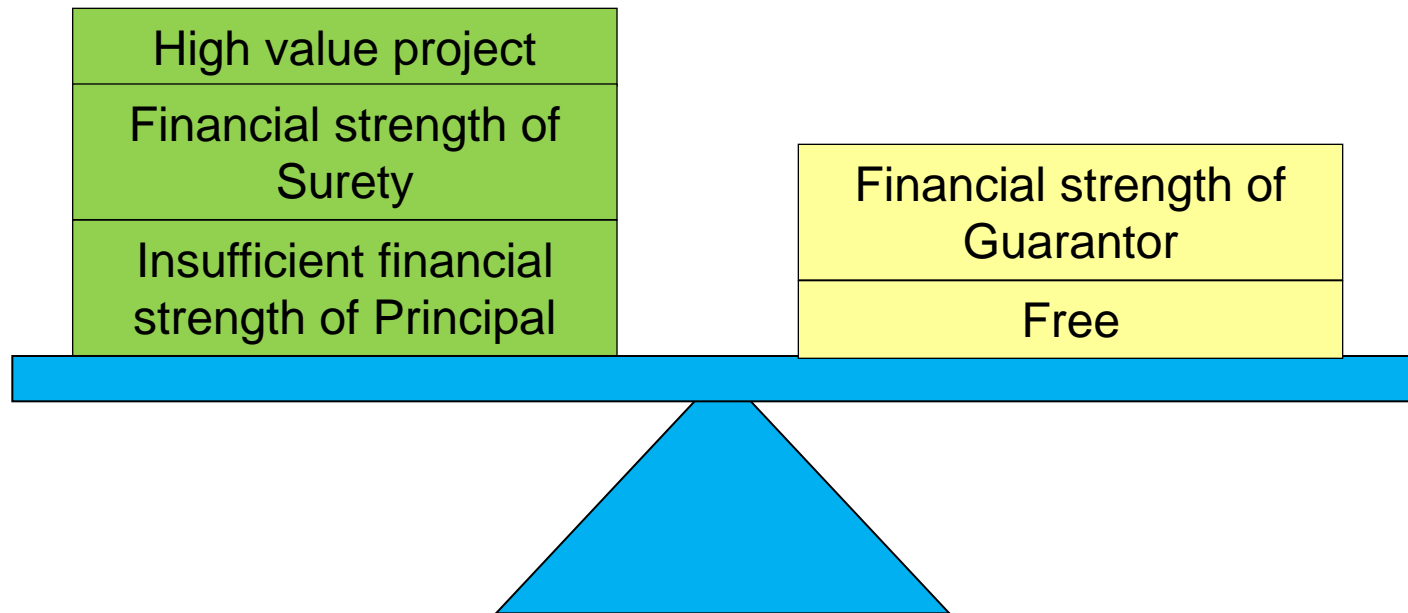
Guarantee or Bond?

- Some considerations an Employer often weighs up

Bond

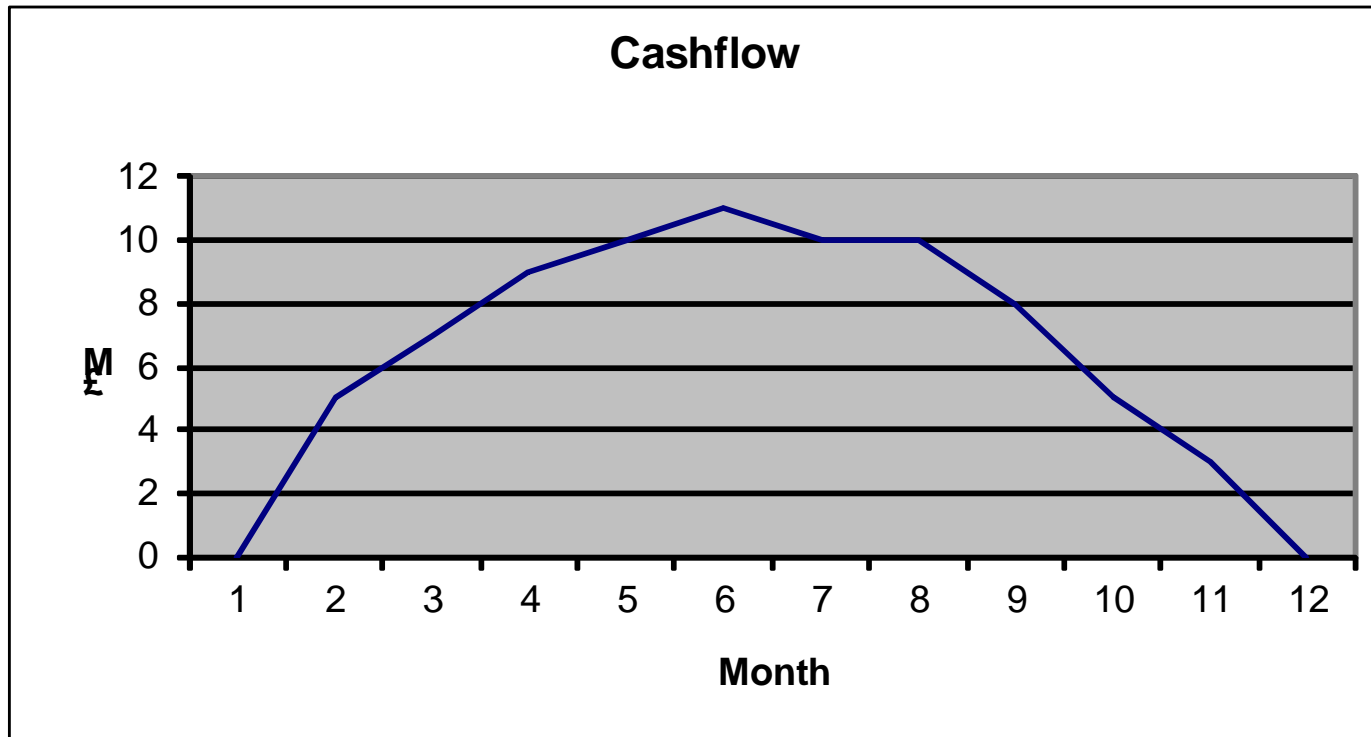
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Guarantee



Payment Security

- Payment Security
 - From employer related company to contractor
 - Covenant or cash?
 - Payment cycle, suspension rights (s112) and quantum



Payment Guarantees

- Typically from a related entity with a significant balance sheet
- Guarantee of payment as a secondary obligation, conditional on employer default
- Quantum and capped liability?

Escrow Account Agreements

- Cash deposited into a designated account as security for payment
- Typically on demand, with a form of Mandate
- The appointment of an "Agent" and role in:
 - establishing account
 - receiving funds
 - managing any Mandate
 - paying out and top-ups
 - closing the account
 - liability of Agent
- AML issues
- CLLS published form

Project Bank Accounts

- An account set up between the Employer and the Contractor whereby payments to the construction parties are made from and all from the same time
- Designed to increase payment security
- Prevent long chains of payment
- Needs to be clear when deciding how to withhold monies and in insolvency situations

Any questions?

ABI Performance Bond

THIS GUARANTEE BOND is made as a Deed BETWEEN the following parties whose names and [registered office] addresses are set out in the Schedule to this Guarantee Bond (“the Schedule”):-

- (1) The “Contractor” as principal
- (2) The “Guarantor” as guarantor, and
- (3) The “Employer”

WHEREAS

(1) By a contract (the “Contract”) entered into or to be entered into between the Employer and the Contractor (particulars of which are set out in the Schedule) the Contractor has agreed with the Employer to execute works (the “Works”) upon and subject to the terms and conditions therein set out

(2) The Guarantor has agreed with the Employer at the request of the Contractor to guarantee the performance of the obligations of the Contractor under the Contract upon the terms and conditions of this Guarantee Bond subject to the limitation set out in Clause 2.

NOW THIS DEED WITNESSES as follows:-

1. The Guarantor guarantees to the Employer that in the event of a breach of the Contract by the Contractor the Guarantor shall subject to the provisions of this Guarantee Bond satisfy and discharge the damages sustained by the Employer as established and ascertained pursuant to and in accordance with the provisions of or by reference to the Contract and taking into account all sums due or to become due to the Contractor.

2. The maximum aggregate liability of the Guarantor and the Contractor under this Guarantee Bond shall not exceed the sum set out in the Schedule (the “Bond Amount”) but subject to such limitation and to clause 4 the liability of the Guarantor shall be co-extensive with the liability of the Contractor under the Contract.

3. The Guarantor shall not be discharged or released by any alteration of any of the terms conditions and provisions of the Contract or in the extent or nature of the Works and no allowance of time by the Employer under or in respect of the Contract or the Works shall in any way release reduce or affect the liability of the Guarantor under this Guarantee Bond.

4. Whether or not this Guarantee Bond shall be returned to the Guarantor the obligations of the Guarantor under this Guarantee Bond shall be released and discharged absolutely upon Expiry (as defined in the Schedule) save in respect of any breach of the Contract which has occurred and in respect of which a claim in writing containing particulars of such breach has been made upon the Guarantor before Expiry.

5. The Contractor having requested the execution of this Guarantee Bond by the Guarantor undertakes to the Guarantor (without limitation of any other rights and remedies of the Employer or the Guarantor against the Contractor) to perform and discharge the obligations on its part set out in the Contract.

6. This Guarantee Bond and the benefits thereof shall not be assigned without the prior written consent of the Guarantor and the Contractor.

7. The parties to this Guarantee Bond do not intend that any of its terms will be enforceable, by virtue of The Contracts (Rights of Third Parties) Act 1999 or otherwise, by any person not a party to it.

8. This Guarantee Bond shall be governed by and construed in accordance with the laws of England and Wales and only the courts of England and Wales shall have jurisdiction hereunder.

ABI Performance Bond

THE SCHEDULE

The Contractor: []

The Guarantor: []

The Employer: []

The Contract: A contract dated the [] day of []
to be entered into between the Employer and
the Contractor for the construction of works comprising for the
original contract sum of £[] ([] Pounds)

The Bond Amount: The sum of £ (Pounds)

The Expiry Date: The date of issue of the [Certificate of
Practical Completion] of the Works under the Contract which
shall be conclusive for the purposes of this Guarantee Bond.

IN WITNESS whereof

[]

JCT Advance Payment Bond

Advance Payment Bond

(Agreed between the JCT and the British Bankers' Association)

1 THE parties to this Bond are: _____ whose registered office is at _____ ('the Surety'), and _____ of _____ ('the Employer').

2 The Employer and _____ ('the Contractor') have agreed to enter into a contract ('the Contract') for building works ('the Works') at _____.

3 The Employer has agreed to pay the Contractor the sum of [_____] as an advance payment of sums due to the Contractor under the Contract ('the Advance Payment') for reimbursement by the Surety on the following terms:

.1 when the Surety receives a demand from the Employer in accordance with clause 3.2 below the Surety shall repay the Employer the sum demanded up to the amount of the Advance Payment;

.2 the Employer shall in making any demand provide to the Surety a completed notice of demand in the form of the Schedule attached hereto which shall be accepted as conclusive evidence for all purposes under this Bond. The signatures on any such demand must be authenticated by the Employer's bankers;

.3 the Surety shall within 5 Business Days after receiving the demand pay to the Employer the sum so demanded. 'Business Day' means the day (other than a Saturday or a Sunday) on which commercial banks are open for business in London.

4 Payments due under this Bond shall be made notwithstanding any dispute between the Employer and the Contractor and whether or not the Employer and the Contractor are or might be under any liability one to the other. Payment by the Surety under this Bond shall be deemed a valid payment for all purposes of this Bond and shall discharge the Surety from liability to the extent of such payment.

5 The Surety consents and agrees that the following actions by the Employer may be made and done without notice to or consent of the Surety and without in any way affecting changing or releasing the Surety from its obligations under this Bond and the liability of the Surety hereunder shall not in any way be affected hereby. The actions are:

.1 waiver by the Employer of any of the terms, provisions, conditions, obligations and agreements of the Contractor or any failure to make demand upon or take action against the Contractor;

.2 any modification or changes to the Contract; and/or

.3 the granting of any extensions of time to the Contractor without affecting the terms of clause 7.3 below.

6 The Surety's maximum aggregate liability under this Bond which shall commence on payment of the Advance Payment by the Employer to the Contractor shall be the amount of _____] which sum shall be reduced by the amount of any reimbursement made by the Contractor to the Employer as advised by the Employer in writing to the Surety.

7 The obligations of the Surety under this Bond shall cease upon whichever is the earliest of:

JCT Advance Payment Bond

- .1 the date on which the Advance Payment is reduced to nil as certified in writing to the Surety by the Employer;
 - .2 the date on which the Advance Payment or any balance thereof is repaid to the Employer by the Contractor (as certified in writing to the Surety by the Employer) or by the Surety; and
 - .3 [longstop date to be given],
- and any claims hereunder must be received by the Surety in writing on or before such earliest date.

- 8 This Bond is not transferable or assignable without the prior written consent of the Surety. Such written consent will not be unreasonably withheld.
- 9 Notwithstanding any other provisions of this Bond nothing in this Bond confers or is intended to confer any right to enforce any of its terms on any person who is not a party to it.
- 10 This Bond shall be governed and construed in accordance with the laws of England and Wales.

Example PCG

EXAMPLE PARENT COMPANY GUARANTEE

THIS DEED OF GUARANTEE is made on the _____ day of _____

Between _____ whose registered office is situated at _____ called the “Guarantor” of one part and [_____] of [_____] (hereinafter called the “Beneficiary” which expression shall include its successors and assigns) of the other part

WHEREAS the Beneficiary has entered into a contract dated the day of _____ (hereinafter called the “Contract”) with whose registered office is situate at _____ (hereinafter called “The Contractor”) for at (hereinafter called the “services”) for the sum mentioned in the Contract: and

WHEREAS the Guarantor has agreed to guarantee the due performance of the Contract in the manner hereinafter appearing

1. The Guarantor shall, as primary obligor, guarantee the due and proper performance of the Contract and the due observance and punctual performance of all obligations, duties, undertakings, covenants and conditions by or on the part of the Contractor contained therein and to be observed and performed by it, which guarantee shall extend to included any variation or addition to the Contract.

2. In the event of the Contractor failing to carry out, observe or perform all any of the said obligations, duties undertakings, covenants and conditions under the Contract (unless relieved from the performance of any part of the Contract by statute or by the decision of a court or tribunal of competent jurisdiction) the Guarantor shall be

liable for and shall indemnify the Beneficiary against all losses, damages, costs and expenses, whatsoever which the Beneficiary may incur by reason or in consequence of any such failure to carry out observe

3. The Guarantor shall not be discharged or released from this Guarantee by the occurrence of any one or more of the following:-

3.1 Any alteration to the nature of extent of the services or otherwise to the terms of the contract;

3.2 Any allowance of time, forbearance, indulgence or other concession granted to the Contractor under the Contract or any other compromise or settlement of any dispute between the Beneficiary and the Contractor (but so that the Beneficiary shall not pursue against the Guarantor a remedy contrary to the terms of any such compromise or settlement insofar as the Contractor shall have complied with such terms.)

3.3 The liquidation, bankruptcy, administration, absence of legal personality, dissolution, incapacity or any change in the name, composition or constitution of the contractor or the Guarantor.

4. This Guarantee is a continuing guarantee and accordingly shall remain in operation until all obligations, duties, undertakings, covenants, conditions and warranties now or hereafter to be carried out or performed by the Contractor under the Contract shall have been satisfied or performed in full and is in addition to an not in substitution for any other security which the Beneficiary may at any time hold for the performance of such obligations and may be enforced without first having recourse to any such security and without taking any other steps or proceedings against the Contractor.

Example PCG

5. So long as any sums are payable (contingently or otherwise) by the Contractor to the Beneficiary under the terms of the Contract then the Guarantor shall not exercise any right of set off or counterclaim against the Contractor or any other person or prove in competition with the Beneficiary in respect of any payment by the Guarantor hereunder and in case the Guarantor receives any sum from the contractor or any other person in respect of any payment of the Guarantor hereunder the Guarantor shall hold such monies in trust for the Beneficiary so long as any sums are payable (contingently or otherwise) under this Guarantee.

6. The Guarantor will not, without prior written consent of the Beneficiary hold any security from the Contractor or any other person in respect of the Guarantor's liability hereunder or in respect of any liabilities or other obligations of the Contractor to the Guarantor. The Guarantor will hold any security held by it in breach of this provision in trust for the Beneficiary.

7. This Guarantee is in addition to and not in substitution for any present and future guarantee lien or other security held by the Beneficiary. The Beneficiary's rights under this Guarantee are in addition to and not exclusive of those provided by law.

CLLS Escrow Account Agreement



DATED

[•]
and
[•]

as Principals

[•]

as Escrow Agent

Template
ESCROW AGREEMENT
relating to a project at [•]

DATED

PARTIES

- (1) [•] (company no [•]) whose registered office is at [•] (the "Employer")
- (2) [•] (company no [•]) whose registered office is at [•] (the "Contractor")
(together, the "Principals")
- (3) [•] (company no [•]) whose registered office is at [•] (the "Escrow Agent")

BACKGROUND

- (A) The Principals are the parties to an agreement dated [•] (the "Main Agreement") for the carrying out of works at [•] as more particularly described in the Main Agreement.
- (B) Pursuant to clause 1.2, the Employer is obliged to pay to the Escrow Agent the sum of £[•] (the "Escrow Sum") which is to be held subject to the escrow arrangements set out in this Agreement.
- (C) The Principals have instructed the Escrow Agent to pay the Escrow Sum following receipt into an interest bearing bank account (the "Escrow Account") to be opened in the name of the Escrow Agent with [•] Bank plc (the "Bank") and to be called the "[•] Escrow Account".
- (D) The Principals have requested that the Escrow Agent hold and apply the amount from time to time standing to the credit of the Escrow Account (the "Escrow Funds") on the terms of this Agreement.
- (E) In this Agreement "Business Day" means any day which is not a Saturday, a Sunday or a public holiday in [England and Wales]¹.

OPERATIVE PROVISIONS

- 1 APPOINTMENT OF ESCROW AGENT AND CREATION OF ESCROW ACCOUNT
 - 1.1 The Principals jointly appoint the Escrow Agent to act as escrow agent to hold and apply the Escrow Funds in accordance with this Agreement. The Escrow Agent accepts that appointment.
 - 1.2 [Within [•] Business Days after the date of this Agreement][On or before the Date of Possession stated in the Main Agreement]², the Employer shall deposit the Escrow Sum with the Escrow Agent as security for the payment of sums from time to time becoming due to the Contractor under the Main Agreement.
 - 1.3 Forthwith on receipt of the Escrow Sum, the Escrow Agent shall open the Escrow Account and pay the Escrow Sum into the Escrow Account.

¹ Consider amending if the Works are located outside England and Wales.

² Amend as appropriate.

CLLS Escrow Account Agreement

1.4 [Within [●] Business Days after the date of this Agreement][On or before [●]]³, the Employer shall issue an irrevocable instruction to the Escrow Agent in the form set out in Schedule 1. Only one instruction is required to be issued for all and any payments to be made to the Contractor under clause 2.2.2.

2 APPLICATION OF ESCROW FUNDS⁴

2.1 Employer's interest in Escrow Funds

2.1.1 The Employer's interest in the Escrow Funds is fiduciary as trustee for the purposes set out in this Agreement (but without obligation to invest) with effect from the date of establishment of the Escrow Account until all sums due to the Contractor under the Main Agreement have been discharged by the Employer or until the Escrow Account is closed in accordance with clause 2.5.4.

2.1.2 All interest accruing on amounts from time to time held in the Escrow Account shall belong to the Employer.

2.1.3 The Employer shall not be entitled to make any withdrawals from the Escrow Account other than as contemplated by clause 2.5.4 or as otherwise agreed between the Principals.

2.2 Contractor's right to payment

2.2.1 The Contractor may require payments to be made from the Escrow Account only in the circumstances described in clause 2.2.2.

2.2.2 If the Employer fails to pay a notified sum (as that term is defined in section 111(2) of the Housing Grants, Construction and Regeneration Act 1996, as amended by the Local Democracy, Economic Development and Construction Act 2009) to the Contractor under the Main Agreement by its final date for payment, the Contractor may give to the Employer notice of its intention to require the Escrow Agent to make payment of the unpaid amount from the Escrow Account. If the notified sum or any part of it remains unpaid on the expiry of five Business Days following receipt by the Employer of such notice, the Contractor may issue to the Escrow Agent a demand in substantially the form set out in Schedule 2 requiring the Escrow Agent to make payment of the unpaid amount from the Escrow Account to the Contractor.

2.2.3 A demand under clause 2.2.2 shall be valid if (and only if) it is accompanied by:

- (a) a copy of the notice referred to in clause 2.2.2; and
- (b) a certificate purporting to be signed by a director or other authorised officer of the Contractor, confirming that the amount requested is the notified sum and that it remains unpaid.

2.2.4 Forthwith on receipt of a demand under clause 2.2.2, the Escrow Agent shall send a copy of the demand and the accompanying documents to the Employer.

2.2.5 Subject to clauses 3.4 and 3.6, the Escrow Agent shall comply with any valid demand for payment issued by the Contractor pursuant to clause 2.2.2 upon the expiry of five Business

Days following receipt (or deemed receipt) by the Employer of the demand and accompanying documents referred to in clause 2.2.4, unless within that period:

- (a) the Contractor notifies the Escrow Agent that it has been paid the whole of the notified sum; or
- (b) the Employer obtains an order from an English court or other competent tribunal binding on the Escrow Agent that prohibits it from complying with the demand.

2.2.6 Any amount received by the Contractor from the Escrow Account pursuant to clause 2.2.5 shall to that extent discharge the Employer's obligation to make payment of such amount to the Contractor as required by the Main Agreement.

2.2.7 If the Contractor is entitled to give notice to the Employer or to issue a demand to the Escrow Agent under clause 2.2.2 but fails to do so, the Employer shall be deemed for the purpose of clause [8.9.1] of the Main Agreement (but not for any other purpose) to have made payment to the Contractor by the final date for payment.

2.3 Replenishment of Escrow Account

2.3.1 If the Contractor receives a payment out of the Account pursuant to clause 2.2.5 or any other sum is withdrawn from the Account (whether by the Escrow Agent or otherwise), the Escrow Agent shall forthwith so notify the Principals. Within five Business Days of receiving such notification, the Employer shall:

- (a) direct the Escrow Agent to apply any interest then accrued in the Escrow Account in full or partial satisfaction of its obligation to make further payment into the Escrow Account; and
- (b) (where such interest is insufficient) deposit with the Escrow Agent such further sum as will ensure that the balance in the Escrow Account is not less than the Escrow Sum.

2.3.2 If the Employer fails to make the deposit referred to in clause 1.2 or the further deposit referred to in clause 2.3.1(b), the Contractor may give to the Employer a notice requiring the Employer to do so. If the Employer fails to make such deposit or further deposit within five Business Days of the Contractor's notice, such failure shall be treated for the purposes of clauses [4.11] and [8.9.1] of the Main Agreement as a failure to pay the Contractor in accordance with clause [4.9] of the Main Agreement by the final date for payment.

2.4 Statements of account

2.4.1 Forthwith on receipt of any further deposit referred to in clause 2.3.1(b), and in any event at intervals of not more than six months from the date of this Agreement until the Escrow Account is closed in accordance with clause 2.5.4, the Escrow Agent shall issue a statement of account to the Principals recording the Escrow Funds then held and any transactions in relation to the Escrow Account since the last such statement was issued.

2.5 Closure of the Escrow Account

2.5.1 On the occurrence of any of the following events (whichever occurs first):

- (a) payment of the balance (if any) stated as due in the Final Statement or the Employer's Final Statement under the Main Agreement, or such other amount as may be determined to be payable pursuant to clause [1.8.2] of the Main Agreement;

³ Amend as appropriate.

⁴ This clause assumes that the Main Agreement will be based on the JCT 2016 Design and Build Contract (DB 2016) and cross-refers to the clause numbers in that form of contract. It will need to be adapted if a different form is used.

CLLS Escrow Account Agreement

- (b) determination of the Contractor's employment under the Main Agreement by the Employer pursuant to any of clauses [8.4, 8.5 or 8.6] of the Main Agreement (or, if the Contractor disputes the validity of that determination, when an adjudicator, arbitrator or court decides that the determination was valid, subject in the case of an adjudicator's decision to a right for the Contractor to challenge that decision within 20 Business Days in accordance with the dispute resolution provisions in the Main Agreement, failing which the decision will be treated for the purposes of this clause 2.5.1 only as being final and conclusive);
- (c) determination of the Contractor's employment under the Main Agreement by the Contractor pursuant to clause [8.9] or clause [8.10] of the Main Agreement and payment by the Employer of the amount due to the Contractor upon such determination under clause [8.12.5] of the Main Agreement;
- (d) agreement between the Principals that the escrow arrangements in this Agreement are no longer required; or
- (e) *[longstop date, if required]*;

the purpose of this Agreement shall be treated as having been fulfilled and the Employer may give notice to the Escrow Agent (with a copy to the Contractor) requiring the Escrow Agent to close the Escrow Account.

2.5.2 The Employer's notice under clause 2.5.1 shall specify:

- (a) which of the events listed in clause 2.5.1 has occurred; and
- (b) details of the bank account to which any credit balance in the Escrow Account should be transferred.

2.5.3 Within five Business Days following receipt of a notice under clause 2.5.1, the Contractor may issue a counter-notice to the Employer (with a copy to the Escrow Agent) disputing that the event stated in the Employer's notice has occurred. In that event, the matter shall be determined in accordance with the dispute resolution provisions in the Main Agreement. If the determination is in the Employer's favour, the Employer may then give a further notice under clause 2.5.1.

2.5.4 The Escrow Agent shall close the Escrow Account and release any balance then standing to the credit of the Escrow Account (including accrued interest) to the Employer:

- (a) five Business Days following receipt of the Employer's notice under clause 2.5.1, if the Contractor has not issued a counter-notice under clause 2.5.3; or
- (b) five Business Days following receipt of the Employer's further notice under clause 2.5.3, if the Contractor has issued such a counter-notice.

3 OPERATION OF THE ESCROW ACCOUNT BY ESCROW AGENT

3.1 The Escrow Agent shall:

- (a) hold the Escrow Funds in the Escrow Account as stakeholder for the purposes and on the terms set out in this Agreement;
- (b) pay into the Escrow Account any further amounts received by it from the Employer pursuant to clause 2.3.1(b); and

- (c) transfer or otherwise deal with the Escrow Funds only in accordance with the terms of this Agreement.

3.2 The Escrow Agent may accept and rely without enquiry on any instruction which appears on its face to be signed by or on behalf of the relevant Principal, provided that (in the case of a demand issued by the Contractor pursuant to clause 2.2.2) it is accompanied by the documents referred to in clause 2.2.3.

3.3 Without limiting clause 3.2, the Escrow Agent shall not be responsible for ascertaining:

- (a) whether any amount it is instructed to pay has been correctly calculated or is properly payable; or
- (b) whether an instruction has been properly executed or validly authorised.

3.4 The Escrow Agent shall promptly comply with any demand or other obligation to pay monies out of the Escrow Account by instructing the Bank to do so, but the Escrow Agent shall not be liable or responsible for:

- (a) any delay or failure on the part of the Bank or any third party in receiving or executing any instructions sent by the Escrow Agent;
- (b) any loss or damage suffered by any person in connection with any fraud, negligence, default or other act or omission on the part of the Bank or (except to the extent directly resulting from the fraud or wilful default of the Escrow Agent or its directors, servants or agents) any other person; or
- (c) any loss or damage suffered by any person as a result of the insolvency, bankruptcy, winding-up, administration, reorganisation or any analogous event in the United Kingdom or any other jurisdiction relating to the Bank or any other person.

3.5 The Escrow Agent shall be entitled to be satisfied that any receipt or payment made or to be made into or out of the Escrow Account complies with all applicable money laundering and other laws and regulations and its own anti-money laundering policies. The Escrow Agent shall not be liable or responsible for any failure to take, or any delay in taking, any action which in its judgment may:

- (a) be contrary to any provision of this Agreement or any court order or any money laundering or other laws and regulations or any of its own anti-money laundering or other risk management policies; or
- (b) expose it to any liability or expense against which it has not been indemnified and secured to its satisfaction.

3.6 The Escrow Agent shall not be obliged to make (or to instruct the Bank to make) any payment from the Escrow Account except out of immediately available cleared funds which have been irrevocably credited to and are standing to the credit of the Escrow Account, nor shall it be required to take any other action to the extent that such action (if taken) would leave a debit balance in the Escrow Account.

4 INVESTMENT OF THE ESCROW SUM

4.1 The Escrow Agent shall not be responsible for investing the Escrow Funds in any particular way. Any interest earned on the Escrow Funds shall be credited to the Escrow Account and shall be applied as directed by the Employer in accordance with clause 2.3.1(a).

CLLS Escrow Account Agreement

4.2 The Escrow Agent shall not be required to determine or dispute the rate or amount of any interest, charges, fees, costs or expenses paid or levied by the Bank or any tax or other liabilities relating to the Escrow Funds.

5 ROLE OF THE ESCROW AGENT

5.1 The responsibilities of the Escrow Agent under this Agreement are administrative only.

5.2 The Escrow Agent shall have only those duties, obligations and responsibilities expressly set out in this Agreement and shall have no implied duties, obligations or responsibilities. In particular, the Escrow Agent is not bound by the Main Agreement or any other agreement, arrangement or understanding between the Principals, nor shall the Escrow Agent be treated as having actual, constructive or implied knowledge of any of the terms of the Main Agreement or any such other agreement, arrangement or understanding.

5.3 If at any time the Escrow Agent is uncertain as to its duties, obligations or responsibilities under this Agreement or receives instructions, claims or demands which in its opinion conflict with each other and/or with any provision of this Agreement:

- (a) the Escrow Agent may, but shall not be required to, take legal action to resolve any such uncertainty or conflict and in doing so may consult with legal advisers of its own choice; and
- (b) the Escrow Agent shall be entitled to hold the Escrow Funds and to refrain from taking any action until it receives:
 - (i) a joint instruction from the Principals in terms satisfactory to the Escrow Agent; or
 - (ii) an order of an English court or other competent tribunal binding on the Escrow Agent,

following which the Escrow Agent shall deal with the Escrow Funds in accordance with such instruction or order.

5.4 The Escrow Agent may resign its appointment as escrow agent under this Agreement at any time on at least [40] Business Days' prior notice to the Principals. If the Escrow Agent resigns, the Principals shall use all reasonable endeavours to procure a replacement within the notice period and the Escrow Agent shall co-operate with the Principals as necessary to facilitate a smooth handover of the Escrow Agent's duties to the appointed replacement. If a replacement has not been made before the expiry of the notice period, the Escrow Agent may instruct the Bank to pay the Escrow Funds (including any accrued interest, but less any deductions yet to be made under clause 6.4 or clause 7.3) into court.⁵

6 AUTHORITY AND INDEMNITY

6.1 The Principals irrevocably authorise the Escrow Agent to:

- (a) pay all taxation, bank charges, CHAPS fees, penalties and other liabilities arising out of or in connection with this Agreement, or the opening or operation of the Escrow Account; and

⁵ If the Contractor will not accept this provision, an alternative would be to allow the Escrow Agent to resign if there is a change of control of the Employer, because of the potential regulatory difficulties to which this scenario may give rise.

- (b) make any payments, deductions or withholdings (whether on account of tax or otherwise) or do anything else required by any law, regulation or court order (or, if so required by any law, regulation or court order, refrain from making any payment, or from doing anything else, otherwise required by this Agreement).

6.2 The Principals hereby jointly and severally agree to indemnify⁶ the Escrow Agent and its directors, servants and agents, on demand, against all claims, demands, actions, proceedings, costs, expenses, liabilities, damages and losses (including all interest, penalties and legal and other professional costs and expenses, but excluding the Escrow Agent's fees and expenses as provided for in clause 7) which it may suffer or incur arising out of or in connection with this Agreement (including any taxation, bank charges, CHAPS fees, penalties, liabilities, payments, deductions or withholdings referred to in clause 6.1) (together "Losses"), subject only to clause 6.3.

6.3 The indemnity in clause 6.2 shall not apply to Losses to the extent that they are caused by or attributable to the wilful default or fraud of the Escrow Agent or any of its directors, servants or agents.

6.4 Without limiting the rights of the Escrow Agent under clause 6.1, or the obligations of the Principals under clause 6.2, the Principals irrevocably authorise the Escrow Agent to withdraw from the Escrow Account for its own account and benefit, without any further instruction or consent, any amount authorised to be paid by the Escrow Agent under clause 6.1 and/or any amount which the Principals are liable to pay to the Escrow Agent under clause 6.2.⁷

7 ESCROW AGENT'S FEES AND EXPENSES

7.1 The Escrow Agent shall be entitled to be paid its professional fees (at the usual hourly rates charged by it from time to time⁸), for its services as escrow agent under this Agreement and the opening, operation and closing of the Escrow Account (together with its costs and expenses and any applicable VAT), including any fees, costs and expenses incurred in any action taken pursuant to clause 5.3(a).

7.2 The Employer shall alone be responsible for the fees of the Escrow Agent under clause 7.1.⁹

7.3 Without limiting the rights of the Escrow Agent under clause 7.1, or the obligations of the Employer under clause 7.2, the Principals irrevocably authorise the Escrow Agent to withdraw from the Escrow Account for its own account and benefit, without any further instruction or consent, any amount for which the Employer is responsible under clause 7.2.¹⁰

⁶ Alternatively this indemnity could be given by the Employer alone, possibly with a right for the Employer to claim a contribution from the Contractor (see the footnote to clause 6.4 below).

⁷ An alternative possibility would be to allow the Escrow Agent to withdraw only accrued interest, with any balance being payable by the Employer directly. It would then be open to the Principals to agree an apportionment of the balance between them, if that reflects their commercial bargain. If so, appropriate provisions would need to be included in the Agreement.

⁸ This may need to be amended to reflect the agreed basis on which the Escrow Agent will charge for its services.

⁹ Again the Principals may agree to apportion these fees between them; see the footnote to clause 6.4 above.

¹⁰ Again see the footnote to clause 6.4 above.

CLLS Escrow Account Agreement

8 COMMUNICATIONS

8.1 Any notice, instruction or other communication under this Agreement must be in writing (but may consist of separate documents in the same form) and shall be delivered by hand or sent by special delivery post or e-mail to the relevant party at its address and for the attention of the individual set out below (or as notified in accordance with clause 8.2):

(a) The Employer

Address: [•]
E-mail address: [•]
Attention: [•]
Reference: [•]

(b) The Contractor

Address: [•]
E-mail address: [•]
Attention: [•]
Reference: [•]

(c) The Escrow Agent

Address: [•]
E-mail address: [•]
Attention: [•]
Reference: [•]

8.2 A party may notify the other parties of a change to its details specified in clause 8.1. The new details shall take effect as against the other parties five Business Days after receipt of the notice or on such later date as it may specify in the notice.

8.3 Unless proof of earlier receipt exists, a communication complying with clause 8.1 shall be deemed received:

- (a) if delivered by hand, at the time of delivery, unless deemed receipt would occur after 5.00 pm on a Business Day, or on a day which is not a Business Day, in which case deemed receipt will be at 9.00 am on the next Business Day;
- (b) if sent by special delivery post, at 9.00 am on the second Business Day after posting; or
- (c) if sent by e-mail, at the earliest of:
 - (i) the time a return receipt is generated automatically by the recipient's e-mail server;
 - (ii) the time the recipient acknowledges receipt; and
 - (iii) 24 hours after transmission,unless the sender receives notification that the e-mail has not been successfully delivered.

8.4 This clause does not apply to the service of any document required to be served in relation to legal proceedings.

9 TERMINATION

9.1 The Principals may at any time agree to terminate the appointment of the Escrow Agent under this Agreement by notice to the Escrow Agent.

9.2 The obligations of the Escrow Agent under this Agreement will automatically terminate:

- (a) at midnight on [•] (or, as the case may be, any later deadline agreed in writing by the Escrow Agent) if the Escrow Agent has not received the Escrow Sum by that deadline; or
- (b) if, at any time after the Escrow Sum is credited to the Escrow Account, the Escrow Funds (less any unpaid permitted deductions) are zero and the Employer is not required or has not taken steps to replenish the Escrow Account in accordance with clause 2.3.1.

9.3 Upon termination of the Escrow Agent's appointment for any reason, the Escrow Agent shall co-operate with the Principals as necessary to facilitate a smooth handover of the Escrow Agent's duties to any person appointed by the Principals to act in its place.

9.4 Termination of the Escrow Agent's appointment for any reason shall not prejudice or affect any accrued rights or obligations of the parties to this Agreement.

9.5 The Escrow Agent shall not close the Escrow Account other than in accordance with the express terms of this Agreement.

10 GENERAL

10.1 Each of the Principals shall provide the Escrow Agent with such information as it may reasonably require in connection with the establishment and operation of the Escrow Account and shall execute any document and do anything else that the Escrow Agent reasonably requires to give effect to this Agreement.

10.2 The rights and remedies of the Escrow Agent expressly conferred by this Agreement are cumulative and additional to any other rights or remedies that it may have.

10.3 The Escrow Agent shall not be liable for any failure or delay in the performance of any of its duties arising (in whole or in part) from circumstances beyond its control, including civil disturbances, acts of terrorism, natural disasters, loss or disruption to utilities or any failure of computer or other electronic services or systems.

10.4 In this Agreement, the interpretation of general words shall not be restricted by words indicating a particular class or particular examples.

10.5 The clause headings in this Agreement are for ease of reference only and shall not affect the interpretation of any provision of this Agreement.

10.6 No variation of this Agreement shall be effective unless it is in writing and signed by or on behalf of each party.

10.7 A failure or delay in exercising any right or remedy under this Agreement shall not constitute a waiver of that right or remedy. A single or partial exercise of any right or remedy shall not prevent the further exercise of that right or remedy. A waiver of a breach of this Agreement shall not constitute a waiver of any other breach.

CLLS Escrow Account Agreement

- 10.8 Neither the Employer nor the Contractor may assign the benefit of this Agreement or any rights arising under it without the written consent of the other parties to this Agreement.¹¹
- 10.9 The parties do not intend any third party to have the right to enforce any provision of this Agreement under the Contracts (Rights of Third Parties) Act 1999, except that, with the consent of the Escrow Agent, any of its directors, servants or agents may enforce the indemnity in clause 6.2 as if they were a party to this Agreement. The parties may terminate or vary this Agreement without the consent of any third party.
- 10.10 This Agreement is the entire agreement between the parties and replaces all previous agreements and understandings between them relating to its subject matter. The parties agree that no representations, warranties, undertakings or promises have been expressly or impliedly given in respect of the subject matter of this Agreement other than those which are expressly stated in this Agreement. No party shall have any remedy in respect of any statement not set out in this Agreement upon which it relied in entering into this Agreement, unless the statement was made fraudulently. The parties agree that they shall have no right to bring a claim in tort or under the Misrepresentation Act 1967 in connection with this Agreement.
- 10.11 This Agreement may be executed in any number of counterparts, which shall each constitute an original and together constitute one agreement. If this Agreement is executed in counterpart, it shall not be effective unless each party has executed at least one counterpart.
- 10.12 This Agreement and any non-contractual obligations arising in connection with it shall be governed by English law.
- 10.13 The English courts shall have exclusive jurisdiction to determine any dispute arising in connection with this Agreement (and, unless provided otherwise, any document entered into in connection with it), including disputes relating to any non-contractual obligations. Each party irrevocably waives any objection which it may now or later have to proceedings being brought in the English courts (on the grounds that the English courts are not a convenient forum or otherwise). Nothing in this Agreement (or, unless provided otherwise, any document entered into in connection with it) shall prevent a party from applying to the courts of any other country for injunctive or other interim relief.

Schedule 1 Letter of Instruction from Employer to Escrow Agent

Dear Sirs

Works at [●] (the "Project")

We refer to the Escrow Agreement dated [●] (the "Escrow Agreement") entered into between yourselves, ourselves and [●] (the "Contractor") in connection with the Project.

We confirm that we have today paid the sum of £[●] into your bank account no [●] at [●] Bank plc, [●] branch (sort code [●]), to be held by you and applied in accordance with the terms of the Escrow Agreement.

We hereby irrevocably authorise and instruct you to comply with any requirement validly made by the Contractor in accordance with clause 2.2.2 of the Escrow Agreement, provided that:

- (a) such requirement is accompanied by the documents referred to in clause 2.2.3 of the Escrow Agreement;
- (b) you have first complied with clause 2.2.4 of the Escrow Agreement; and
- (c) the conditions to compliance set out in clause 2.2.5 of the Escrow Agreement are satisfied.

Any payment made by you pursuant to this instruction shall be made to the Contractor's account no [●] at [●] Bank plc, [●] branch (sort code [●]) and to no other account.

Yours faithfully

For and on behalf of [●]

¹¹ Note that the restriction on assignment by the Contractor may fall foul of the Business Contract Terms (Restrictions on Assignment of Receivables) Regulations 2015 when it comes into force.

CLLS Escrow Account Agreement

Schedule 2 Form of Instruction

EXECUTION PAGE

ESCROW ACCOUNT PAYMENT INSTRUCTION

From: [Contractor]
To: [Escrow Agent]
[address]
Attention: [●]
Reference: [●]

[date]

In accordance with and subject to the terms of the Escrow Agreement dated [●], we irrevocably and unconditionally authorise and instruct you to make the following payment out of the Escrow Account:

the sum of £[●] to be paid to:

Bank: [name and address]
Sort code: [●]
Account name: [●]
Account number: [●].

We enclose copies (certified by a Solicitor of the Supreme Court or other notarised attorney) of the accompanying documents referred to in clause 2.2.3 of the Escrow Agreement.

Signed for and on behalf of [Contractor])

Authorised signatory

Signed by)
for and on behalf of [EMPLOYER]:)

Duly authorised person

Signed by)
for and on behalf of [CONTRACTOR]:)

Duly authorised person

Signed by)
for and on behalf of [ESCROW AGENT]:)

Duly authorised person

INDUSTRY STANDARD FORMS

Presented by Richard Ceeney



What I've been asked to speak about

- **Bodies Producing Standard Forms**
- **What forms are available**
- **What types of projects are they used on**
- **Words of warning**

What I'm actually going to speak about

- **Bodies producing standard forms**
- **Format of a standard form contract**
- **How commonly are standard forms used?**
- **Analysis of the most common forms**
- **Words of warning**

Bodies producing standard forms

- **JCT**
- **MF/1**
- **NEC**
- **AIA**
- **FIDIC**
- **ICC**
- **IChemE**

Format of a standard form contract

- **Contractual terms**
- **Commercial terms**
- **Appendices**
- **Contract documents**

How commonly are standard forms used

- **Why use standard forms?**
- **More suitable as a starting point**
- **Complex mechanisms**
- **Fully bespoke forms can be counterproductive**

Analysis of key standard forms

- **JCT**
- **NEC**
- **FIDIC**

JCT



JCT

- **Flexibility**
- **Approach/Style**
- **What kind of projects is it suitable for?**
- **Balance of risk**
- **Liability position**

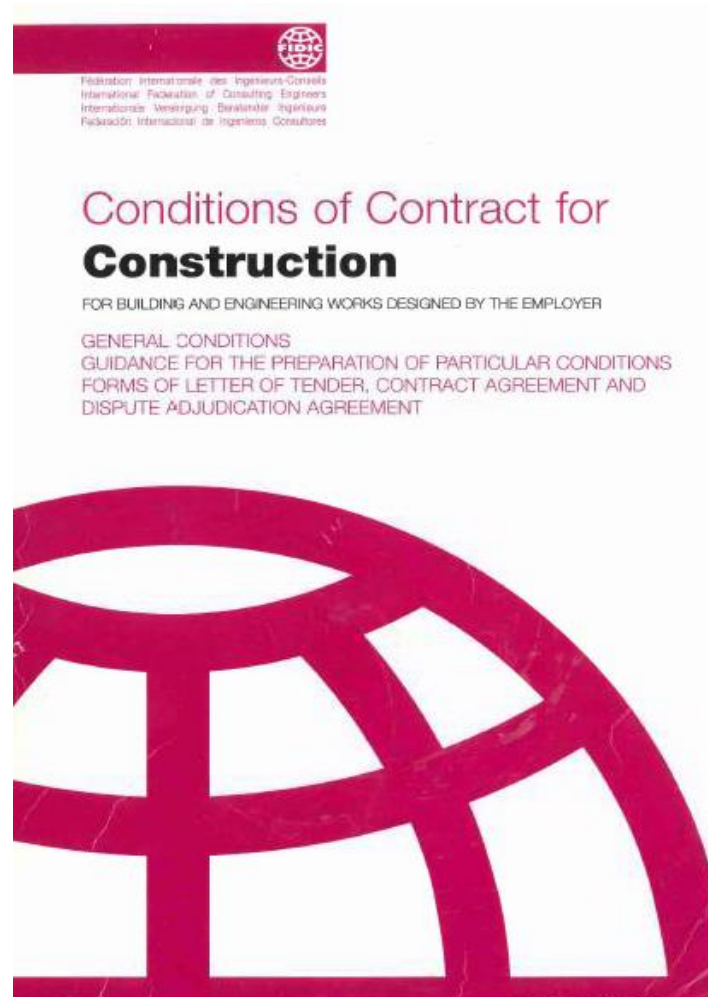
NEC



NEC

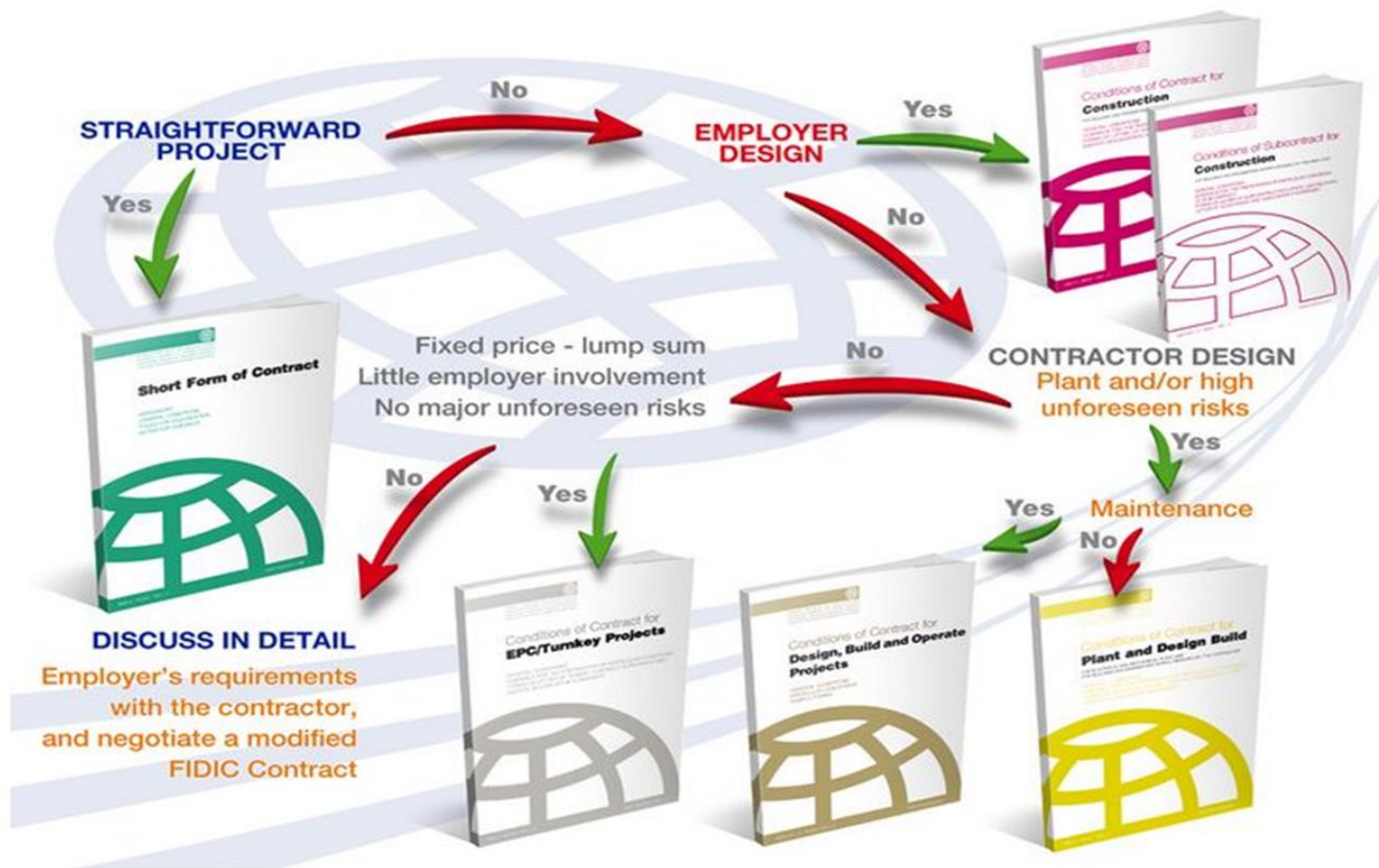
- **Flexibility**
- **Approach/Style**
- **What kind of projects is it suitable for?**
- **Balance of risk**
- **Liability position**

FIDIC



FIDIC

WHICH FIDIC CONTRACT SHOULD I USE?



FIDIC

- **Flexibility**
- **Approach/Style**
- **What kind of projects is it suitable for?**
- **Balance of risk**
- **Liability position**

A WORD OF WARNING...



Contracts as Tools

- **Balance risk & responsibility**
- **Use the mechanisms and make project-specific**

Guess the Contract Form?



Questions??





HERBERT
SMITH
FREEHILLS

CLLS – CONSTRUCTION FOUNDATION TRAINING Introduction to Construction Insurance

NOVEMBER 2019

Nicholas Downing, Partner and Head of Construction, Herbert Smith Freehills
+44 20 7466 2741, nicholas.downing@hsf.com

CONTENTS

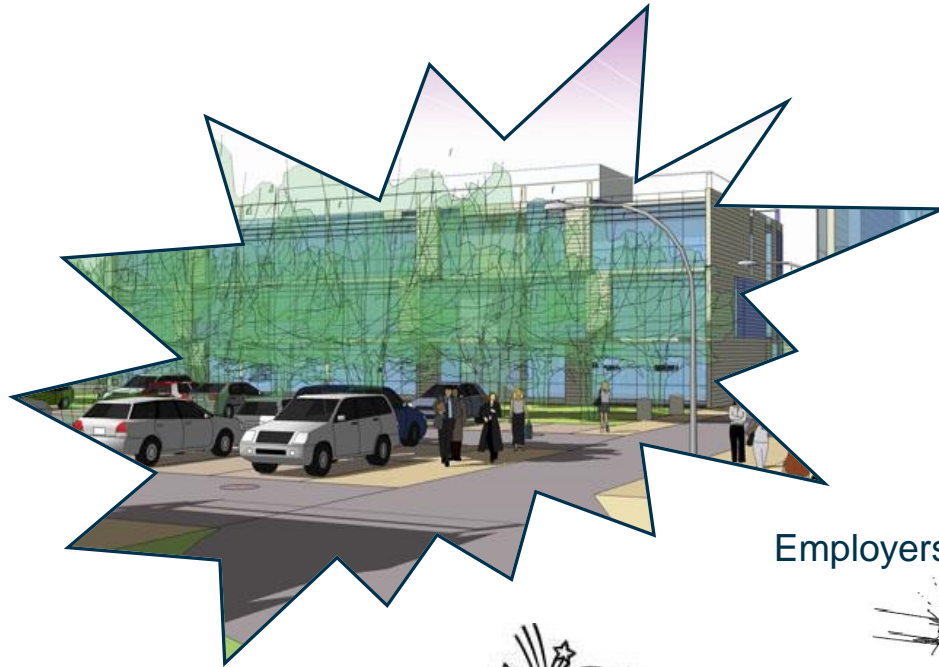
1. Types of Insurance
2. Insurance of the Works
3. Basis of Cover for Works
4. Delays to Completion
5. Insured Status
6. Standard Form Provisions – JCT 2016
7. Latent Defects Insurance

TYPES OF INSURANCE: LIABILITY

Directors & Officers



Professional Indemnity



Public Liability



Employers Liability



Property Owner's Liability



TYPES OF INSURANCE – MATERIAL DAMAGE AND CONSEQUENTIAL LOSSES

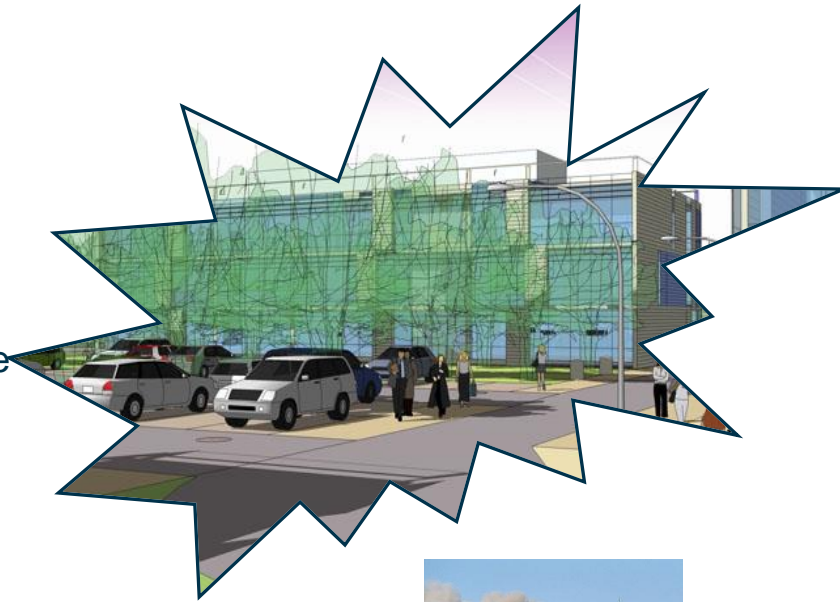
Contractor's All Risks



Property Damage



Delay in Start Up / Advance
Loss of Profit / Advance
Loss of Rent



Business Interruption



Terrorism Cover



TYPES OF INSURANCE – SPECIALIST

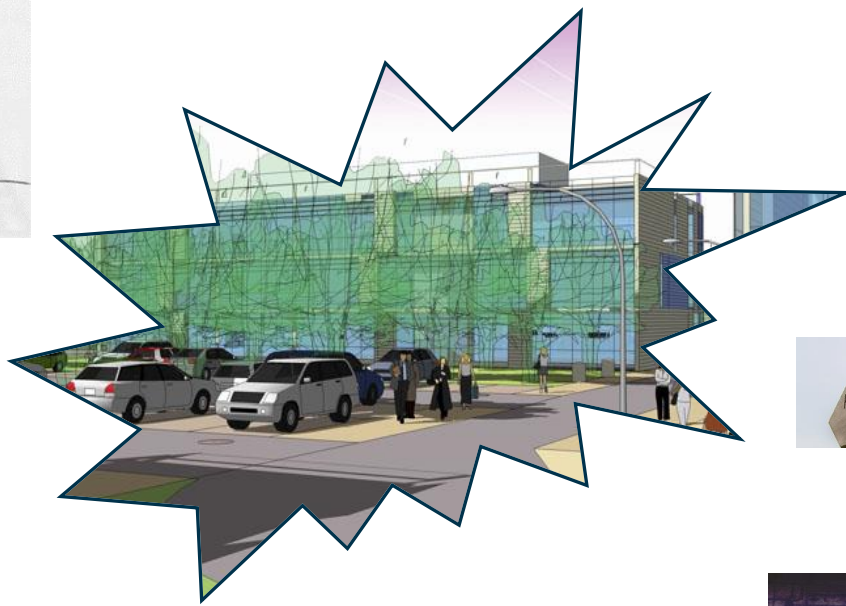
Chancel Repair



Right of Light



Restrictive
Covenant



Defective Title

Latent Defects



Environmental/Pollution



Planning Permission

INSURANCE OF THE WORKS

- First consideration is whether this is an owner controlled insurance programme (“OCIP”) or whether the contractor will arrange the insurance.
- Why opt for an OCIP? Allows an employer control over insurance arrangements (e.g. in respect of scope of cover, extensions to cover, costs etc.).
- High value developments will generally involve an OCIP.
- Assuming OCIP, usually all parties involved in the project are insured under the composite CAR policy (developer, contractor, sub-contractors and consultants in respect of site based activities only).
- Cover is to “...indemnify the Insured in respect of loss of or damage to the Insured Property occurring during the period of Insurance arising from any cause whatsoever except as hereinafter provided.”

BASIS OF COVER FOR WORKS

The Insured Property

Permanent works and temporary works including materials to be incorporated into each but not contractor's plant, tools and equipment

Location

At the site

The indemnity

Payment in respect of repair, reinstatement or replacement.

Duration

Up to the specified date / practical completion / handover / end of defects liability period – period is therefore important and be aware of interface with property damage policy

Exclusions

Must be fortuitous

Express exclusions, including DE1 to DE5 and LEG 3/06

DELAYS TO COMPLETION

- Contractor's entitlement to extensions of time
 - for loss or damage occasioned by any of the Specified Perils under JCT contracts
 - reinstatement can be a variation
 - operation of the contract (e.g. instructions to postpone)
- DSU/ALOP may be purchased as an extension to the CAR policy and, accordingly, may be a factor influencing the insurance strategy (OCIP/contractor led)
- Responds to an event of physical loss or damage that delays the commencement of the revenue stream the completed project will earn

INSURED STATUS

Co-insurance

Two types of co-insurance:

- 1) Joint insurance – only where identical insured interests
- 2) Composite insurance – applies where there are different insured interests:
 - Mortgagor / mortgagee
 - Landlord / tenant
 - Employer / contractor / subcontractor

Note that labelling a party as a 'joint' or 'composite' insured will not be definitive. Consideration must be given to the nature of the insured interests.

The phrases co-insured/composite insured/joint insured are often used interchangeably (and thus incorrectly) in the market.

STANDARD FORM PROVISIONS – JCT 2016

- **Clause 6 and Schedule 3**
- **Three options for insurance of the Works**
 - A – new buildings – All Risks insurance by the contractor
 - B – new buildings – All Risks insurance by the employer
 - C – insurance by the employer of existing structures and works

STANDARD FORM PROVISIONS AND PUBLIC LIABILITY INSURANCE – JCT 2016

- **Clause 6 – Public Liability Insurance**
- **Backs indemnities given to Employer**
- **Contractor to insure for death or personal injury**
 - Arising out of the works
 - Irrespective of negligence by a Contractor
- **Contractor to insure against damage to property**
 - Arising out of the works
 - Due to Contractor's negligence
 - But not as regards damage to existing structure

JCT COVERAGE (OPTION A)

Joint names policy (Contractor and Employer) for

•“All Risks” insurance

- Defined in clause 6.8

•Insurance against any damage to work executed and site materials excluding

- Wear and tear
- Failures in design or workmanship (NB DE1 to DE5)
- War and similar risks and
- Excepted Risks (nuclear and terrorism not covered by insurance)

•Full cost of reinstatement (i.e. no recognition of excesses, deductibles etc.)

JCT COVERAGE (OPTION A)

- Contractor's annual policy may be an alternative to project-specific cover
- Sub-contractors are recognised as insured or have waivers of subrogation in respect of loss or damage by Specified Perils (fire, flood etc.)
- Contractor's entitlement to an EOT is limited to loss or damage occasioned by any of the Specified Perils (note that the loss or damage does not need to occur to the works or at the site)
- Insurance proceeds are paid to employer and paid on to contractor following remedial work
- Contractor bears any shortfall in remedial cost

JCT COVERAGE (OPTION A)

- If Contractor defaults, employer can take out the policy then recover premiums
- Maintained until Practical Completion/Sectional Completion
- If terrorism cover ceases, employer may terminate or continue at risk
- Clause 8.11.3 – right of either party to terminate for prolonged suspension as a result of loss or damage to the works occasioned by any risk covered by the Works Insurance Policy or an Excepted Risk

JCT COVERAGE (OPTION B)

- Employer takes out joint names policy
- Cover is as for Option A
- If employer defaults, contractor can take out the policy then recover premiums
- Remedial works are a Change/Variation so that if there is a shortfall in recovery the employer bears the risk (reverse of Option A) and the contractor will be entitled to an EOT/loss and expense
- Note clause 5.6 where compliance with a Change/Variation instruction gives rise to a substantial change in the conditions under which any other work is executed

JCT COVERAGE (OPTION C)

- **Employer takes out policy for existing structures**
 - For losses due to Specified Perils
 - E.g. fire, flood, burst pipes, but not Excepted Risks
 - This coverage is not duplicated by Contractor's insurance against damage to property
- **Employer takes out policy in respect of the Works**
 - For All Risks as defined above
- **Same insurers for existing structures and the Works?**
- **Replacement Schedule may be needed if tenant is insuring**

JCT COVERAGE (OPTION C)

- **Payment of insurance monies as for Option A but**
 - Contractor's employment may be terminated by either party after loss or damage to existing structures "if it is just and equitable" within 28 days
 - If not terminated, remedial work for reinstatement of the works is treated as a Change/Variation then as for Option B
 - Neither party has a duty to reinstate loss or damage to the existing structures

MATERIALS BOUGHT BY EMPLOYER PRIOR TO DELIVERY TO SITE

- Contractor responsible for loss or damage to materials and costs of storage, handling and insurance until delivered to site
- Clause 4.15.2 of JCT 16 D&B/4.16.2 of JCT16 SF (PXQ) – Contractor to provide reasonable proof that relevant off-site materials are insured against loss or damage under a policy of insurance *protecting the interests of the Employer and Contractor* in respect of Specified Perils
- Contractor remains responsible for loss or damage to materials from delivery subject to insurance arrangements for the works

LATENT DEFECTS INSURANCE

- Taken out in respect of new build to provide cover in the event of an inherent defect in design, workmanship or materials becoming apparent after PC.
- Provides cover for 10-12 years from later of (a) PC or (b) certification by the insurers' technical auditor that it is satisfied with the quality of design and construction.
- Cover provided against defects in the structure of the building which are undiscovered at PC (load-bearing structures necessary for the stability and strength of the premises and external envelope).
- Extensions to basic cover can be purchased for an additional premium (e.g. mechanical and electrical services, loss of rent).

LATENT DEFECTS INSURANCE

- Exclusions from cover will usually include (subject to extensions):
 - defects in non-structural works
 - defects for which the contractor is responsible during the defects notification period under the building contract
 - consequential or economic loss arising from the defect
 - known defects excluded by insurers.
- The policy is principally for the benefit of the building owner but can be extended to include other parties with an insurable interest (e.g. funders or tenants).
- Insurers usually have rights of recourse against the design and construction team.

CLLS – Construction Foundation Training

Introduction to Construction Insurance – Part II

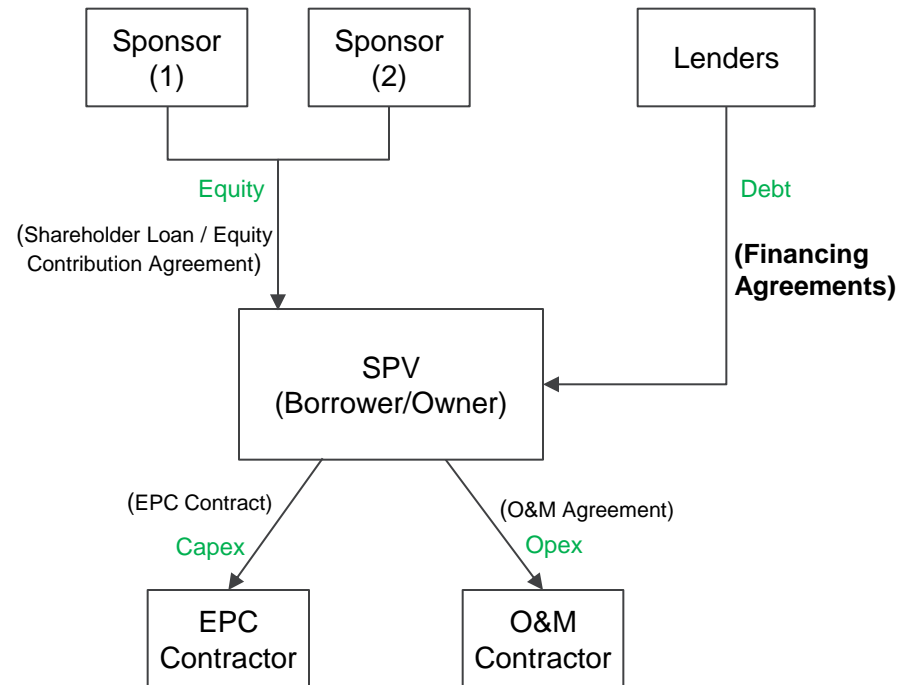
Chris Duncan, Counsel – White & Case LLP

Paddy Mohen, Senior Associate – White & Case LLP

15 November 2019

Insurance in project finance transactions

- Overview of project finance structure
- Risk allocation and role of insurance
- Role of lawyer and insurance advisors/brokers
- Different insurance for construction vs operations
- Different insurance required for different projects



Key construction insurances in international project finance

Construction All Risk (CAR) Insurance

- ❑ Risks covered: physical loss or damage to the works being constructed during the course of construction. Can cover other property during construction, including temporary buildings, construction plant and equipment, contractor's tools and equipment
- ❑ Who maintains: Employer
- ❑ Insured parties: Employer, Contractor (and Lenders)
- ❑ Period of cover: normally from start of construction until practical completion/handover
- ❑ Amount of cover: no less than the replacement cost of the works



Public Liability / Third Party Insurance

- Risks covered: Loss or damage to third party property or death or injury to a third party caused by negligence
- Who maintains: Employer often holds project wide policy, or may be held by Contractor
- Insured parties: if Employer led, will cover Contractor, Subcontractors and the Employer
- Period of cover: From commencement of the Works to Practical Completion and (sometimes) Defects Notification Period
- Amount of cover: Dependent upon situation and/or nature of the Works.

Marine Cargo Insurance

- Risk covered: lost or damage to plant/material during transit to site
- Who maintains: generally Employer (to ensure DSU coverage)
- Insured parties: Employer, Contractor (and Lenders)



Marine Cargo Insurance (cont'd)

- Period of cover: shipment of key plant/materials
- Interplay with project delay/DSU insurance
 - Key plant may have long lead times for replacement, which may delay the project
 - If loss/damage due to a force majeure event, contractor will usually be entitled to an extension of time (and potentially additional costs), in which case delay liquidated damages will not be payable under the construction contract

Political Risk Insurance

- Risks covered
 - Expropriation
 - Forced abandonment
 - Political violence, war
 - Exchange transfer restrictions preventing conversion and transfer of foreign exchange under a contract
- Who maintains: Employer
- Insured parties: Employer



Political Risk Insurance – example projects

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KENYA
Thika Power Limited

SPG | Power | Oct 12, 2018

The project will support Kenya's electricity sector by ensuring stability of electricity as well as enhancing energy security in the Thika industrial zone

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PAKISTAN
Hyundai Motor Pakistan Project

Project Brief | Manufacturing | Oct 01, 2018

The project involves the design, construction, and operation of a greenfield motor vehicle plant with an annual production capacity of 30,000 units. [READ MORE →](#)



SOUTH AFRICA
Scatec Solar South Africa

Project Brief | Power | Oct 01, 2018

These projects are expected to generate climate mitigation benefits by increasing renewable energy capacity in South Africa. [READ MORE →](#)



ARGENTINA
Vientos Los Hercules S.A.

Project Brief | Power | Oct 01, 2018

The project involves the design



EGYPT, ARAB REPUBLIC OF
Pasabahce Egypt Glass Manufacturing SAE

Project Brief | Manufacturing and Services |

Oct 01, 2018



ETHIOPIA
Tulu Moyo Geothermal Project

ESRS | Renewable Energy | Sep 05, 2018

This Environmental and Social Review

Delay in Start Up (DSU) and Business Interruption

- Risks covered: Loss of profit or other revenue related losses (including increased costs) arising from damage to the Works (which delay completion of the construction phase, or delay operation during the operation phase)
- Who maintains: Employer
- Insured parties: Employer (and Lenders)
- Period of cover: Linked to CAR policy
- Amount of cover: Variable depending upon nature of works and cost of coverage
- Points to note:
 - Excess/deductibles
 - Limits of indemnity
 - Relationship with any liability for delay liquidated damages



Construction insurance – lender concerns/requirements in limited recourse project financing

Lender concerns/requirements

- Identity of insurer (and reinsurer, if necessary)
 - Required financial strength / minimum credit rating requirements
 - Compliance with local law, including to insure with local insurers
 - Direct access / cut through rights to re-insurers
- Scope of insurance cover
 - Risks, exclusions and amounts to provide comprehensive coverage
 - Deductibles not exceeding pre-agreed amounts
- Being entitled to receive proceeds of a claim
 - Lenders (or agent) being named as an additional / composite / co-insured
 - Lenders (or agent) being a loss payee
 - Non-vitiation (whereby non-compliance with policy conditions by other insured(s) will not prejudice rights of others under the policy)

Lender concerns/requirements (cont'd)

- Control over insurance proceeds
 - Having security over the rights in respect of insurance
 - Proceeds going to correct accounts
 - Mandatory prepayment / “head to the hills provisions” in the event of catastrophic loss events
- Waiver of subrogation rights
- Insurances being in place when required
 - Broker’s letter of undertaking

Broker's letter of undertaking

- Broker – acts as an adviser on matters of insurance and as an arranger of insurance cover with an insurer on behalf of a client
- BLOU meant to be given when insurances are effected and renewed
- Confirmation that:
 - Insurances in full force and effect and premia paid
 - The endorsements included
 - The Lenders are named as additional / composite insured
 - Insurer has acknowledged notice of security assignment
- Undertaking to give notice of material changes and defaults in payment of premium.

Questions?



CLLS Construction Law Committee

Foundation Level Training – Day 3



The City of London Law Society

