



# CONSTRUCTION & ENGINEERING TOOLKIT

## Construction Insurance: taking an interest

### "Noting" and other ways in which interests in insurance policies can be protected

Finance parties and others interested in major construction projects will usually want to be able to take the benefit of the project insurance arranged by the developer or contractor, so that their position can be protected if the project is subject to a an insured loss. There are various ways in which this can be done. The mechanisms used will depend on a number of factors including the risks, costs involved, type of policy - and what the insurers are willing to agree. This briefing considers some of these mechanisms.

#### NOTING AN INTEREST

"Noting" a lender's interest on a policy used to be common practice. Under a protocol agreed with the British Bankers Association, insurers who were members of the Association of British Insurers (ABI) agreed to advise a lender whose interest had been noted if the policy holder failed to renew, or reduced, restricted or cancelled all or part of the cover. The insurers undertook to keep the policy in force providing the lender took responsibility for any unpaid premium. However that protocol came to an end on 31 December 2012, and UK insurers have not considered themselves bound by it in respect of any policy which has inception or renewed since then.

The result is that a bank now has no stronger protection than any other party whose interest is noted on the policy - in practice this is very little. Noting in itself does not afford the noted party any rights under the insurance policy. This means it will be left without protection should the insured invalidate the policy, unless further specific provisions are included.

## KEY POINTS ABOUT NOTING

The noting of an interest:

- Does not create a separate contract between the noted party and the insurer or create a binding obligation on the insurer to confer a benefit on the noted party.
- Is not sufficient to give the noted party any right to enforce terms of the policy under the Contracts (Rights of Third Parties) Act 1999 - (the 1999 Act) unless the policy is drafted to give the noted party an express right to enforce it, or contains terms purporting to confer a benefit on the noted party. The noted party will not be able to enforce the policy if it includes provisions expressly excluding the 1999 Act, or excluding the rights of third parties to enforce its terms. Insurance policies very commonly contain such provisions.
- Will not effect an assignment of the policy or its benefit to the party whose interest is noted.
- Will not necessarily prevent the insurer bringing a subrogated claim against the noted party.

## MAKING NOTING MORE EFFECTIVE

If a party does want to protect its interest by noting, it should make sure that clear terms are also included in the policy confirming what protections it will benefit from, and that the party is able to enforce those terms under the 1999 Act.

The following should be considered:

- a loss payee clause (see *Alternatives to Noting* below);
- a term specifically stating that the noted party is to be informed if a claim is made under the policy; or if the policy is not amended, renewed or cancelled,
- a term under which the noted party is able to pay the premium so the policy remains in force if the policy holder has defaulted
- a term stating that the insurer cannot bring a subrogated claim against the noted party.

## ALTERNATIVES TO NOTING

There are other ways of ensuring that a lender or other third party can benefit from an insurance policy:

### Loss payee clause

This is a clause in a policy requiring the insurer to pay any proceeds under the policy to a named third party, the 'loss payee' rather than the policy holder. From a lender's perspective, this is an improvement on having its interest noted on the policy.

However, the lender is still not a party to the insurance contract and therefore cannot enforce compliance by the insurer, unless he can take advantage of the Contracts (Rights of Third Parties) Act 1999. Further, unless other provisions are included the loss payee may not be able to recover if the policyholder's breaches have invalidated the policy.

### Composite policy i.e. "joint names"

Here, two or more parties with different and distinct interests in the subject matter can be insured under the same policy. Each party insures its own interest and can recover only the amount representing its own interest in the subject matter. If a lender is a "joint names" insured it may still be able to recover even if another insured party is in breach - ideally the lender will seek express terms under which the insurers agree that other insureds' actions will not vitiate its rights under the policy. Such clauses need to be drafted carefully to ensure that all potential defences that might be available to insurers are covered.

### Broker's letter

A letter from a broker may be relied upon by the parties to confirm what protection, if any, the insurance policy affords the lender or other party relying on it however such a letter will usually only give rise to a cause of action against the broker who has provided it, and very often the broker will seek to exclude or limit its liability under the letter as far as possible.

## DRAFT CONTRACTUAL TERMS CLEARLY

If you expect to receive some benefit from an insurance policy to which you are not a party, or intend to confer a benefit on a third party in respect of an insurance contract to which you are a party, consider carefully what you intend that benefit to be and seek insurers' agreement to appropriate provisions and protections in the policy.

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