

Construction/Building  
Guarantee Insurance Policies 'v'  
Professional Consultants' Certificates

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When developers are building or converting domestic properties, they generally need to provide some form of assurance to potential purchasers and their lenders that their position is protected in the event that structural problems develop with the property some time after handover.

Many lenders will generally only lend on newly built (or newly converted) properties where one of the following applies:

1. The Contractor and/or Developer can offer a building guarantee scheme such as those offered by NHBC or one of the major property insurance companies
2. A qualified professional acting as the professional consultant (e.g. a member of CIAT, RICS or RIBA) has signed a Council of Mortgage Lenders' ('CML') Professional Consultant's Certificate or similar certificate. For the purposes of this information sheet, these certificates are referred to generically as 'PCC' certificates. However, it is important to distinguish between different types of certificate.

Although lenders will accept either option, there are fundamental differences between the way these two options operate both in terms of legal technicality and in terms of 'what is covered'. It is vital to ensure that the appropriate option is chosen at the outset of the project. It is also extremely important that these differences are understood by:

1. The Developer
2. Purchasers
3. Their Lenders
4. The Lawyers involved at all stages from the initial appointment documents on the construction project, through the purchase/sale of the properties (conveyancing), to the solicitor who pursues the claim in the unfortunate event that a problem arises.

The purpose of this information sheet is to highlight the differences between the two options in order to ensure that they are correctly understood and that, in the event that a claim arises, the Claimant, be they the Purchaser or Lender, does not have incorrect expectations as to his possible recovery.

## Building Guarantee

A Building Guarantee is a form of insurance policy taken out by the Contractor or Developer to protect the purchasers, the lenders and their successors against latent structural defects in the property. The vast majority of new build properties now have the benefit of insurance under warranty schemes.

Both NHBC and policies provided by insurers require that newbuild properties are inspected by approved inspectors during their construction in order to minimise the risk of defects. In order to register for NHBC cover, the developer and/or the Contractor must show suitable financial security and technical competence.

## NHBC

NHBC runs a number of schemes which offer wide-ranging cover for residential properties, self build properties and social housing. The Buildmark scheme offers cover to residential properties and, for homes registered with NHBC from 1 October 2005, this cover is divided into four time periods:

- Cover before the property is completed
- The first two years after the property is completed
- Cover in years 3-10
- Additional cover in years 3-10 where NHBC's subsidiary carried out the building control (not in Scotland).

Aspects that can be covered include:

1. If the property is not completed, or even not started, then the cover will reimburse the purchaser for any money they have paid the Contractor but which they cannot recover from him, up to a maximum of £100,000 or 10% of the original purchase price (whichever is the less).
2. For the first two years after the property is completed, Buildmark covers purchasers against physical damage to the home caused by the Contractor's failure to meet NHBC Standards. This part of the cover usually runs from the date of legal completion of the first sale of the property and it is the Contractor who is responsible for any repairs necessary (hence the need for the Contractor to show financial security in order to register with NHBC).

3. For the next eight years, Buildmark provides cover direct to the purchaser only in relation to structural defects (as opposed to wear and tear) within the property and is, in effect, first party cover. If the Contractor defaults, NHBC arranges for the remedial work to be carried out and seeks to recover from the defaulting Contractor.

## Insurers

Insurers offer a number of different warranties covering residential properties, commercial and mixed-use developments, self build properties, housing associations and social housing landlords. Typically, policies cover damage arising from defects in new properties for ten years. As with NHBC, normally the Contractor/Developer is liable for the first two years (one year for conversions), after which the insurer will deal directly with the homeowner.

## Professional Consultants' Certificate

Not all Contractors are able to or choose to provide NHBC or other insurance backed cover. This is usually a function of the size and sophistication of the contractor. For those who do not have the benefit of building guarantee cover, the PCC may be an acceptable alternative but on a rather different basis.

The PCC is a certificate in a prescribed form, endorsed by professional consultants when designing and/or inspecting the construction or conversion of residential buildings. The most common form of certificate is that approved by the CML, which represents approximately 98% of the UK mortgage market ([www.cml.org.uk](http://www.cml.org.uk)).

The PCC published by CML can be relied upon both by the original purchaser and lender and by any subsequent purchasers and their lenders for a period of six years from the date of the certificate. This may not be the case with other PCCs. Clearly, it is important for the purchaser and his advisors to check the wording of the individual certificate as, if the certificate is not transferable, this could have a profound effect on the saleability of the property.

The CML PCC also confirms to the lender that the professional consultant will keep a certain level of professional indemnity insurance ('PII') in force to cover his liabilities under the

certificate. Again, this is an important element to check in non CML certificates.

The effect of the PCC is to confirm that the professional consultant has visited the property at appropriate periods to check the progress of construction, conformity with drawings approved under building regulations and conformity with drawings/instructions issued under the building contract. A purely visual inspection of the works suffices. It is therefore recognised that, by their very nature, interim inspections will not reveal all defects. In addition, some certificates expressly exclude liability for poor workmanship.

It is important to note the following:

- The PCC is not the same as a structural warranty. In general, the scope of what it covers is, in isolation, considerably narrower than a structural warranty. The main purpose of the PCC is to give an opinion on the work-stage reached insofar as can be ascertained from periodic visual inspection and confirms apparent compliance with Building Regulations and the drawings/instructions properly issued under the Building Contract. This, in turn, allows the lender to release funds based on the information.
- The PCC does not impose a duty on the professional consultant to 'supervise' the Contractor's work. That would imply a near constant presence on site. The professional consultant is simply under a duty to inspect the development at periods appropriate to the individual project.
- The PCC 'does what it says on the tin'. It is, by its very nature a limited certificate. The professional consultant (which, for the purposes of this information sheet includes the practice for whom they work if appropriate) can only be held liable for defects that ought reasonably to have been apparent to him when fulfilling his inspection duties. Therefore, latent defects and those which a visual inspection would not reveal are not covered.
- To issue a CML certificate PII must be in place and maintained by the professional consultant who signs the certificate. This must be checked if a different PCC is used. Any claim arising from issues pursuant to the PCC has to be brought against the professional

consultant as opposed to an insurer. It should be noted, however, that other professionals involved in the project (including the Contractor) may be liable for their part in the project, in which case they should be pursued separately. In practice, it is likely that the PI insurers will deal with the claim. However, the professional consultant (or practice) is not obliged to make a claim on his or the practice PII in the event of a claim. For example where the amount of the claim is likely to be less than the aggregate of the excess on the policy and the premium increase likely if a claim is made; or where the loss of reputation may be more valuable than the monetary amount of paying the claim quickly.

- To succeed in a claim against the professional consultant, it will be necessary to show that the professional consultant has breached a term of the PCC to a level of rigour that would be appropriate to a court of law (or ADR)
- By contrast, the Building Guarantees are no fault, first party policies, i.e. the claimant is entitled to make a direct claim under the policy provided he is in the class of people who can benefit from it.

The PCC may not be appropriate for all developments. In particular, a building warranty would be more suitable in a large scale mixed-use development. However, where building warranty cover is not available or, perhaps due to the limited size of a project, not appropriate, the PCC operates as a viable alternative. The PCC is a useful way to secure funding in the case of a self-build project.

It is vital that all interested parties understand the differences between the two options in order that:

1. the appropriate balance between breadth of cover and cost effectiveness is struck when deciding between the two options;
2. appropriate steps are taken in the event that problems occur and, particularly in the case of the PCC, the Claimant is not given unrealistic expectations as to the likely level of his recovery;
3. the client secures the service he requires at the outset of the project.

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Disclaimer: This note is for general guidance only and legal/professional advice should be sought to cover any particular situation