

# Liability Insurance

**This fact sheet has been prepared to help smaller companies in the construction sector to understand better how liability insurance is sold and priced. It also provides details of sources of further information on this topic and a glossary of liability insurance terms.**

## Introduction

One of the basic principles of insurance is that the premiums paid by the many should cover the costs of the claims made by the few. In today's claims conscious environment however the cost and numbers of claims, particularly liability claims, has risen so sharply that the size of the insurance fund has to be increased and everybody has to contribute more.

Liability policies are insurance products that provide insurance cover for the damages awarded and the legal costs of claims made against your business under liability law. Such claims can arise under the laws of negligence, nuisance and contract. It is a complex area and it is important that you have some understanding of the nature of liability insurance products.

The main liability products that this factsheet is concerned with are Employers' Liability (EL) and Public and Products Liability (PL/Products) insurance.

## Employers' Liability Insurance

EL covers employers against liability claims from their employees for accidents or ill health that they may suffer whilst working and that are due to the negligence of their employers.

Insurance contracts are drawn up under the principle of "utmost good faith", as insurers must be fully aware of the nature of the risk that they are insuring.

It is therefore important that the description of your business that you give to your insurers via your broker includes all of your activities.

EL is a compulsory insurance that all employers are required to have under Employers' Liability (Compulsory Insurance) Act 1969. It was introduced to avoid employees who had suffered injury or illness being unable to recover compensation due to a company's insolvency. By law you must have EL insurance with a limit of indemnity of at least £5 million, most policies provide £10 million.

EL provides cover in respect of injury or disease caused during the period of the policy. Hence the policy that is in force at the time the injury to the employee was caused will deal with the claim, irrespective of when the claim is actually made against the employer. EL will therefore cover you for claims for ill health made in the future due to exposures that may occur today but do not manifest themselves during the current policy period e.g. asbestos related diseases.

Your insurance should cover all employees, including contract staff, casual and temporary workers.

As a compulsory insurance only a few restrictions e.g. exclusions or warranties are allowed. EL insurance does not cover exposure to nuclear radiation or risks which should be covered by motor insurance.

## Public and Liability /Products Insurance

Public liability (PL) and products liability insurance are generally, but not exclusively sold together.

PL covers your business for damages payments and legal costs of bodily injury to third parties and damage to third party property caused negligently during your business activities. It covers claims from members of the public, visitors, passers-by, trespassers, bona fide sub contractors both on your own premises and at third party premises where you or your employees may work.

Product liability insurance provides cover for third party bodily injury and damage claims arising from any defects in products you may design, manufacture or supply.

PL/Products is not a compulsory class of insurance and typically policies can provide between £1 million and £5 million cover, but more can be negotiated.

There are many conditions, exclusions and warranties that can be applied to PL/Products policies and it is therefore important that you are aware of any that are applicable to your policy. For example:

- A standard PL policy does not indemnify against claims for financial loss where there has been no injury or damage, but any financial loss to the claimant flowing directly from an injury or damage claim is covered;
- You may be required to or “warranted” to act in a certain way when undertaking certain hazardous activities e.g. to operate a “hot work” permit system if you carry out work such as welding at third party premises;
- Most PL/products policies exclude gradual pollution damage and only cover pollution damage caused by sudden and unforeseen events;
- Certain activities are excluded from policies by endorsement because they are insured under other insurance arrangements e.g. aircraft, ships, advice given for a fee;

- Product policies may be endorsed to exclude the so called “efficacy risk” i.e. where damage is inevitable if the product fails to perform its intended function e.g. rust inhibitor, fire alarms.

## How is liability insurance sold?

Liability insurances such as EL and PL/Products can be purchased on their own or as part of insurance packages that include other commercial insurances such as insurance for buildings and contents, money and business interruption. Package policies are generally more suitable for small and medium sized or less hazardous construction businesses.

Whilst you may be able to get liability cover directly from some insurers for a construction business it is probably best to seek the advice of an insurance agent or intermediary. An agent should be able to advise you of the cover you require and have access to insurance providers who can provide suitable products for your needs.

Further guidance on finding an agent can be found in the Guidance Pack.

## How is my liability premium calculated?

Liability premiums not only have to cover the costs of claims but also the costs of reinsurance, agents’ commission, claims handling costs expenses as well as providing an element of profit to insurers. Such costs would be included in rates charged by insurers.

There are two main methods in which liability premiums can be calculated.

The first and most frequently used is called “book rating”. This starts with a base rate for specific trades that is applied to the risk exposure. For EL the exposure measure used is usually the estimated wage roll with turnover during the forthcoming year used for PL/Products.

Base rates are obtained either from the insurer's own experience for the trade and/or by using other data that may be available e.g. HSE statistics. They will also reflect the insurer's appetite for a particular type or size of business.

The base rate is used as the starting point for a premium calculation and this is adjusted according to the merits of an individual case for things such as:

- a good claims record;
- evidence of a positive approach to risk management; and
- size of risk.

It is therefore important that you provide your insurer with as much detail as possible of the way in which you manage your health and safety risk, as this will influence the premium charged.

Further information on this can be found in your guidance pack.

For larger construction businesses a "burning cost" method is used. In this approach the premium rate is based upon the actual claims experience of that risk over a suitable time period. This figure is then adjusted to take account of insurer's costs and expenses as well as possible changes that might affect future claims performance e.g. regulation or law reforms.

## Insurer additional services

Whilst premium and extent of cover are key features for you when deciding upon a liability insurance provider you should also consider the additional services offered to support your business particularly on risk management. Effective risk management will minimise claims and have the greatest impact upon your premium levels in the long term.

Many liability insurers in addition to dealing with claims offer advice and information on health and safety risk management issues by means of internet web sites and telephone help lines as well as providing free or fee paying on-site assistance by their Risk Control Survey Teams.

## Further help and information

A glossary is attached which explains in more detail many of terms commonly used in liability insurance.

Other sources of further advice and information on liability insurance for can be obtained from:

- Your insurer;
- Your broker.

Also from organisations such as

Association of British Insurers (ABI)  
51 Gresham Street  
London  
EC2V 7HQ

Tel: (020) 7600 3333  
Website: [www.abi.org.uk](http://www.abi.org.uk)

British Insurance Brokers' Association (BIBA)  
BIBA House  
14 Bevis Marks  
London  
EC3A 7NT

Tel: (020) 7623 9043  
Website: [www.biba.org.uk](http://www.biba.org.uk)

Institute of Insurance Brokers (IIB)  
Higham Business Centre  
Midland Road  
Higham Ferrers  
Northamptonshire  
NN10 8DW

Tel: (01933) 410 003  
Website: [www.iib-uk.com](http://www.iib-uk.com)

Constructing Excellence  
Website: [www.cbpp.org.uk](http://www.cbpp.org.uk)

## GLOSSARY OF LIABILITY INSURANCE TERMS

**ADDITIONAL PREMIUM:** A premium payable by the insured as a result of a change in policy cover or declaration adjustment to reflecting increased exposure or sums insured.

**ADJUSTER:** A person who investigates claims on behalf of insurers (see claims adjuster or loss adjuster).

**AGENT:** One who introduces a business to an insurer for commission, but can continue to act as an intermediary between the insurers and the insured.

**AGGREGATE LIMIT OF INDEMNITY:** The maximum amount an insurer will pay under a policy in respect of all accumulated claims arising within a specified period of insurance.

**ARBITRATION:** Settlement of a dispute by an independent person, whose decision is to be accepted by both parties. It is an alternative to legal action.

**ASSURANCE:** A term interchangeable with insurance but generally used in connection with life cover as assurance implies the certainty of an event and insurance the probability.

**BROKER:** An intermediary who acts as an agent for insurers and on behalf of the insured who is regulated by a professional body and codes of practice.

**CANCELLATION:** Termination of a policy before it is due to expire.

**CLAIM:** Injury or loss to a claimant against the insured arising so as to cause liability under a policy it has arranged.

**COMMON LAW:** The common law consists of the ancient customs and precedents that have been recognised by the courts and given the force of law. It is in itself a complex system of both civil and criminal, although it is greatly modified and extended by statute law and equity. It is unwritten and has come down over the centuries in the recorded judgements of courts.

**CONCEALMENT:** Deliberate suppression by a proposer for insurance of a material fact relating to the risk, usually making the contract null and void.

**CONDITIONS:** Stipulations written in a policy, with which a policyholder must comply. Failure to do so may result in insurers refusing to pay a claim.

**CONTRIBUTION:** When more than one policy covers the same risk, each insurer contributes by paying its rateable proportion of any loss.

**COVER NOTE:** A document issued to the insurer or agent confirming details of the insurance cover placed. Some cover notes are a legal requirement, e.g. motor.

**DAYS OF GRACE:** Number of days for which insurance cover continues beyond the actual expiry date of a policy, that you intend to renew. If you fail to pay the renewal premium within this period, your policy lapses.

**DECLARATION:** A signed statement by the insured, usually at the foot of a proposal or claim form, certifying that the information given is accurate.

**DECLARATION ADJUSTMENT:** If the premium has been calculated based on estimates provided by the insured, they are required to maintain records to enable a declaration of actual wage roll or turnover during the period to be made. The insurer may then adjust the premium charged for that period by making an **ADDITIONAL** or **RETURN PREMIUM**.

**DEDUCTIBLE:** The specified amount which the insured will contribute to any claim, also called excess or Insured's Contribution. As the insurer is dealing with the claim on the insured's behalf, they may require payment of the deductible prior to settlement with the claimant.

**DEFERRED PREMIUM:** The part of a premium which, following agreement with the insurer, is payable by instalments, monthly, quarterly or half-yearly.

**DUTY OF DISCLOSURE:** Obligation placed on someone taking out insurance, to inform insurers of anything that could influence their judgement on whether the risk is acceptable, or the terms to be offered.

**EMPLOYERS LIABILITY INSURANCE:** Insurance for employers in respect of their liability to

employees for injury or disease arising out of and in the course of their employment. With some exemptions this insurance is compulsory in Great Britain, and can only be provided by an authorised insurer.

**ENDORSEMENT:** An amendment or alteration to a policy, which becomes an integral part of that policy.

**EX GRATIA:** Payment made 'as a favour' by an insurer, when there is no obligation under the policy terms.

**EXCESS (or deductible):** Specified initial amount of a claim that the insured has to contribute. If a claim fails to exceed this amount stated in the policy, no payment is made by the insurers.

**EXCLUSION (or exception):** An event or circumstances specifically excluded from the terms of a policy.

**EXTENSION:** An addition to an existing policy to provide cover not previously considered or included, either temporarily or permanently..

**GROSS PREMIUM:** A term normally applied to gross written premiums before deduction of brokerage or commission and expenses.

**INCEPTION DATE:** The date from which, under the terms of a policy, an insurer is deemed to be at risk.

**INDEMNITY:** Insurance principle by which a policyholder is placed in the same financial position after a loss, as they were immediately before it.

**INSURABLE INTEREST:** The principle that the insured must have an interest, usually financial, in the risk for which the policy is to be issued.

**INSURANCE BROKER/AGENT:** An insurance intermediary who advises their clients and arranges their insurances. Although they act as an agent for their client, they will normally be remunerated by a commission (brokerage) from the insurer. An insurance broker is a full-time specialist in handling insurance business who belongs to a professional body and complies with their code of practice.

**INSURANCE PREMIUM TAX:** The Finance Act 1994 introduced this new tax on most general insurance risks located in the UK. All amounts stated on documentation should make clear the

amount of tax payable.

**INSURED:** The person, firm or company in whose name the policy is issued.

**INSURER:** An insurance company or Lloyd's underwriter who, in return for a premium agrees to provide indemnity in the event of any loss suffered by the person paying the premium as a result of some accident or occurrence.

**INSURER FINANCIAL RATING:** Rating of an insurer's financial strength and condition by an independent body e.g. A. M. Best, Standard & Poor.

**LAPSE:** The non-renewal of a policy for any reason.

**LATENT (GRADUALLY DEVELOPING) DISEASE:** An illness that lies dormant for some years before manifesting itself.

**LIABILITY:** Legal responsibility for injury to other persons or damage to their property.

**LIMIT OF INDEMNITY:** Maximum sum an insurer can be expected to pay under a policy or section of a policy. May be expressed 'per accident', 'per event', 'per occurrence', 'per annum', etc.

**LLOYD'S (OF LONDON):** A society, incorporated under Act of Parliament of 1871 and known as the Corporation of Lloyd's, which provides the premises for a wide variety of services, administrative staff and other facilities to enable the Lloyds market to carry on insurance business efficiently.

**LOSS ADJUSTOR:** Independent professional claims expert, who is engaged by insurers to impartially check and arrange settlement of claims in accordance with policy terms.

**LOSS ASSESSOR:** Person specialising in compiling and negotiating settlement of claims on behalf of the insured, by whom they are paid.

**LOSS:** Another term for a claim.

**MATERIAL FACT:** Any fact that could influence an underwriter in their acceptance of the risk, or calculating the premium.

**NAME:** Another term for an underwriting member of Lloyd's.

**NEGLIGENCE:** A form of tort or civil wrong that can give rise to civil liability.

**NET PREMIUMS:** Term variously used to mean gross premiums net of expenses, commission taxes, or any combination of these.

**NON-DISCLOSURE:** The failure by the insured or their agent to disclose a material fact or circumstance to the insurer before acceptance or renewal of the risk.

**OMBUDSMAN:** Official body, financed by participating insurers, to whom unresolved complaints can be referred.

**PERIOD OF RISK/INSURANCE:** The period during which the insurer can incur liability under the terms of the policy.

**POLICYHOLDER:** The person in whose name the policy is issued. (See also insured and assured).

**POLICY:** A document detailing the terms and conditions applicable to an insurance contract and constituting legal evidence of the agreement to insure. It is issued by an insurer or their representatives for the first period of risk. On renewal a new policy may not be issued although the same conditions would apply, and the current wording would be evidence by the renewal receipt.

**PREMIUM:** The consideration paid for a contract of insurance.

**PRO -RATA PREMIUM:** Charge for a number of days a risk is covered, calculated as a precise fraction of the annual premium.

**PROFESSIONAL INDEMNITY INSURANCE:** Insurance that indemnifies a professional against their legal liability towards third parties for loss arising from their professional negligence or that of their employees.

**PROPOSAL FORM:** Document completed by a prospective insured, giving details required by insurers to enable them to decide whether to accept the risk and what premium terms and conditions. Once agreed by both parties, it forms the basis of the insurance contract.

**QUOTE:** A statement by an insurer of the premium terms and conditions they will require for a particular insurance.

**RENEWAL:** Continuation of a policy for a further term, on payment of a fresh premium.

**RETURN PREMIUM:** A premium payable back to

the insured as a result of a change in policy cover or declaration adjustment to reflect reduced exposure or sums insured.

**RISK MANAGEMENT:** The identification, measurement and economic control of risks that threaten the assets of a business or other enterprise.

**RISK:** In insurance, this is the probability of an insured loss occurring.

**SCHEDULE:** Policy section setting out the main details of the insured, their business activities, the period of cover the application of any special terms or restrictions plus other details specific to the particular insurance and premium.

**STATUTE LAW:** Otherwise known as Acts of Parliament; which may create entirely new law, over-rule, modify, or extend existing principles of common law or repeal or modify existing Statute Law.

**SUBJECT TO SURVEY:** Phrase used by an insurer to signify provisional acceptance pending inspection by a surveyor whose report is then part of the assessment of that risk. The insurer reserves the right to vary or withdraw any offer as a result of the survey. The insurer may also make requirements or recommendations for risk improvement that will need to be complied with.

**SUBROGATION:** Insurer's right to pursue action in the insured's name against the party considered legally liable for the loss or damage.

**THIRD PARTY LIABILITY:** Liability of the insured to persons who are not employees of the insured.

**THIRD PARTY:** Person who is injured or whose property is damaged by the policyholder (the first party). The second party is the insurer.

**UNDERWRITER:** A person who accepts business on behalf of an insurer.

**UTMOST GOOD FAITH:** Duty placed on both parties to an insurance contract. The insured has to disclose all facts material to the risk while insurers have to act reasonably and communicate clearly.

**WARRANTY:** A condition which forms part of a policy and must be strictly complied with for a claim to be paid under the policy for example, use of a hot work permit