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UNDERSTANDING THE INDEMNITY & INSURANCE REGIME

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INTRODUCTION

1 Many contracts have indemnity or insurance clauses. These provisions are found in contracts where the subject matter is an activity or project that may expose a party to risks of physical or financial loss, usually from an accident or negligence. Contracts that contain these provisions include design, construction, labour hire, and consultancy services. They are also found in commercial leases.

2 Indemnity and insurance provisions define who will bear the ultimate burden of loss during the commercial relationship. An indemnity clause imposes the burden on one party. An insurance clause requires a party to obtain insurance so that the burden is borne by an insurer.

3 The most obvious "damage or destruction" relevant to a lessor is loss of the leased premises and their contents. Often this may be from fire, but losses to lessors or lessees may also result from flood as exemplified by problems caused

to the Brisbane CBD by the Queensland floods of early 2011. Numerous other risks may be realised during a tenancy, resulting in other losses and liabilities.

4 The lessor and lessee are free to agree the structure of a regime for risk allocation. Indemnity and insurance clauses often comprise kitchen sink collections that focus on protecting the lessor but are not necessarily well crafted. The regime should have a coherent and well thought out structure. Clauses should be drafted with proper regard for the risks that might be realised during the term of the lease, risk allocation, and availability of insurance.

LESSEE FOCUSED CLAUSES

5 Commercial leases drafted for lessors commonly tackle issues of risk by imposing obligations on lessees.

6 For example the lessee might be required to:

6.1 Indemnify the lessor against any claim for death or personal injury or loss of or damage to property arising from use of the leased premises;

6.2 Indemnify the lessor against loss of or damage to the leased premises including fixtures and fittings. This obligation may be qualified by the requirement that the loss has been caused by the negligence of the lessee or its employees, agents or contractors;

6.3 Obtain insurance in the names of both lessor and lessee;

6.4 Expend insurance proceeds on making good any damage to or loss of property;

6.5 Reimburse the lessor for the cost of insurance obtained by the lessor that was required to be, but was not, obtained by the lessee;

6.6 Produce on demand by the lessor copies of the insurance policies required to be obtained by the lessee.

7 Other clauses sometimes included in leases are:

7.1 The lessee will have the interests of the lessor noted on the insurance policy;

7.2 The lessee will not do anything that may cause the insurance to be avoided or cancelled or a claim declined or reduced;

7.3 The lessee will insure against damage to plate glass;

7.4 The lessee will insure its own property and against its business losses;

7.5 The lessee will notify the lessor of circumstances that may give rise to a claim;

7.6 The lessee releases the lessor from liability for loss;

7.7 The lessee will not settle or waive any claim under a policy.

8 Clauses that benefit only the lessor might be legally attractive from a lessor's perspective but they might impose burdens that are commercially or practically inappropriate, if not unattainable.

9 Improved drafting of insurance or indemnity clauses might result from improved understanding of risk issues and insurance.

ISSUES

10 There are numerous legal and factual issues that must be understood before intelligent, effective and appropriate insurance and indemnity clauses can be drafted. Important issues are:

10.1 Types of risks, and categories of losses or liabilities that might arise;

10.2 Causes of action that underlie potential liabilities that are to be covered;

10.3 Categories of insurance;

10.4 What will be the ambit and scope of the parties' respective obligations;

10.5 Who will be insured;

10.6 Allied questions:

10.6.1 What are the principles of construction of contracts that are to be applied to determine the meaning of the words used; and

10.6.2 Is there any presumption in favour of lessor or lessee;

10.7 If a loss occurs:

10.7.1 Who will bear the burden of the loss: lessor, lessee or insurer;

10.7.2 By what mechanisms may loss be re-allocated.

11 I will say more about these issues.

TYPES OF RISKS AND LOSSES

12 Losses that might occur during the currency of a lease include damage to property, death or personal injury, and financial loss. These losses may be incurred by the lessor, the lessee or by third parties. The property may be the building structure, glass, plant or equipment. In addition the lessor or lessee may incur liability for loss or injury. There may be statutory penalties.

13 The losses might or might not be caused by the fault of the lessee or someone for whom the lessee was responsible. The lessor or its agents or employees might be wholly or partly at fault. Both lessor and lessee might be at fault or both may be blameless.

14 The reason for the seemingly desperate solution of kitchen sink clauses becomes obvious at this point. There is so much to cover in terms of potential

losses and losers, why not try to cover everything? And do it for the lessor's advantage?

15 Simplified drafting would cover the most obvious and likely risks. The risks (to the lessor) that are most obvious and likely to occur are injury to people and damage to, or destruction of, the premises or property within it.

Accident from dangerous condition of or activity on leased premises

16 A number of liabilities may arise from risks associated with the condition of, or activities on, leased premises. A party that creates a danger on premises may be liable for loss caused by that danger. The lessee may become liable as occupier of premises for injury or death or damage to property. Usually a lessor will not be an occupier because it does not have control of premises: ***Jones v Bartlett*** (2000) 205 CLR 166.

17 Some lease clauses expressly make the lessee the occupier or responsible as occupier! They merely state the obvious. The lessee is the occupier. The lessor is not vicariously liable for the negligence of the lessee.

18 The lessor may be liable for an injury where the lease imposes an obligation of maintenance or repair and it fails to exercise reasonable care to maintain or repair: Section 9 of the *Occupiers' Liability Act 1985*.

19 There may be statutory duties imposed by occupational health and safety laws.

Injury to workers

20 In most instances a lessor will not require protection against liability to pay damages for death or injury to a worker employed or subcontracted to the lessee, because the lessor will not undertake risk creating activities on the premises. If it does so it must ensure that proper protection is in place.

21 The lessee may incur liability for injury to a worker on site. If the injury is to an employee of the lessee or one of its subcontractors there will be liability to pay workers' compensation. Additionally there may be a liability to pay damages if the injury was caused by a party's negligence.

Act, neglect or default

22 Broad expressions that make the conduct of the lessee a foundation for liability to the lessor seem to find their way into leases, without apparent thought for need or consequences. Expressions such as "act, neglect, or default" and the like seem to be the product of habit rather than careful evaluation of the conduct likely to produce loss or injury and the circumstances where the lessee's conduct should make it responsible for that loss or injury. It is not obvious why a lessee should be liable for loss in the absence of proof of negligence.

Damage to property

23 Fire is a cause of damage to the premises. However damage may also be caused by water (flooding), electrical failure, collision or impact. Broken glass may be a common loss. Apart from the premises there may be plant or equipment of the lessor or others that could be damaged or destroyed.

List of some risks and losses that may need to be covered

24 Risks and potential losses against which lessors may require protection include:

24.1 Liability for death or personal injury to entrants on the premises (including lessor, lessee and their employees, agents or invitees);

24.2 Liability for damage to the property of third parties;

24.3 Loss of or destruction of the premises or the lessor's or lessee's other property;

24.4 Loss of income.

LEGAL GROUNDS FOR ALLOCATING BURDEN OF LOSS

25 Losses might be suffered by lessor, lessee or a third party. There is a number of rules that determine whether the lessor or the lessee will be liable for the loss.

26 The law of negligence is the main source of liability to pay damages for property damage, financial loss, injury, or death. Liability can also arise as a remedy for misleading or deceptive conduct under the *Competition and Consumer Act 2010* (Cth) or the *Fair Trading Act 2010* (WA). A cause of action might also arise for breach of statutory duty or from the law of equity.

27 These causes of action may underlie liabilities of lessor and lessee to each other, as well as the liabilities of either of them to third parties. The allocation of ultimate responsibility as between lessor and lessee can be largely re-shaped by the terms of the lease.

Allocation of liabilities to third parties

28 In the absence of indemnity or insurance clauses in the lease the rules that determine whether the lessor or the lessee with bear the ultimate burden of liability to a third party differ according to whether the loss is death or injury or is property damage or financial loss.

Negligence and personal injury

29 In most cases of liability for death or injury the issue will be determined according to whether one or both of the parties was negligent. A negligent party is called a tortfeasor. Where each of a number of tortfeasors has caused different damage it will be responsible for the damage it has caused.

30 Multiple tortfeasors whose negligent conduct has caused the same damage fall into one of two categories: concurrent or joint. Concurrent tortfeasors are those whose acts are independent and unrelated but are connected by their

contribution to the damage that has happened. The principal and the contractor whose separate acts of negligence contributed to a worker's injury are concurrent tortfeasors.

31 Parties are joint tortfeasors where the negligent conduct is by one person on behalf of or in concert with another. An employer, for example, is responsible for the negligent conduct of the employee. If the employee negligently causes loss both the employer and the employee are jointly responsible for that loss.

32 Lessor and lessee are not likely to be joint tortfeasors. If both have a liability to a third party this will more likely be the result of separate acts in breach of a duty owed to someone on the leased premises. For example, the lessor might have created a dangerous condition (such as slippery or unlit steps) and the lessee might have failed to take steps to warn about or remove the danger.

33 Allocation of loss among a number of tortfeasors is governed by statute. The rules that govern how much one wrongdoer must pay and how liability is split between wrongdoers who cause death or personal injury are different from the rules that apply where the loss is property damage or purely financial.

34 In personal injury cases usually only one total amount of damages can be awarded against several tortfeasors liable for the same damage. As against each tortfeasor the plaintiff is entitled to recover his damages in full subject to any reduction for contributory negligence, which is an amount common to all tortfeasors. This has been called 'solidary' liability in contradistinction with 'proportionate' liability.

35 Each tortfeasor must share in the loss by payment of a just contribution to any tortfeasor who has paid more than its just share. The amount of contribution that is recoverable is such as may be found by the court to be just and equitable. The

court has power to exempt any person from liability to make contribution or to direct that contribution to be recovered from any person shall amount to a complete indemnity. The contribution laws provide that that no person is entitled to recover contribution from any person entitled to be indemnified in respect of the liability for which contribution is sought.

Proportionate liability for property damage and economic loss

36 Since 1 December 2004 liability of defendants to a third party in tort for pure economic loss or property damage caused by failure to take reasonable care has been 'proportionate'. The extent of liability of a tortfeasor to a plaintiff may be less than the full amount of the damages if another tortfeasor contributed to the loss. Hence proportionate liability is a defence. Previously each tortfeasor was liable for the full amount of the damages with a right to claim contribution from other tortfeasors.

37 Rules of proportionate liability extend beyond tort claims to claims for economic loss or property damage under other causes of action (including contract or statute) that arise from failure to take reasonable care or where the loss was caused by misleading conduct.

38 Proportionate liability schemes have been introduced in all States and Territories and under some Commonwealth legislation. Proportionate liability extends to claims for losses caused by misleading conduct. Changes to Commonwealth laws took effect from 26 July 2004. Proportionate liability rules are not the same for every Australian jurisdiction.

39 Proportionate liability applies only to "apportionable claims" and for the benefit of a "concurrent wrongdoer". The benefit is that in proceedings involving an "apportionable claim" the liability of a defendant who is a "concurrent wrongdoer"

is limited to an amount reflecting that proportion of the damage or loss claimed that the court considers just having regard to the extent of the defendant's responsibility for the damage or loss.

MODIFYING THE BURDENS OF RISK AND LOSS

40 Indemnity and insurance provisions may shift or re-allocate the burdens of risk of loss in many different ways. The agreed provisions, rather than statute or general law, will then determine whether the ultimate burden of loss or liability is borne by the lessor or by the lessee. One party might be required to carry the full burden of liability for a particular risk irrespective of the quality of conduct of the other party.

41 Indemnity and insurance clauses that are commonly found in commercial leases for the lessor's benefit have the aim of re-distributing the burden of loss or liability by imposing the ultimate burden on the lessee or its insurers. They alter the outcomes that would prevail in the absence of those clauses.

42 An indemnity clause might impose on the lessee the full burden of liability for loss or injury, irrespective of whether the lessee was negligent. This might be uninsurable.

43 A related kind of clause is one that exempts a party from a particular liability. This is the "exclusion clause". The lessee might agree to exempt, or "release", the lessor from liability that would otherwise arise.

44 Where a lessor would, but for the terms of the lease, incur liability for conduct that is misleading or likely to mislead an indemnity an exclusion or release clause may not apply according to its terms to defeat a claim arising under

Competition and Consumer, or Fair Trading, laws. It is a matter to be taken into account in determining whether conduct overall was misleading.

45 Alternatively, an indemnity clause might be worded so that it imposes the burden only where the lessee is negligent. If the indemnity provision requires the parties to share the burden according to their respective responsibilities for the loss or injury it probably does not alter the result that would be reached without the clause.

46 Proportionate liability must be taken into account if a loss is caused by more than one party other than lessor or lessee. In Western Australia contracting out is permitted for claims in negligence or where a claim is made for misleading conduct relying on a State law. It is unclear whether contracting out is permitted where a claim is made under the *Competition and Consumer Act 2010* (Cth).

CONSTRUCTION OF INDEMNITY CLAUSES

47 An indemnity might be drafted so that its extent is limited by reference to the fact of and degree of negligence of the party for whose benefit the clause has been drafted. The language used in an indemnity clause might not clearly reveal the significance of negligent conduct by the party entitled to the indemnity. A common issue in the decided cases is whether an indemnity clause covers a loss or liability that results from negligence of one of the parties.

48 English cases suggest that there is a presumption against an indemnity clause applying where the party for whose benefit it was drafted was negligent: ***Canada Steamship Lines Ltd v R*** [1952] AC 192. There does not appear to be such a presumption under Australian law. The significance or otherwise of negligence by one or other party must be ascertained from the meaning of the words used:

Darlington Futures Ltd v Delco Australia Pty Ltd (1986) 161 CLR 500. To the extent that an indemnity clause is ambiguous, that ambiguity is to be construed in favour of the indemnifier: see ***Andar Transport Pty Ltd v Brambles Ltd*** (2004) 317 CLR 424, 433, 437.

49 Careful drafting should put this issue beyond doubt.

50 It has been suggested that where a contract contains both an indemnity clause and an insurance clause, in the absence of express words, the obligation under the insurance clause does not require insurance against loss occasioned by the negligence of the party that has the benefit of the indemnity: eg. ***Steele v Twin Rigging Pty Ltd*** (1992) 114 FLR 92; ***Erect-Safe Scaffolding (Australia) Pty Ltd v Sutton*** [2008] NSWCA 114 [165]-[167]. In my view however the extent of the insurance required will be determined by the language used in the insurance clause having regard to the principles of construction set out in ***Darlington Futures*** and ***Andar Transport***: cf ***Westina Corporation Pty Ltd v BGC Contracting Pty Ltd and Keys*** [2009] WASCA 213.

CATEGORIES OF INSURANCE

51 There are two principal categories of insurance. The first category is liability insurance. Liability insurance indemnifies against the insured's liability to pay money to someone else when a loss occurs. Where a loss occurs without fault liability insurance will not be applicable. The second broad category of insurance indemnifies for the occurrence of loss itself.

Liability insurance

52 Liability insurance is associated with loss allegedly caused by someone's fault. Public liability, workers' compensation liability, professional liability, and motor

vehicle (third party) liability policies are examples. Public liability insurance covers liability from breach of duty as occupier as part of broader cover for liability for negligence.

53 If a person is injured on the leased premises and that person is an employee of the lessee, cover for the lessee's liability should be provided by a workers' compensation policy. From 1 October 2011 an employer has been required by the *Workers' Compensation and Injury Management Act 1981* to insure for liability to pay damages, in addition to the long standing statutory obligation to insure against liability to pay workers' compensation.

54 If the injured person is not an employee of the lessor or the lessee then cover for any liability the lessor may have might be provided by a public liability policy.

55 It is theoretically possible for cover under a lessee's workers' compensation policy to be extended to the liability of the lessor to an employee of the lessee or for cover to be provided by a public liability policy. Public liability policies however typically exclude claims by workers or employees. If a lessor requires public liability policy cover against claims by the lessee's workers the worker/employee exclusion in the policy must be scrutinised carefully to ensure that it does not create an unintended gap in cover.

56 Many cases in the courts against insurers have been concerned with disputes over whether a claim is excluded by an employee or workers' compensation exclusion in a public liability policy. Policy wordings for these exclusions vary greatly. They must be checked carefully. Too often they exclude liabilities that are not covered by other policies. Without careful checking of the wording, and cover provided by other policies, the result can be that the party is left without

insurance cover for its liability to pay compensation or damages to another party's worker.

Property insurance

57 The second broad form of insurance attaches to the occurrence of a loss rather than to a liability. If the insured suffers injury, property damage, or financial loss the insurer agrees to pay money to the insured. For example, an Industrial Special Risks policy indemnifies against damage to the business property. The insurer's obligation to pay arises from the occurrence of the loss and not from a liability imposed on the insured to pay money to a third party.

58 Property insurance *prima facie* covers only loss representing the value of the property. Financial or consequential losses are not recoverable unless they are expressly insured: ***Maurice v Goldsborough Mort & Co Ltd*** [1939] AC 452.

Business loss insurance

59 If cover is required for lost income then it may be provided by business interruption insurance.

List of insurance that may be required

60 The types of insurance that may be most relevant to lessors, therefore, include:

60.1 Public liability;

60.2 Workers' compensation;

60.3 Property cover (including glass);

60.4 Business loss.

WHO WILL BE INSURED OR IDENTIFIED IN THE CLAUSES

61 The lessor must determine who will be entitled to the benefit of the insurance cover. The lessor may require, for example, that the lessee include the lessor as

an insured on the lessee's policies. It could impose a more onerous obligation that extends the benefit of cover to the lessor's employees, agents or contractors.

62 The obligations of indemnity or insurance might extend further to losses or liabilities caused by the lessee's employees, agents or contractors. The more onerous the obligation the greater the risk that cover will not be obtained.

63 A lease may require that the insurance "note the interests of the lessor". This term is vague and unhelpful. It is preferable for the lease to require that the insurance contract names the lessor as an insured. Section 48 of the *Insurance Contracts Act 1984* (Cth) enables a lessor to sue on a contract of insurance if the lessor, although not a party to the contract, is specified or referred to as a person to whom the benefit of cover extends. To "note the interests of the lessor" does not seem to me to go far enough to protect the lessor.

64 I am not sure that the expression "note the interests of the lessor" has any practical value, except perhaps in possibly imposing a duty of care on the insurer not to cancel cover without notice to the lessor.

65 In the absence of a term limiting cover to the lessor's interest alone, section 49 of the *Insurance Contracts Act* would confer upon a lessee a right to recover under the lessor's property insurance even though the lessee is not named as an insured under the insurance contract. The lessor would have the same right under the lessee's insurance if it covered the leased premises for full value and not merely the lessee's interest.

66 Insurance of the interests of the lessor and the lessee is called composite, as opposed to joint, insurance. This is so even though clauses often require insurance to be taken out in the "joint names" of the lessor and lessee. Joint

insurance is insurance of the same interest. Insurance of the interests of lessor and lessee is not "joint insurance". In my view better drafting would not use the expression "joint names", but would require that the lessor be named as an insured and its interests insured under the policy.

67 Generally speaking under a contract of composite insurance a breach of the contract by one insured should not affect the right of the other to recover. The expression "for their respective rights and interests" adds nothing.

68 Composite insurance policies cover more than one insured and commonly contain a clause called a "cross liabilities" clause. This type of clause provides that for each insured the policy is to be read as if that insured was the only insured. For example if the policy excludes liability to the "insured's employees" it will be read as applying to a claim by an employee of one insured against that insured but not to a claim brought against another insured.

List of potential insureds or persons whose conduct may be required to be covered

69 Potential insureds or persons whose conduct may give rise to losses or liabilities include:

69.1 The lessor and the lessee;

69.2 Employees;

69.3 Agents;

69.4 Contractors;

69.5 Other entrants.

IMPACT OF INSURANCE LAW

70 The practical operation of indemnity and insurance clauses may however be affected or modified by insurance law principles or the terms of insurance contracts.

Cover for contractual liability

71 A common exclusion from a liability policy is for liability assumed by contract unless the liability would arise in the absence of the contract. Hence if a lessee assumes an indemnity obligation and wishes to insure against the risk covered by the indemnity clause then it must ensure that the cover is sufficient to provide for the full extent of the indemnity. Ideally the insurance cover should be against liability to pay damages and the indemnity in the lease should be confined to damage or loss caused by the negligence of the lessee or those for whose negligence the lessee is vicariously liable.

72 A problem will arise where a lessee is required to indemnify the lessor irrespective of the lessee's negligence. Typically a liability insurance policy will not provide cover for that kind of obligation. Accordingly a lessor should not assume that a lessee will be able to obtain insurance against an indemnity obligation, particularly one that extends beyond indemnity where the loss has been caused or liability has arisen by reason of the lessee's negligence.

Subrogation

73 If a loss occurs it is possible that the lessor's insurer might take action, using a right of "subrogation" against the lessee using the lessor's rights and name. Likewise a lessee's insurer may have subrogation rights it can exercise against a lessor.

74 Subrogation comprises a number of “indemnity” rules that operate to ensure that an insured is fully indemnified, but never more than fully indemnified, under a contract of indemnity insurance.

75 The indemnity principle has three requirements:

75.1 Any amount that the insured receives in reduction of its loss must be taken into account in reduction of the amount the insurer is required to pay;

75.2 If the insurer fully indemnifies the insured then any amount that the insured subsequently receives that reduces the amount of the loss must be paid to the insurer;

75.3 If the insurer has fully indemnified the insured the insurer is entitled to sue to recover any sum from any third party that reduces the amount of the loss and may use the name of the insured to do so:

Burnand v Rodocanachi (1882) 7 App Cas 333 at 339; ***Castellain v Preston*** (1883) 11 QBD 380; ***British Traders' Insurance Co. Ltd v Monson*** (1964) 111 CLR 86. See also ***Insurance Commission of Western Australia v Kightly*** [2005] WASCA 154; (2005) 30 WAR 380.

76 Rights of subrogation can be affirmed, modified, “waived” or eliminated by express terms of the contract of insurance. They are as extensive as, but no more extensive than, the insured’s rights. Hence, if the leased premises have been destroyed by the lessee’s negligent conduct, but the lease requires that the lessor recoup its loss from insurance proceeds, the insurer will not be able to use a right of subrogation against the lessee: ***Mark Rowlands v Berni Inns Ltd*** [1986] QB 211. The reason is that in that situation the lessor’s rights were confined to recovering and applying insurance proceeds.

77 Many claims against lessees are brought by the lessor's insurer after it has paid for a loss. The lessor may prefer not to litigate, particularly where it has an ongoing commercial relationship with the lessee. Accordingly it is important that insurance and indemnity clauses are not drafted so broadly that they serve only to benefit the lessor's insurer by giving it a basis for seeking to recover from the lessee the amount of the indemnity the insurer has provided to the lessor.

Breach of contract to obtain insurance

78 A related issue arises where one party contracts to obtain insurance for another. A contractual obligation to obtain insurance effectively equates with an obligation to indemnify. Breach gives rise to a right to claim damages being the amount of the insurance fund that would have been available if the clause had been complied with: see ***Thiess Contractors Pty Ltd v Norcon Pty Ltd*** [2001] WASCA 364; (2001) 11 ANZ Ins Case 61-509.

79 Further, a defendant may set off against a plaintiff's claim for damages for loss caused by negligence the amount of an insurance fund that should have been available if the plaintiff had complied with a contractual obligation to obtain insurance for the benefit of the defendant: ***Hacai Pty Ltd v Rigil Kent Pty Ltd*** (SCt of WA, 19 December 1995, unreported, library number 960450; BC960384).

80 In my experience, usually these principles are raised in subrogated actions brought for the benefit of the insurer. They tend to benefit insurers and they are not necessarily for the benefit of an insured lessor. If the lessor has its own insurance it may not be concerned that the lessee did not also obtain cover. However the insurer, for the insurer's benefit rather than the lessor's benefit, may be able to take advantage of the lessee's breach of its obligation to obtain cover.

81 If a lessee was obliged to but failed to obtain insurance for the lessor's benefit, and a loss occurred, the lessee could be sued for breach of that obligation. If the loss was covered by the lessor's insurance the insurer may be entitled, using the lessor's name, to sue the lessee to recover the amount of the insurance fund that should have been provided under the lessee's insurance. Further, if the negligence of both lessor and lessee caused personal injury to a third party, even though the lessor had its own liability insurance, the insurer may defend a claim for contribution by the lessee against the lessor on the ground that the lessee did not obtain insurance cover for the lessor's benefit. In these instances, absent some benefit to the lessor in terms of future insurance premium costs, only the insurer seems to benefit.

Exclusion under insurance contract for lessor limiting recovery rights

82 Some contracts of insurance may purport to exclude or limit cover where the insured has entered into an agreement that excludes or limits the right of the insured to recover contribution or damages from a person in respect of a loss. The insurer cannot rely on such a provision unless it clearly informed the insured in writing of the effect of the provision before the contract of insurance is entered into: section 68 of the *Insurance Contracts Act 1984* (Cth).

83 It is not a breach of the insured's duty of disclosure not to disclose the existence of a contract that so limits the insured's rights: section 68(2).

Duty of disclosure/misrepresentation to insurer

84 As to the effect of breach of the proposed insured's duty of disclosure or misrepresentation see sections 21 and 28 of the *Insurance Contracts Act 1984.*

85 Where the clauses contemplate that the lessee will take out insurance for the benefit of the lessor, the legal adviser for the lessor should advise the lessor

about its duty of disclosure and the ramifications of failing to disclose material facts to the insurer before the contract of insurance is made. Non-disclosure of matters material to the insurer's underwriting decision, or misrepresentation, may entitle the insurer to avoid or reduce its liability on a later claim.

86 It would be prudent to include in the insurance contract that non-disclosure or misrepresentation by the lessee will not affect the right of the lessor to claim under the contract.

Waiver of subrogation rights clause

87 A special limitation on an insurer's subrogation rights arises where insurance cover has been taken out for the benefit of the lessor and the lessee. The contract of insurance might contain a "waiver of subrogation rights" clause by which the insurer agrees not to exercise a right of subrogation against an insured. If one insured suffers a loss that is caused by the negligence of another insured the insurer must indemnify for the loss and it is precluded from using an insured's name to sue the negligent insured: ***Woodside Petroleum Pty Ltd v HR&EW Pty Ltd*** (1997) 18 WAR 539.

88 In addition the nature of the cover provided might reveal that every insured is entitled to indemnity. In the event of a loss the insurer may not be able to use the name of a blameless insured to sue a negligent insured: ***Co-operative Retail Services Limited v Taylor Young Partnership*** [2002] 1 WLR 1419; ***Bovis Lend Lease Ltd (formerly Bovis Construction Ltd) v Saillard Fuller & Partners*** (2001) 77 Con LR 134; see also Mead *Recent Developments in Contract Works Insurance* (2002) ILJ 209.

Double insurance

89 The lessor and the lessee might each obtain insurance cover for the same loss or liability with the result that for a particular claim more than one insurer may be liable. This situation of "double insurance" occurs where the same insured is insured for the same risk. In the case of lessor or lessee ti is most likely to happen inadvertently. If one insurer pays the claim to its insured it is a defence to a claim by that insured against the second insurer that the claim has been paid. There is no right of subrogation by the first insurer against the second. It has a right in equity to claim contribution from the second insurer: ***Sydney Turf Club v Crowley*** (1972) 126 CLR 420.

PRACTICAL ISSUES

Drafting

90 Before drafting indemnity and insurance clauses the draftsperson should consider the proposed activities at the leased premises and identify and create a checklist of:

90.1 Risks of death, personal injury, property loss or damage and financial loss that may operate during the term of the lease;

90.2 Classes of persons who may suffer loss;

90.3 Potential grounds of legal liability that may give rise to causes of action against the lessor or the lessee in the event of loss;

90.4 Types of contracts of insurance and levels of cover that are available to protect the lessor or lessee against identified risks;

90.5 How the risks of loss are to be allocated by reference to insurance or indemnities, bearing in mind the availability and affordability of insurance, and the ability of the lessee to pay for an uninsured loss;

90.6 Who will be named as insureds;

90.7 Who has responsibility for payment of an excess under an insurance contract;

90.8 What limitations are to be imposed on the insurers' rights of subrogation or rights to deny indemnity;

90.9 What are the consequences if the lessee fails to obtain insurance or causes a claim to be denied or the amount paid reduced, and the loss is not met by the lessor's insurance.

Imposing burdens by reference to insurance

91 A lessor should be capable of obtaining its own insurance for its own potential losses and liabilities. If it imposes indemnity obligations on a lessee then the indemnity clause may serve to benefit only the lessor's insurer. If a loss occurs and is paid out under the lessor's insurance the insurer then has a right to exercise the lessor's recovery rights against third parties including the right of indemnity against the lessee.

92 In most cases the lessor's goal should be to ensure that losses that result from the lessee's negligence are met by the lessee and its insurers. However the lessor may wish to be covered in a case where both lessor and lessee were negligent or where the lessor incurs liability for the lessee's negligence.

93 It may be appropriate to include in an indemnity clause a limit on the amount of indemnity required. This in turn could be matched to the limit of indemnity under insurance cover that is available and affordable for that party.

94 There may be times when insurance seems unavailable or unaffordable. In that circumstance it might be appropriate for the draftsperson to start with the insurance provisions so that they identify and require available and affordable insurance in the relevant areas of risk. The party that is required to take out the insurance could then have imposed on it an indemnity obligation within the ambit of available insurance cover limited to the extent of liability covered by insurance (and subject to the lessee paying the excess).

95 If the indemnity provisions are not drafted by reference to affordable and obtainable insurance there is a risk that, in breach of its contractual obligation, the lessee will not obtain the required insurance. The breach gives rise to a right for the lessor to claim damages being the amount of the insurance fund that would have been available if the contractor had obtained the necessary insurance. Damages will be recoverable by the lessor even though it has obtained its own insurance cover for the loss. Where a lessor recovers its loss from its own insurer the availability of a claim against the lessee may be of commercial interest and benefit only to the insurer.

Use an insurance broker

96 The task of drafting appropriate clauses may require expert assistance from an insurance broker to determine availability and affordability of insurance covering the risks that have been identified as associated with the common venture contemplated by the contract.

Excessive breadth

97 It may not be appropriate for the lessor to seek to extend indemnity to losses or liabilities incurred by employees, agents and contractors of the lessor. By doing

so the range and potential magnitude of the risk may be magnified substantially and make insurance for the lessee more expensive or difficult to obtain.

98 In a different area, contracts between principal and contractor, I have seen excessively broadly worded indemnity clauses imposed by principals on contractors. These clauses may have made insurance harder to obtain or more expensive, if not impossible to obtain:

98.1 The clause extended the indemnity to numerous classes of persons other than the principal;

98.2 The clause appeared to cover every conceivable kind of loss or liability (other than loss resulting from the principal's negligence);

98.3 The indemnity was not confined to losses caused by the contractor or its subcontractors or employees.

99 These problems could also occur with indemnity or insurance clauses in a lease. Indemnity or insurance clauses that impose on the lessee liability irrespective of negligence by the lessee may cause problems for the lessee. The main problem for the lessee will be availability and affordability of insurance.

100 I have attached a draft set of clauses that illustrates the complexity of the issues that must be addressed. I have focussed on insurance and then confined the indemnities to what is recoverable under insurance.

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DRAFT INSURANCE AND INDEMNITY CLAUSES
For Discussion Purposes Only

1 INSURANCE

1.1 In this clause:

Loss or damage includes:

1.1.1 loss of, destruction of, damage to, or loss of use of, real or personal tangible property;

1.1.2 financial or economic loss including loss of money;

1.1.3 death, personal injury or illness;

1.1.4 interest on an award of damages.

Workers' compensation insurance means insurance that is required by law and that insures the insured against its liability to pay workers' compensation or damages for or in respect of the death of or any personal injury or illness of any person who is defined or deemed to be a worker of the insured under the workers' compensation laws.

Public liability insurance means insurance that insures the insured against its liability to pay damages to any person for loss or damage, but does not include workers' compensation insurance, professional liability insurance, marine insurance, or insurance that the insured is required by law to obtain and maintain.

Property damage insurance means insurance that insures the insured against loss or damage to the insured's property (including property that is in the insured's possession or control) from any cause whatsoever.

Professional liability insurance means insurance that insures the insured against its liability for a claim for loss or damage connected with the advice or services of the insured in the conduct of the insured's profession.

Marine insurance means a contract whereby the insurer undertakes to indemnify the insured in manner and to the extent thereby agreed, against marine losses, that is to say, the losses incident to marine adventure or as otherwise defined under the *Marine Insurance Act 1909* (Cth).

Waiver of subrogation clause mean a clause in an insurance contract whereby the insurer agrees to waive its potential rights of subrogation against the lessor or the lessee as the case may be, unless that party is insured under another contract of insurance and will be indemnified for its liability.

Conduct giving rise to liability means the conduct of a party, or a person for whose acts or omissions the party is vicariously liable, that is negligent, in breach of a statutory or any other duty, or otherwise gives rise to liability under any other cause of action whatsoever, but does not include liability

for breach of a clause of the lease unless a corresponding liability for the same loss or damage would arise in the absence of that clause.

1.2 The lessee shall obtain and keep current during the term of the lease and any renewal or extension of the lease the following contracts of insurance:

1.2.1 Workers' compensation insurance.

1.2.2 Public liability insurance with a limit of indemnity for any one claim that is not less than the amount stated in Item * of Schedule *.

1.2.3 Property damage insurance, by one or more contracts of insurance, with a limit of indemnity under each contract in an amount that is not less than the aggregate replacement value of the lessee's property insured under the contract.

1.2.4 If the lessee is a person or company that carries on the business of a profession, professional indemnity insurance as required by law or otherwise with a limit of indemnity for any one claim that is not less than the amount stated in Item * of Schedule *.

1.3 The lessor shall obtain and keep current during the term of the lease and any renewal or extension of the lease the following contracts of insurance:

1.3.1 Workers' compensation insurance.

1.3.2 Public liability insurance with a limit of indemnity for any one claim that is not less than the amount stated in Item * of Schedule *.

1.3.3 Property damage insurance, by one or more contracts of insurance, with a limit of indemnity under each contract in an amount that is not less than the aggregate replacement value of the lessor's property insured under the contract.

1.4 Each contract of public liability insurance or property insurance shall include a waiver of subrogation rights clause for the benefit of the lessee under the lessor's insurance and for the benefit of the lessor under the lessee's insurance.

2 INDEMNITY

2.1 The lessee shall indemnify the lessor against:

2.1.1 loss or damage that is sustained by the lessor.

2.1.2 liability that is incurred by the lessor for loss or damage to a third party.

2.2 The lessor shall indemnify the lessee against:

2.2.1 loss or damage that is sustained by the lessee.

2.2.2 liability that is incurred by the lessee for loss or damage to a third party.

2.3 The indemnity of the lessee to the lessor or the lessor to the lessee:

2.3.1 shall apply only to loss or damage sustained or liability incurred during the term of the lease and any renewal or extension of the lease.

2.3.2 shall apply only to loss or damage or liability that results from the indemnifier's conduct giving rise to liability.

2.3.3 shall not apply to a liability that results from the indemnitee's conduct giving rise to liability for the same loss or damage.

2.3.4 shall be limited to, and the amount of the indemnity shall not exceed, the amount that the indemnifier is entitled to recover and will recover under one or more of the contracts of insurance that the party is required by clause(s) * of this lease to obtain and maintain.