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> Policy wording and exclusions left Baulderstone uninsured for defective workmanship, costing $65 million

Professional Indemnity insurance

Claim example: Construction of the third runway at Sydney Airport

The following is an example of a major construction project that had latent defects which were not discovered until some time after the construction phases. The importance of proper insurance coverage is evident from the facts below.

Background

In 1992, the Federal Airports Corporation, the predecessor to Sydney Airport Corporation Limited (Sydney Airport), appointed Baulderstone Hornibrook Engineering (Baulderstone) as the contractor for the design and construction of the third runway at Sydney airport.

Baulderstone constructed a 7 kilometre retaining wall along the third runway at the airport in 1994 at a cost of $200 million. Within a year of the construction being completed, it became evident that there were subsidence problems with the seawall and retaining walls (the walls). The walls were supposed to be maintenance free and last for a period between 50 to 100 years. Instead, sand was blowing out between the joints into Botany Bay.

In 2002, Sydney Airport brought legal action against Baulderstone and those proceedings were settled in 2004 on the basis that Baulderstone would rectify the walls. The estimated cost for carrying out the rectification works exceeded $60 million.

Insurance claims

After the settlement with Sydney Airport, Baulderstone sought indemnity under its project specific professional liability policy for approximately $50 million. Baulderstone settled the claim with certain insurers but two of the insurers denied indemnity so Baulderstone sued them. The primary issue for determination in the proceedings was the cause of the loss of sand from the walls.

Baulderstone argued that negligent design by their sub-contractors was the cause of the loss. The walls were constructed with prefabricated concrete facing panels. The joints between the panels were sealed with a geotextile material through which water, but not sand, could flow.

Behind the concrete panels was sand backfill which was required under the contract to be compacted to a uniform 80% density. Baulderstone contended their action in prescribing the use of the geotextile material (which the claimant argued was 'negligence') was a matter covered under the policy. The insurers, on the other hand, argued that the cause of the loss was not negligent design but defective workmanship in the compaction of the backfill by Baulderstone. Loss arising from defective workmanship was excluded under the policy.



The key question became – which was the dominant cause of the loss? Were the two causes concurrent causes? The general principle at common law is that where there are two or more proximate or dominant causes of loss, but one of those causes is the subject of an exclusion, the insurer is not liable to indemnify the insured for the loss, notwithstanding the fact that the other cause of the loss is not an excluded loss and falls within the ambit of policy coverage. Ultimately, based on the facts and the particular wording of the policy, the court held that the loss was caused by defective workmanship and the insurers were therefore entitled to deny indemnity for the entire loss. The court said that the loss was caused not so much by the use of the geotextile material but by the failure of Baulderstone to take appropriate steps during the compaction of the sand backfill to ensure that this compaction would not adversely affect the geotextile material.

Multiple causes of loss – are you at risk?

The Baulderstone case demonstrates the importance of the precise wordings of professional indemnity liability policies in major construction projects. The costs of rectification works in major projects are often extremely high. Where a claim of loss involves multiple causes and one is an excluded cause, costly and protracted negotiations, and possibly litigation may ensue between the insurer and the insured in determining the dominant cause of the loss.

At the end of the day, whether or not a claim involving multiple causes might fall outside of a policy depends very much on how the multiple causes interrelate in relation to the loss and the precise wording of the relevant exclusion clause.

Liberty's solution

Liberty offers a unique solution to our Design & Construct insureds in claims involving multiple causes of loss. In our Professional Indemnity Insurance policies for D&C Contractors and Construction Projects, we have included an automatic extension which provides that, where there are a number of causes which contribute to the loss for which a claim is made, Liberty will indemnify the insured in respect of that part of the loss which is covered under the policy notwithstanding that one or more of the other causes is excluded under the policy. This is important in the event of a claim involving multiple causes of loss.

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