

WINDOW PAIN - DAMAGE OR DEFECT? SEELE AUSTRIA GMBH & CO. v TOKIO MARINE EUROPE INSURANCE LTD [2008] EWCA Civ 441

In our Property & Construction Top Ten Insurance 2007 booklet we reviewed ten significant decisions during 2007, including the first instance decision of Seele Austria GmbH & Co. v Tokio Marine Europe Insurance Ltd. An appeal was heard in February 2008 and judgment was recently handed down. The decisions of both courts will be of interest to those concerned with contractor's all risks cover and the perennial issues of the interpretation of 'damage' and 'defect' under such policies.

Facts

Seele supplied and installed window units on a project where Tokio Marine provided joint names contractor's all risks cover. Shortly after installation the units were identified as defective and had to be modified. No damage as such was done to the windows nor to any other part of the works, save that cladding and internal finishes were necessarily disrupted in order to effect the modifications.

The policy covered loss of, or damage to, the insured property. Any loss due to defective design, materials or workmanship was governed by Memorandum 18. Memorandum 18(1) covered the cost of repairing loss or damage to the insured property. However, memorandum 18(2) excluded from the indemnity: (a) the cost necessary to replace or rectify the defective insured property itself; and (b) loss or damage to insured property free of defects unless it was unintentionally damaged in the course of enabling rectification of the defective insured property. Memorandum 18(3) stated that insurers would additionally indemnify the insured "in respect of intentional damage necessarily caused to the Insured Property....to enable the

replacement repair or rectification of Insured Property...which is in a defective condition".

Seele's primary argument was that 18(2) and 18(3) were independent and that 18(3) did not require that there had to be unintentional damage to the insured property before there could be cover for intentional damage that enabled repair of the defective insured property.

First instance

The court rejected Seele's argument. Mr Justice Field held that 18(1) to 18(2) began by providing cover for loss or damage arising out of defective work, then excluded the cost of repairing or replacing any defective insured property and the cost of intentional damage to enable repair. The clauses went on to create an exception to the exclusion if there was unintentional damage to insured property. In all cases cover was conditional on the works, or the works free of the defect, having been unintentionally damaged as a result of the defect. The fact that the windows were defective did not mean that the insured property itself was damaged. The Judge said, "in short, no damage no indemnity.

And damage here means not a defect in the works but an adverse physical effect on the physical state of the works as a result of the defect". The only additional damage that could be shown was the costs of removing cladding and internal finishes, but it was held that such damage was intentional and thus excluded. Seele's entire claim was therefore rejected.

Court of Appeal

The Court of Appeal decided that Memorandum 18(3) operated as a free-standing agreement, providing additional cover to sub-contractors (such as Seele) in accordance with its terms, and was not conditional upon the operation of clause 18(2). The Court of Appeal held that Mr Justice Field had erred in holding that clause (3) was subject to clause (2) and therefore only provided cover if a defect in the sub-contract works had caused unintentional damage to other work that was free of the defective condition.

The Court of Appeal stated that on its face memorandum 18(3) provided additional cover in respect of access damage necessarily caused to the works to enable a defect to be made good. The clause was

not expressly linked either to clause (1) or clause (2) and its language was not couched in terms of a derogation from the exclusions contained in those clauses. Contrary to the view of the judge at first instance, the Court of Appeal considered it was intended to stand as a separate clause in its own right. External cladding and internal plasterboard ceilings had had to be removed in order to enable the sealing of the windows to be replaced. That constituted damage to the works other than those affected by the defect, but it was deliberate damage carried out for the purpose of gaining access to the sealing membranes. The cost of making good the defects themselves and the access damage was not covered under memorandum 18(1) because the defects were not themselves damage and did not cause damage to other parts of the works. Nor, for the same reason, was it covered by clause 18(2). However, because it was necessary to carry out remedial work to preserve the physical integrity of the building, the insured (including Seele as a sub-contractor), were entitled to be indemnified under clause (3) in respect of the cost of making good the necessary access damage.

Comment

The hearing before the Court of Appeal was primarily concerned with the construction of memorandum 18. However, the Court of Appeal confirmed that in its opinion, insured property (external cladding and plasterboard ceilings) had been damaged, but not by the direct action of a defect. It was the windows themselves which were defective, and intentional damage was caused to the cladding and plasterboard ceilings in order to repair the defective windows. As memorandum 18(3) was a free-standing agreement, this provided cover for the intentional damage caused to access the defective windows.

This case is a further reminder that an inherent defect is not 'damage'. At first instance the Judge considered Pilkington v CGU [2004] where it was held that cracked glass panels in the Waterloo Eurostar terminal did not mean that the roof itself had been damaged, and the cost of taking steps to prevent the panels falling was therefore not covered. This issue was not before the Court of Appeal.

In Seele the first instance Judge also referred to the fundamental purpose of a contractor's all risks policy being the provision of cover against fortuitous damage to the contract works. In the Court of Appeal it was not in dispute that the cover provided by the policy was in general against accidental damage to the works, but Richards LJ stated that there was no reason in principle why the policy should not also include specific separate cover against intentional damage occurring in circumstances that do not involve accidental damage on the proper construction of the policy. Richards LJ considered that to read clause 18(3) as a free-standing indemnity in respect of access damage, even where there has been no accidental damage to the works, did not seem to him to produce a result so obviously contrary to the commercial purpose of the contract, and that it was a relatively small step to cover access damage caused in making good a defect that had not yet given rise to such accidental damage.

The Court of Appeal's decision does not alter the principle that fortuitous damage is nearly always a prerequisite for payment under a policy. It is always open to insurers and contractors to agree sensible provisions such as memorandum 18(3) to cover intentional damage necessarily required to repair a defect which, if left in disrepair, could seriously disrupt the project as a whole.

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