Exclusions for assumed liability: Why promising "the best" may be bad for your insurance

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Clients naturally want "the best" from their service providers. However, service providers and other suppliers who agree to provide "the best" – or any standard or duty higher than usual – should be aware of the possible implications this may have on their insurance cover.

Exclusions for "assumed liability"

Professional indemnity policies (and some other types of insurance) usually exclude cover for "assumed liability". This typically arises when a supplier enters into a contract or arrangement that:

- Extends the supplier's duties beyond what the law would normally impose; or
- Increases the compensation that the supplier may have to pay for a negligent act or some other breach.

The exclusion means that, if a supplier agrees to take on greater obligations or accept greater potential legal liability than the law would otherwise impose (such as the normal duty to exercise reasonable care and skill), then their insurance may not cover the additional obligations or liabilities.

The rationale for this exclusion is clear: liability insurance is intended to provide cover for breaches of standards imposed by law, where the standard is typically one of "reasonable care and skill" or some other objective and conventional measure. A supplier who promises to deliver to a higher, more demanding standard – one that may turn out to be more difficult or even impossible for the supplier to achieve, does so at their own risk (unless they arrange special cover with their insurer).

Examples of assumed liability

The following are examples of how a supplier might assume liability under a contract that **may**, depending on the specific circumstances, result in cover being declined or limited under an "assumed liability" insurance exclusion:

- Agreeing to perform services to "the highest international standards and practices";
- Agreeing to provide deliverables of "the best quality";
- Providing indemnities or "hold harmless" obligations;
- Accepting liability without proof of fault;
- Extending liability to third-parties.

Other scenarios may arise where the supplier assumes liability above what the law would otherwise require, such as agreeing that the supplier will be liable for any delays, even where the delay is beyond the supplier's control.

It is important to remember that while assumed liability typically arises from contractual commitments, it can also arise from pre-contractual representations or other conduct outside of a contract.

Insurance cover for "ordinary" liability

An assumed liability exclusion normally excludes cover only to the extent that that it goes beyond what the law would have imposed anyway. This means that a supplier may still be partially covered for an event arising where there is some assumed liability.

However, in practice, it can be difficult to distinguish and quantify the "ordinary" liability that would be covered (i.e. liability that would have arisen even if the supplier had not assumed further liability) from any assumed liability that may be excluded.

Recommendations

It is common sense that a supplier should attempt to limit their obligations and liabilities as much as is commercially and legally possible, such as minimising acceptance criteria and having an appropriate limitation of liability clause. However, it can be tempting for a supplier to make generous (perhaps overly generous) representations and commitments to a customer in the hope of closing a deal.

The common exclusion in insurance policies for "assumed liability" does not mean that a supplier can never agree to such provisions. It may be commercially necessary, and appropriate in the right circumstances, for a supplier to agree to be held to a higher standard or greater potential liability than the law would normally impose.

However, before agreeing to such an obligation, suppliers should:

- Understand what additional specific risks and liabilities they will be committing to, and the potential insurance and other implications that may arise;
- Consider whether the heightened obligation is truly necessary and appropriate, or whether a lesser obligation can be negotiated;
- Consider the potential scope of indemnity / "hold harmless" clauses and third-party liabilities, whether they are appropriate in the circumstances, and whether they can be limited or (ideally for the supplier) excluded;
- Expressly define quality requirements, e.g. instead of committing to potentially vague concepts such as "high quality", "highest industry standards", or even "best practices", the contract could define the specific standards or practices that the supplier must achieve. This reduces uncertainty for both parties, and is good practice regardless of insurance implications.

If in doubt, suppliers can seek advice on specific clauses from their insurer, broker or lawyer.

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