



# COMMUNIQUÉ

*Newsletter of the New Zealand Architects Cooperative Society Ltd  
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## **PROFESSIONAL INDEMNITY INSURANCE COVER 2003**

*Graham Strez puts the record straight.*

The **NZACS** – arranged Professional Indemnity Insurance policy and Subscription for 2002/2003 has now reached most Member Firms.

In today's insurance market there should have been no surprises, particularly after reading the Chairman's letter. Statements on *NZIA Chatline* suggest otherwise.

I comment to clarify issues for Members.

1. **Architects like other professionals practice in an increasing risky and litigious environment.**
2. **Architects have a freedom of choice to either have their risk underwritten by an insurer, or accept the risk themselves i.e. to risk losing their assets.**
3. **The majority of architectural risks fall within the policy excess. Even so, this entails an administrative and /or subsidising cost to NZACS.**
4. **A substantial number of claim notifications are settled within the range of \$50 - \$100,000; a few lie between \$200 - \$600,000. Claims in excess of \$1,000,000 are not unknown.**
5. **Insurers, like Architects, operate in a commercial and litigious environment. They have suffered significantly by global economic constraints and insurance disasters – Sept 11, 2001 and its loss of aircraft, life and business continuity; oil tanker sinking and oil pollution, climate disasters and asbestos related claims.**
6. **Internationally, many insurers are withdrawing from unprofitable insurance portfolios. Those few who remain in the specialist liability insurance market are imposing tougher conditions and higher premiums. There is a limited market for liability coverage in New Zealand and Australia.**
7. **Within New Zealand insurers are nervous about the implications of the “Leaky Building Syndrome” and its currently unquantifiable potential liabilities. Most “standard “ liability policies available now seem to exclude any loss, which occurs as a result of water entry causing rot or fungal decay, moisture deterioration and failure to comply with the NZ Building Code.**

*What cover is this?*

8. **Architects cannot dictate terms to an Insurer unless it is commercially attractive to the Insurer. It isn't. No statements of self-belief, or promises to reform will induce an Insurer to ignore the past performance of the Insured – the Architectural Profession. The Insurance loss ratio for each of the past five years has exceeded 100%, i.e. Insurers have paid out far more than they have received in premiums.**
9. **Accordingly, premiums were due for a hike anyway, without the added threat of “Leaky Buildings.”**
10. **NZACS has engaged in substantial negotiation with a number of Insurers to obtain a meaningful cover for Architects. The current Insurer, Lumley's, provided a receptive ear and was able to bring their Reinsurers along with them. Other Insurers were not receptive.**
11. **The NZACS policy contains an exclusion for loss arising from the use of timber with a preservative treatment less than H3. At least there still remains cover for water ingress causing damage.**
12. **It is important to view this exclusion in the context of claims. NZACS statistical records suggest there is little numerical risk of claims falling within the leaky building category. Some that do, however, have been expensive.**
13. **Most small scale leaks – e.g. bathroom floors, overflowing gutters, leaking windows etc, fall within the insurance excess – i.e. the insured firm's excess or NZACS layer. Architects would fund these costs now, as they have done previously.**
14. **If Architects enter into appropriately qualified conditions of engagement and provide adequately detailed and specified documents, and undertake thorough project observation, they should have little to fear from the “below H3 exclusion.”**
15. **In general terms Policy exclusions are subject to interpretation in accordance with the Insurance Reform Act which states, inter alia, that for the exclusion to apply the excluded cause must be material to the loss. In this instance the use of timber treated below H3 must be the cause of the insurance loss, not that the building leaked causing material damage and there was unaffected untreated timber framing, nor that the overweight structure was built from untreated framing, nor that the burnt building was constructed from untreated timber.**
16. ***Hypothesise*; if a house was constructed with say H1 treated framing, with bottom plates separated from the concrete floor by malthoid strip, with timber weatherboard cladding or drained/ventilated cavity to Harditex or stucco cladding with appropriate movement control joints and flashings, there should be little more than localised timber framing damage resulting from water leaks – i.e. minimal repair costs.**

17. Perhaps NZIA/AAS may need minor modification to endorse (say) the requirement for H3 framing to bottom plates and exterior framing, or have the client accept responsibility for the consequences of using untreated timber.

*(The Building Code's acceptable solution may exclude the use of untreated framing anyway in the near future.)*

18. The NZACS policy provides for one automatic reinstatement of cover – against the unlimited reinstatement that applied previously. Only two claims in 1500 (during the last 30 years) have exhausted the first level of indemnity. If Architects are concerned as to whether they have adequate cover, they can always increase their level of indemnity.
19. The NZACS policy now includes legal defence costs within the level of indemnity. (Previously these costs were additional to the indemnity provided.) Legal and expert witness costs are increasing steadily, and not uncommonly reach \$30 - \$50 - \$80,000 plus. This can be compensated for by increasing the level of indemnity sought. This aside, most claims can be resolved without recourse to legal costs. We suspect “Leaky Building” claims will have a high cost component, just to remove the Architect from the proceedings.

### *Comments in response to recent chatline questions.*

20. *“The Insurers are elevating the standard of the NZ Building Code's acceptable solutions.”*

The insurers are not. All they are saying is that as a result of “Leaky Building Syndrome,” they wish to protect their commercial interests by incorporating the exclusion for timber treated below H3.

21. *“There is conflict between the NZIA Practice Alert “Timber Treatment & Rot” and insurance policy requirements”*

Again, no conflict. The insurers just wish to take more care in controlling their risk.

22. *“Insurers are making up for past losses by increasing the premium and reducing the service provided – e.g. H3 exclusion, one automatic reinstatement, legal defence costs included within indemnity.”*

The present Insurer has only one year's insurance experience with NZACS. They therefore have not raised their premiums to cover earlier losses. Premiums have risen to reflect the risk to Insurers. NZACS has endeavoured to minimise the premium contribution from Member Firms, and to obtain useful policy coverage. Both NZACS and *Acanthus* have been subject to payouts, which have far exceeded the premium pool. No organisation can continually trade at a deficit.

23. *“NZIA has no statistical data on failures of architects own making, compared with the making of others.”*

NZACS has this data, and it is commercially sensitive. Whilst broadly the professional risk to Architects is low, the commercial consequences can be very high – e.g. *where the builder or property developer goes into liquidation.*

Through the legal doctrine of “*Joint and Several Liability,*” the deepest pockets of insured professional and territorial authority are those that end up paying the majority of the claim. Architects and Insurers have no control over this.

It is for this reason that both NZACS and NZIA have been seeking to have the joint and several liability removed from our common law reference and /or alternatively to have professional liability limited on the basis of proportionate liability.

### *What are our options?*

24. The reality of our situation is that there are none. NZACS has, in conjunction with AON, its Insurance Consultants, sought to obtain an insurance cover that affords qualified protection against the “*Leaky Buildings Syndrome.*” We have used our claims history to ensure that the vast majority of our Members need not be concerned about the qualified protection provided.

All insurers have raised premiums. Market forces are at work. We are aware that one or two insurers have lower premiums than the NZACS Insurers, but the quality of their policy and their claims procedures are wanting by comparison and there are concerns about their commitment in the long term to maintain the cover required.

NZACS Directors are also Principals of architectural firms insured under the NZACS scheme. What is good for the members of NZACS is also good for their firms.

The current deal comes with their unanimous support.

### ***COMMUNIQUÉ***

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***We welcome contributions from readers, on how they manage risk.***