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

The Professional Consultants' Certificate mentioned in this document was originally issued by the Council of Mortgage Lenders which was taken over by UK Finance in 2017. It was therefore sometimes referred to as the CML Certificate.

Area of Operation: UK

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

Many lenders provide finance on newly built (or newly converted) properties only where one of the following options applies:

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

Although lenders may accept either option (individual terms can be viewed at ukfinance.org.uk), there are fundamental differences between the way the warranties (guarantees) and PCC's operate in terms of legal technicality and '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 the differences between the two are understood by:

1. the client;
2. the developer;
3. purchasers;
4. their lenders, and
5. the lawyers involved. There may be several lawyers: those handling initial appointment documents on the construction project, those involved with the purchase/sale of the properties (conveyancing), and the solicitor who pursues a claim in the event of a problem arising.

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, should a claim arise, the claimant, be they the purchaser or lender, does not have incorrect expectations as to possible recovery.

1. Types of Construction Warranty/Building Guarantee

Building Warranty/Guarantee

A building warranty/guarantee is a form of insurance policy taken out by the client, contractor or developer to protect the purchasers, the lenders, and relevant successors, against latent structural defects in the property. The vast majority of new build properties now have the benefit of insurance under various warranty/guarantee schemes.

LABC New Homes Warranty, 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. As an example of what is covered, a brief overview of LABC New Homes Warranty and NHBC policies are briefly outlined below:

LABC New Homes Warranty

The New Homes Warranty is aimed at new builds and conversions of residential developments (including mixed use developments). The warranty provides the cost of rectifying works, partial or complete rebuilding where a new property has suffered damage.

Working in partnership with CIAT Insurance Services, LABC Warranty offers a range of comprehensive home warranty insurance products to professional consultants involved in the design and development of both new build and conversion projects.

New Homes Warranty — Cover Overview

- **Main Cover Provided**
  - Defects Insurance Period: 2 Years
  - Structural Insurance Period: 8 Years

- **Financial Limits**
  - New Build: £1,000,000
  - Conversions: £500,000

- **Continuous Structure Limit**
  - New Build: £25,000,000
  - Conversions: £5,000,000

- **Excess**
  - Defects Insurance Period: £100
  - Structural Insurance Period: £1,000

- **Additional Cover Includes**
  - Developer Insolvency Cover (subject to approval)
  - Contaminated Land Cover
  - Additional Costs/Fees
  - Alternative Accommodation
  - Removal of Debris

Additional Warranty types include projects involving Self-Build, Social Housing, Mixed Use and Completed Housing.

For more information contact CIAT Insurance Services on 0161 233 4497, ciat-insurance.co.uk/warranty

NHBC

NHBC runs a number of schemes which offer wide-ranging cover for residential properties, self build properties and social housing. To register for NHBC cover, the developer and/or the Contractor must show suitable financial security and technical competence. The Buildmark scheme offers cover to residential properties and, for homes registered with NHBC from 1 April 2017, 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.

Which Building Warranty/Guarantee?
There are a number of products on the market to choose from. Professional consultants who are considering various options would be advised to scrutinise the financial rating of the provider. A rating of no less than "A" or equivalent is recommended to give confidence that it will still be viable for the duration of the term of cover.

2. Professional Consultants' Certificate (PCC)

Not all contractors are able to, or choose to, provide LABC, 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 warranty/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 the consultant when designing and/or inspecting the construction or conversion of residential buildings. The most common form of certificate is that approved by UK Finance, which represents approximately 98% of the UK mortgage market (ukfinance.org.uk).

The PCC published by UK Finance 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 purchasers and their advisers 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 UK Finance PCC also confirms to the lender that professional consultants will keep a certain level of professional indemnity insurance ('PII') in force to cover their liabilities under the certificate. Again, this is an important element to check in non UK Finance Professional Consultants' certificates.

A further 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 warranty/guarantee. In general, the scope of what it covers and how it works differs from a warranty/guarantee. 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) may only be held liable for defects that ought reasonably to have been apparent to them when fulfilling their inspection duties. Therefore, latent defects and those which a visual inspection would not reasonably reveal are not covered.

- To issue a PCC, 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. However, unlike the Building Warranty, the PCC does not give the recipient the right to make a direct claim against the professional consultant's insurers, as they are not covered under the professional consultant's PII. Any claim arising from issues pursuant to the PCC has to be brought aginst the professional consultant in the first instance.

- Warranties/guarantees for buildings are no fault, first party policies, i.e. the claimant is entitled to make a direct claim under the policy provided they are in the class of people who can benefit from it and it falls within the policy's scope. For a claim to succeed against the professional consultant, it will be necessary for the recipient of the PCC to show that the professional consultant has breached a term of the PCC by failing to use the reasonable degree of skill and care appropriate to provision of a PCC and as expected by a court of law (or ADR). consultant has breached a term of the PCC by failing to use the reasonable degree of skill and care appropriate to provision of a PCC and as expected by a court of law (or ADR).

- In view of the limited scope of a claim under a PCC, it should be noted 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.

The PCC may not be appropriate for all developments. In particular, a warranty/guarantee 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, although it should be noted that not all Funders will be prepared to accept a PCC.

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 their recovery;

3. the client secures the service they require at the outset of the project.

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