

# Unwise approach costs insurer

**Ann Levin** and **Kemi Adekoya** of **Herbert Smith Freehills** explain the background to an appeal court ruling that is thought to be the first time it has considered the wording of a type of insurance policy in common use in construction.

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### KEY POINTS

- The Court of Appeal provided guidance on the interpretation of 'product' and 'superstructure' in composite public and product liability insurance policies
- The hallmark of a product will be that it is something tangible and moveable that can be transferred from one person to another
- A 'superstructure' is not limited to buildings above the ground
- The court expressed reservations as to the appropriateness of granting insurers declarations of non-liability where the facts giving rise to liability had not yet been established

The Court of Appeal in *Aspen Insurance UK Ltd v Adana Construction Ltd* [2015] EWCA Civ 176 provided guidance on the interpretation of a contractor's combined liability policy. Of significance was the court's guidance on the definition of 'product' under the product liability section of the policy in a construction context. It is understood that this case presented the first opportunity for the court to consider the wording of this type of policy.

### The facts

Adana was the construction sub-contractor in relation to works at King's Dock Mill in Liverpool. It was responsible for the supply (but not the

design), delivery and installation of a concrete crane base. Four reinforced piles which had already been constructed by another company were in place when Adana began their work. Adana's work involved drilling holes into each of the piles and then inserting reinforcing bars known as 'dowels' into each of those holes. The dowels were to protrude from the top of each pile and form a connection with the crane base. Concrete was then poured into a shuttered area immediately above the piles, such that each of the dowels was included in the crane base. The pile caps would support the crane legs and the dowels would resist upwards tension (ie preventing one side of the crane being pulled upwards with the other side being pushed down).

Once Adana had completed its work a crane was erected on the crane base. Subsequently another, heavier, crane was erected on the crane base. On 6 July 2009 this heavier crane fell backwards seriously injuring the crane driver, and causing significant damage to neighbouring properties and the crane itself.

Several claims were brought against Adana, the main contractors, and the structural design engineers on the project. At the time of the Court of Appeal judgment these proceedings were still in progress. Expert evidence suggested that the collapse was due to a failure of the connections between the crane base and the piles. Whether that failure arose because of faulty design (for which Adana was not responsible) or because Adana had failed to follow the specification for the dowels had not yet been decided.

Aspen, who were Adana's insurers under a 'Miles Smith' Building Services Combined Contractors' Liability Policy, sought a declaration that they were not

liable under the policy. Therefore, the Court of Appeal was only concerned with deciding whether there was policy coverage.

### The terms of the policy

Product liability cover is often packaged together with public liability cover. In the construction context such insurance is often required from the supplier of products incorporated within the structure of a building. The policy wording in Adana's policy was typical of such policies.

Under Adana's policy, public liability cover was provided for personal injury or damage to property. Loss or damage for 'faulty or inefficient workmanship, materials or design' was covered (save for 'making good'). However, loss caused by a product was excluded. Instead, product liability cover was provided in respect of liability for personal injury or property damage caused by a product, albeit on a limited basis, as the policy included what is often referred to as an 'efficacy exclusion'. This provided that there would be no cover where the product failed to 'fulfil its intended function.'

The Policy also had a 'foundation clause' which provided that there would be no cover in respect of 'loss of or damage to any superstructure' arising out of the foundation works failing to perform their intended function.

### Defining the product

Aspen argued that any liability Adana had arose from a fault with the crane base and contended that the crane base was a Product and therefore excluded from public liability cover. Aspen also argued that there was no liability under the product liability section because any such liability arose in connection with the failure of the product to fulfil its intended function. Aspen further argued that each of the constituent parts of the crane base was a product and each had failed to fulfil its function.

Adana's policy, as is common in policies of this kind, defined a product as

'any product or goods manufactured, constructed, installed ... by or on behalf of [Adana] ...'

The High Court judge declined to make the declaration sought by Aspen. He concluded that

neither the crane base nor the dowels were a product under the policy. He found that Adana had not supplied a product within the meaning of the policy, but rather created the base by pouring concrete in situ, after which it came into existence as a 'lump of concrete'. It was not one of Adana's range of products in that it could not be bought. As for the dowels, the judge considered that they were perhaps component parts of the piles once secured within them, but they were not part of a wider product.

Although the Court of Appeal supported Aspen's submissions that nothing in the definition required a product to be part of an Adana range, the court none the less agreed with the High Court judge in finding that the concrete base (including the dowels within it) was not a product.

In coming to this conclusion, the court provided useful guidance on the meaning of 'product' but stressed that it was not attempting a precise definition. The court stated that the hallmark of a product will be that it is something tangible and moveable that can be transferred from one person to another, and not something which only came into existence to form part of the land on which it was created. The court found that Adana was not reasonably to be regarded as having constructed a product but rather it had carried out concreting works for the purpose of securing a foundation for the crane on and in the site. The fact that the works created something did not mean that everything created should be regarded as a product.

The court overturned the decision at first instance in respect of the dowels and held that these were products. That they were incorporated into the crane base, which itself was not a product, did not matter. If Adana had any liability which arose because of a defect in the dowels, this would be excluded from the public liability cover and instead included in the product liability cover, subject to the efficacy exclusion.

Given the facts of the case, the court did not need to consider whether the efficacy exclusion applied. The dowels had not broken and had been pulled out intact. It was not the dowels that had caused the crane to collapse, instead it was the fact that the holes in which the dowels had been inserted were not drilled deeply enough. Adana's liability (if any) would not have been caused by the dowels but by faulty workmanship in not installing them properly.

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The court noted that, although the definition of product in the policy included a product installed by Adana, this did not mean that product liability cover extended to defective installation, rather there had been faulty workmanship which would be covered under the public liability cover.

Although the court did not have to deal with the application of the efficacy exclusion, it did find obiter that the dowels had not failed to fulfil their own intended function as they neither broke nor fractured. Although the entire load bearing structure as a whole had failed to fulfil the function of keeping the crane upright, this did not mean that each component part had failed to fulfil its function.

### Foundations and superstructures

Aspen argued that it could not be liable to cover Adana for damage caused to the crane itself as this was a superstructure and therefore fell within the exclusionary ambit of the foundation clause. The High Court judge, adopting a literal interpretation of 'superstructure', accepted Adana's arguments to the contrary. He found that a superstructure in its construction sense meant a building above the ground, foundations being permanent features which supported that building, and so a crane was not a superstructure.

The Court of Appeal took a more purposive approach to the interpretation of 'superstructure' and found that the crane was indeed a superstructure.

First, the court noted that the foundation clause was intended to operate within a general building contractors' liability policy which could be expected to cover work incidental to the substantial building work, such as the erection of a crane.

Secondly, the clause referred to 'any superstructure' suggesting it did not only apply to buildings. Simply, if it had been so limited, it would have said so.

Thirdly, the foundation clause did not limit the nature of the foundation works included. In constructing the crane base, Adana was carrying out foundation works in relation to the crane which formed the 'structure', on top of ('super') the base.

Finally the court dismissed the idea that, because the crane base was only intended to be there temporarily, this meant it was not a superstructure.

### Favoured in the decision but chided in the costs

The Court of Appeal upheld Aspen's appeal to the

extent of granting the declaration of non-liability on the basis of the foundation clause.

The declaration was to the effect that:

- the crane was a superstructure;
- the works carried out by Adana in fabricating the crane base were foundation works under the policy; and
- any liability that may be established against Adana in respect of the damage to the crane was excluded from cover by virtue of the foundation clause.

Clarke LJ reiterated the scepticism he shared with the High Court judge as to the appropriateness of making such a premature negative declaration. He noted that there was something artificial in making a declaration on the basis of an assumption of liability that may well be wrong. Gloster LJ also expressed:

*'grave reservations as to whether it was appropriate to determine the coverage issues on the basis that, necessarily, many of the facts were assumed or uncertain'*.

In its judgment on costs, the court made clear that there was limited benefit in the declaration that Aspen had secured. In establishing that there was no coverage for damage to the crane, Aspen had established that it would not be responsible for around £1.7 million of claims valued at around £23 million; whereas the policy had a limit of indemnity of only £5 million. Clarke LJ admonished Aspen's 'unusual' and 'commercially unwise' approach. Inter alia, the Court of Appeal awarded Adana 85% of its costs of the appeal.

### Conclusion

Though this case turned largely on its facts, the court did give some helpful guidance on the meaning of 'product' and 'superstructure' in the context of public/product liability insurance and the application of the efficacy exclusion which commonly appears in the product liability policies. Ultimately, the court will seek to give these words their natural meaning while looking at the policy as a whole. The case highlights the risks for insurers in seeking declarations of non-liability before the facts of a matter have been established. Although, in this case, the insurer obtained the declaration sought, the court made explicit its reservations in granting the declaration and made an adverse costs order against the insurer. **CL**