

# RAIL EXPOSURES FOR DEVELOPERS

Risk and Insurance Considerations





## INTRODUCTION

Rail has been a problematic issue both for developers and their contractors for some years in terms of potential liabilities, difficulties in programming works and the high profile of incidents if anything goes wrong.

This paper explores some of the issues primarily from the point of view of developers and the project insurance that may be available to them. It is not intended to cover off the intricacies of insurance for rail operators themselves or for those contractors actually directly appointed by rail infrastructure owners, where different issues can arise.

Many development opportunities arise adjacent to or over existing rail lines. In London, notable examples have included the Shard next to London Bridge, the extensive development works being undertaken around Kings Cross and many other developments being undertaken around Crossrail.

Clearly if there had been a major issue such as a collapse or fire on any of these (or indeed similar) projects, the potential impact could have been huge, with potential liabilities and exposures for the developer possibly falling under the following headings:

- Damage to the development itself together with delay to their own income generation
- Injury or death to passengers and other users of the station or rail property
- Damage to rail infrastructure
- Damage to property of station concessions
- Consequential loss of train operators, Network Rail and station concessions arising from damage.

Insurance for damage to the developer's own property (i.e. the development itself) and the consequential losses directly arising from such damage can generally be purchased straightforwardly, and this paper will focus more on potential liability issues arising from damage to rail infrastructure.

If such an incident did occur on site, a developer would normally look to protect itself from potential exposure to third parties (including the Rail Authorities) by purchasing an appropriate level of liability insurance cover.

We discuss below some of the considerations that need to be borne in mind when arranging appropriate insurance.

### RAIL SPECIFIC ISSUES:

Potential issues which we will discuss further are:

- Network Rail Contracts with Train Operators
- Network Rail Asset Protection Agreements (APA)
- Limit of Liability required
- Claims Handling Agreements
- Cover under a Standard Liability Policy
- Contractual Liability
- Fines and Penalties Exclusions
- The coverage available for financial losses which are not related to damage (which we will define for remainder of this paper as pure financial loss) and arise from contractual obligations.

# NETWORK RAIL CONTRACTS WITH TRAIN OPERATORS

Network Rail agrees with Train Operating Companies (TOCs) and Freight Operating Companies (FOCs) track access arrangements whereby if the track is not available they will refund these parties under a set formula depending on the track lengths which are unavailable, the time of day and day of the week involved, and will normally also take into account performance over previous periods.

These costs are set out under the Network Code, and in simple terms we understand that these can be summarised as follows:

- Planned closures are subject to schedule 4 charges
- Unplanned closures are subject to schedule 8 charges
- Network change costs arise if works necessitate a change in layout etc. to the Network itself.

So if damage occurs to Network Rail Infrastructure, they will normally attempt to incorporate such contractual costs within any claim.

In recent legal cases involving motor accidents, the courts have clarified that Network Rail contractual costs set out in the formula in each element of the Network Code under the current regime are a fair representation of their losses. This has clarified an area that has been under debate with insurers for some years.

## Conarken Group Limited v Network Rail 2011

The Court of Appeal agreed that Network Rail were entitled to claim for contractual payments they make to train operators which are caused by motor accidents.

The payments were deemed to be reasonably foreseeable and in relation to any future loss of income estimates included within the charges were believed to be a reasonable pre-estimate of loss.

## ASSET PROTECTION AGREEMENTS

For works which are within the “zone of influence” of Network Rail infrastructure, developers generally need to agree a contract under which they indemnify Network Rail for a wide range of issues including injury, damage to infrastructure and disruption to the railway; which can be caused by damage or indeed by other issues which are not damage-related.

Network Rail utilise these agreements to protect themselves comprehensively against the costs of damage to their infrastructure, disruption to the running of the railway and the consequential costs they incur in relation to their agreements with TOCs and FOCs.

The indemnity under an APA includes Network Rail’s liability to pay track access charges to the TOCs and FOCs whether disruption involves damage to Network Rail infrastructure or arises from a non-damage issue. This exposure could relate to an incident on site which adversely affects the safety of the operation of the railway, for example a damaged tower crane overhanging the line or a fire on site which leaves an unsafe building adjacent to the railway.

There is normally also a requirement for developers to purchase a minimum level of liability cover, and for large or complex schemes this limit will normally be up to a limit of £155 million (which is the same limit set for rail operators or authorised rail contractors by the Office of Rail Regulation). Network Rail do offer a top-up scheme to provide capacity up to this required limit over a minimum amount (normally set as £25 million), which can be a value for money

alternative, especially for smaller value contracts. However, the scope of this cover is quite limited and certainly does not fully cover off the contractual indemnities required under a typical APA.

### LIMIT OF LIABILITY

For many years the standard insurance requirement where significant works are being undertaken near rail has been for a limit of indemnity for third party liability cover of £155 million to be purchased. A few years ago, the limit itself was consulted upon as there was talk of reducing this to a lower figure of £100 million.

Whether it is a sufficient figure has been debated. To put this limit into context, it is unofficially estimated that the Ladbroke Grove incident in 1999 may have had a total liability payout of around £80 million and Hatfield in 2000 around £50 million.

If the Ladbroke Grove incident were to be revalued to the current day with awards as they are now, this might possibly exceed the standard regulatory requirement, but the outcome from the consultation was that operators and industry participants were generally happy to continue with £155 million as a minimum limit. Clearly, as time moves on and inflation occurs in the general economy and for liability awards themselves, this limit may be deemed to be too low for many developer clients. Higher limits are currently readily available, if required.

It should be noted that the £155 million insurance limit is not a cap on liability but merely a minimum insurance requirement.

### CLAIMS AND HANDLING ALLOCATION

Another aspect that developers and their contractors may need to understand in this sector is that legal liability claims for parties actually working on the rail network are handled under specific arrangements set out in a wider rail industry “Claims Allocation and Handling Agreement” (CAHA) which is a mandatory protocol overseen by the Railway Industry Disputes Resolution Committee (RIDR).

The principal aim of this protocol is to ensure that members of the public suffering bereavement, injury or loss as a result of a railway incident can make a single claim against any potentially liable railway party, without the need to become embroiled in the contractual and often complex legal relations that exist between other potential parties to a particular claim. Liability for claims up to a £7,500 “threshold” are pre-allocated to a specific party as set out in CAHA. An example includes the scenario whereby liability for personal injury to trespassers occurring on a station including the track between station platforms is borne by the CAHA Party in legal occupation of that part of the station. A further example stipulates that employer’s liability claims up to the threshold are paid solely by the employer, without recourse against any other potentially liable parties. These aspects can prejudice insurer’s position if not previously disclosed and suitable endorsements included, to minimise the potential for coverage issues.

CAHA does not apply to all rail industry parties (for example contractors, suppliers or developers). However they can sometimes be bound into CAHA under contract or, if this has not been done, invited to abide by the agreement. The rules of engagement under CAHA can be complex and there can be unforeseen financial implications that come into play as a claim unfolds – for example on higher value losses, if a party is allocated as lead party, they can be made to front interim and final payments of damages and claimant’s legal costs without recourse to other potentially liable parties, with recovery delayed until final resolution of the liability position which may be decided by arbitration some significant time after the originating incident. Specialist claims or legal advice may well be required when dealing with claims under CAHA.





## COVER UNDER A STANDARD THIRD PARTY LIABILITY POLICY?

Given the issues addressed previously, we detail in the remainder of the paper how a third party liability policy may respond to rail related issues, some of the pitfalls that need to be looked at and a possible solution to the thorny problem of pure financial loss.

### OPERATIVE CLAUSE

Operative clauses vary by sector and also with insurers and brokers. We set out below a version which we believe to be relatively standard.

*“The insurers will indemnify the insured against all sums for which the Insured shall become legally liable to pay in respect of or consequent upon:*

- (a) injury suffered by any person*
- (b) physical loss of or damage to material property*
- (c) obstruction, interference, loss of amenities, nuisance, trespass, stoppage of traffic, infringement of light, easement or quasi-easement, denial of access or any like cause*

*occurring during the overall period of insurance in connection with the project anywhere within the territorial limits except as hereinafter excluded.”*

This paper will not analyse this in detail, but essentially this covers off liability for **injury, death or damage to third party property**. The policy will also cover liability for consequential losses directly consequent upon such damage or injury; for example revenue losses caused by damage to third party infrastructure.

The term “Legal Liability” is normally held to incorporate liability accepted by virtue of a contract, although often this is explicitly added to the operative clause of a policy or as a separate memorandum.

The standard cover does not cover *pure financial loss* (i.e. liability for claims incurred in the absence of injury or damage) although there is also a third limb c) covering nuisance and the like, which could potentially incorporate some non-damage

related issues).

It should be noted that the *Tesco v Constable* decision (also mentioned later) argued that under a *public liability* (as distinct from a *Third Party Liability*) policy (which had a similar operative clause to the above) that contractual liability was included but only to the extent that such liability would be incurred at common law. In other words the ordinary public liability policy would recognise contractual acceptance of another party’s tortious liability but no more. However, some insurers are still tempted to attach more importance to the *Tesco v Constable* decision than it merits and therefore careful drafting is needed to ensure clarity of cover.

### CONTRACTUAL LIABILITY

Third Party Liability policies can specifically incorporate cover for contractual liability and this is particularly relevant in the construction industry.

This can be done by ensuring that the policy is classified as a Third Party Liability policy (not public liability), by modifying the operative clause or by adding a specific memorandum. A modified operative clause is shown below:

*“The Insurers will indemnify the Insured against all sums for which the Insured shall become legally liable to pay (whether contractually or otherwise) in respect of or consequent upon:...”*

The additional words explicitly extend the policy to cover liability under contract, though the claimant’s loss still has to arise from injury, damage or nuisance and the like as contained in the standard operative clause.

## FINES AND PENALTIES

Some insurers may attempt to argue that Network Rail costs are liquidated damages because these amounts are pre-determined in their Track Access Agreements and seek to exclude any such payment by virtue of a “fines and penalties” exclusion. As outlined above in the Conarken v Network Rail case, the courts have clarified that Network Rail costs are in fact a fair representation of their losses and should not be deemed to be penalty amounts; so it will be more difficult in the future for insurers to maintain this argument.

In any event careful drafting of the fines and penalties exclusion can avoid the issue for project specific insurances where full disclosure of relevant contract has been made to insurers.

## FINANCIAL LOSS

What is clear is that, in the absence of some special relationship between the parties, the courts are reluctant to attribute liability for pure financial loss in common law where there is no link with damage to a third party property. Students of law can study the cases of *Anns v Merton London Borough Council* and *Junior Books v Veitchi*, where the courts were allowing financial loss claims in the absence of injury or physical damage. These cases were swiftly overruled or reversed.

There is a gap in cover available for pure/contractual financial loss, which does not arise from damage to third party infrastructure.

One of the more notable cases where this became an issue was the *Tesco Stores Ltd v D A Constable* (2007), which involved a collapse of a tunnel which damaged Network Rail infrastructure. There was an Asset Protection Agreement in place, but one of the (many) points at issue from an insurance point of view was the claim against Tesco coming directly from a train operator, Chiltern Railways. As part of the commercial deal to build the tunnel, Tesco agreed a separate Deed with Chiltern to the effect that they would indemnify them for any losses arising out of the works. When the loss occurred, Chiltern

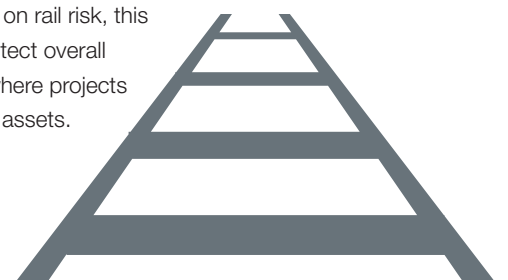
Railways claimed directly against Tesco under the Deed, although none of their property (i.e. their rolling stock) had in fact been damaged. Tesco were liable under the Deed, but their claim against insurers failed. Such direct agreements for contractors and developers with third parties should be avoided.

Even if the standard APA position is maintained and there are no complications of third party agreements as happened in the Tesco case, there remains a gap in cover for disruption to the network which is not due to damage to the Network Rail Infrastructure itself. Clearly much of this potential non-damage exposure can be managed by experienced contractors, but there remains potential for unplanned overruns in an engineering works possession or a health and safety issue on site which means it is unsafe for a rail line to run.

Examples of this could be a fire on site (not affecting Network Rail infrastructure directly) resulting in an unsafe building adjacent to or over rail, a storm causing a tower crane structural damage or cracks in slabs over rail tunnels. These types of claim have happened, and in the worst case, the potential liability could run into many millions of pounds per day.

## INSURANCE SOLUTIONS:

JLT Specialty Limited (JLT) have successfully negotiated cover for contractual financial loss insurance, which responds to disruptions and delays to Network Rail and TfL operations which do not arise from damage to the rail asset. Cover is set up primarily to protect the developer's balance sheet in the event of a protracted incident occurring which cannot be remedied in a reasonable time period. As contractors are becoming more wary about taking on rail risk, this option may have more merit to protect overall investment return for developers where projects involve extensive interface with rail assets.





## CONCLUSION

Developers and contractors are rightly wary of the rail interface on construction projects, as there are potentially significant liabilities to which they are exposed. Care must be taken when signing contracts with rail authorities and particularly with third parties, and legal and insurance advice should be sought wherever possible.

By utilising a well-drafted policy wording and purchasing the right limit of cover together with ensuring full material disclosure, developers can protect themselves adequately against the major risks of damaging rail assets and the consequential losses which arise directly from such damage, as well as potentially options available via JLT to cover pure financial losses arising from non-damage disruption.



### ABOUT THE AUTHOR

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Andrew commenced his career with Sedgwick in 1987, moving to Aon in 1997 and to JLT in 2003. He has varied experience, dealing with major projects worldwide and major UK contractors. For the last few years, Andrew has specialised in major projects and in particular those involving private finance and now heads up our PPP and UK Projects team. Andrew has also led a Research Study Group for the Insurance Institute of London in respect to Insuring Privately Financed Projects. Many of the projects placed by JLT Specialty have involved extensive interface with major infrastructure owners, such as Network Rail and issues raised in the paper are being dealt with on a daily basis by the JLT team.

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Our success comes from focusing on sectors where we know we can make the greatest difference. On using insight, intelligence and imagination to provide expert advice and robust – often unique – solutions. And on building partner teams to work side-by-side with you, our network and the market to deliver responses which are carefully considered from all angles.

And because of this, our clients trust us.

They have total confidence that the vital elements of their operations are covered, enabling their businesses to be even more ambitious and surpass expectations.

We know how we work makes us different. It's quite a claim but we're driven to deliver on it every single day.

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