

Downstream Property Insurance: Accidental Damage



This article compares standard Property insurance cover available from downstream oil & gas underwriters with traditional Non-Marine market cover and considers certain coverage enhancements.

Introduction

The main coverage clause, in a downstream oil & gas Property insurance policy, ordinarily affords cover on an "All Risks" basis. However, notwithstanding the broad nature of "All Risks" cover, contentious debate can still arise regarding the extent of coverage available.

This article analyses certain issues that may give rise to disputes between claimants and insurers. The article also considers certain solutions that are available to policyholders when drafting and negotiating a downstream oil & gas Property insurance contract.

Latent Defects

In order to ensure that "All Risks" cover extends to include physical damage to sound subject-matter insured, sustained during the policy period and arising from a latent defect in other subject-matter insured, downstream oil & gas Property insurance contracts should expressly provide such coverage. This is ordinarily achieved by ensuring the policy wording incorporates terminology such as the following.

"It is understood and agreed that, notwithstanding anything to the contrary which may be contained herein or the clauses attached hereto, this Section is extended to include resultant physical loss of or physical damage to the property

insured arising from the latent defect of any part or parts thereof (including faulty or defective design, materials and workmanship) but in no case shall this insurance extend to cover the cost or expense of repairing, modifying, replacing or renewing such part or parts nor any cost or expense incurred by reason of betterment."

Leeds Beckett University v Travelers Insurance Co Ltd

At English Law, *Leeds Beckett University v Travelers Insurance Co Ltd* ([2017] EWHC 558 (TCC)) represents one of the leading Non-Marine Property insurance cases of recent years to address the issue of accidental damage coverage.

On the night of 13th December 2011 large cracks started to appear on the internal walls and ceilings of the University accommodation block. Subsequent investigations revealed that concrete blockwork, which supported the failed inner walls, had become saturated by groundwater and had *"turned into mush' with no structural strength at all"*. In 2012 the building was demolished.

Although the relevant insurance contract was an "All Risks" policy, the combination of the insuring clause and the definition of "Damage" required the claimant to show that the loss was caused by "accidental damage".

It was held that by the time the 2011 policy Year of Account had inceptioned, the damage which was to occur in December 2011 was inevitable in light of groundwater flows and the progressive weakening of the blockwork which had occurred since the building was built. The building being built in 1996 on the banks of the Leeds – Liverpool canal. Accordingly, the claim under the policy failed.

The judge drew various propositions from numerous pieces of case law. Of particular note were the following propositions.

- Accidental damage means damage that was caused by a chance event, against the risk of which insurance was taken out.

- Damage that was inevitable would not be fortuitous.
- Whether or not damage was foreseeable is irrelevant.
- Accidental damage does not mean damage to property due to the inherent characteristics of that property.
- There is a critical distinction between those cases where the damage was caused by an inherent weakness and those cases where it was caused by an external fortuitous event.

Accordingly, for the avoidance of any doubt, it will be appreciated why downstream oil & gas Property insurance contracts should **expressly** afford coverage for damage to sound subject-matter insured caused by other subject-matter insured containing a latent defect.

Subsequent Damage and Resultant Damage

The Property insurance policy at the centre of the *Leeds Beckett University* case contained a "Subsequent Damage" proviso as follows.

"The insurance provided under this Section does not cover... Damage caused by or consisting of... inherent vice latent defect gradual deterioration wear and tear frost change in water table level its own faulty or defective design or materials...but this shall not exclude subsequent Damage which itself results from a cause not otherwise excluded."

In the judge's view, "subsequent damage" had to be a reference to **different** damage, that is to say damage which could be distinguished in some way from the damage originally caused. Furthermore, the "subsequent damage" had to be caused by a **new or different cause** (and one which was not itself excluded).

Therefore, it will be appreciated, when drafting and interpreting downstream oil & gas Property insurance contracts, that an important distinction can be made between "subsequent damage" cover and "resultant damage" cover. In particular, unlike the judge's interpretation of the "Subsequent Damage" proviso in the case of *Leeds Beckett University v Travelers Insurance Co Ltd*, strong grounds exist to demonstrate that the above detailed downstream oil & gas "resultant damage" terminology does not require there to be a new or different cause.

Accidental Damage – Distinct Coverage

Notwithstanding the "resultant damage" coverage afforded by the downstream oil & gas policy terminology detailed within the *Latent Defects* section above, cover would not be provided for the cost of repairing physical damage sustained by the subject-matter containing the latent defect.

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However, subject always to specific policy terminology, certain sections of the Non-Marine underwriting community refer to "Accidental Damage" cover as denoting coverage distinct from that provided by a normal Property policy. Specifically, such "Accidental Damage" cover does not have to be triggered by an external event and can encompass physical damage sustained by the subject-matter containing the latent defect.

In recent years, a number of underwriters providing downstream oil & gas Property insurance coverage have demonstrated a willingness to agree to policy terminology affording such "Accidental Damage" cover absent of an external event and encompassing physical damage sustained by the subject-matter containing the latent defect. However, such "Accidental Damage" coverage is not intended to cover certain occurrences, especially those of a maintenance nature.

In the general Non-Marine underwriting markets, such "Accidental Damage" cover has remained distinct from "Breakdown" risks, with coverage for the latter remaining the province of specialist engineering underwriters. However, in view of the nature of downstream oil & gas Property risks, such "Accidental Damage" cover can be combined with the traditional "Breakdown" cover already provided within the standard downstream policy wordings.

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