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Design Professional Liability and Coverage Issues: The Expanding Role of Design Professionals in Construction Claims

I. Historical Claims Involving Design Professionals

Historically, construction defect claims against Design Professionals have been narrowly tailored and limited to issues involving the design of the project/building and have involved some specific coverage issues and challenges.

Design professionals (e.g. architects and engineers) are usually at the center of construction projects, preparing plans and specifications, reviewing shop drawings, answering questions, and making recommendations throughout the course of a project. They meet most, if not all, of the project's participants. When something goes wrong, the design professional is often caught in the middle.

In typical construction cases, design professionals are in privity with the owner and/or with each other. In design/build situations, design professionals are in privity with the general contractor. Those in privity with a design professional have typically been allowed to recover both in contract or in tort on a theory of a failure to exercise due care in the performance of contract services. However, historically, in most construction defect case, the focus has been on the construction parties and not the design professionals.

Less frequently, claims of Professional Negligence and E&O claims have been asserted against design professionals as well as claims for property damages and personal injuries allegedly arising from and/or caused by the design of a structure.

II. Insurance Coverage Issues

Types of policies and coverage

For design professionals, the difference between a CGL and a Professional Liability (E&O) policy must be understood. Sometimes these coverages are in separate policies or in one policy. A CGL policy often:

- Includes a Professional Liability Exclusion precluding coverage for “bodily injury,” “property damage” and “personal and advertising injury” arising out of rendering or failure to render any professional service or, alternatively, specified professional services; and may include, by endorsement, separate Errors and Omissions Coverage aka Professional Liability Insurance which may or may not be subject to a sublimit.

- Covers liability arising from the mistakes inherent in the practice of the particular profession or business and usually applies not only to “bodily injury” and “property damage” claims, but also to claims including pure economic loss.

While CGL coverage may provide some limited coverage for losses arising out of design errors, CGL coverage is not a substitute for Professional Liability (E&O) coverage. These distinctions can be described as follows:

CGL Coverage: Designed to provide comprehensive insurance coverage, such as premises and operations liability, protective liability, broad form property damage liability, etc., to protect the insured against liability arising out of “bodily injury” and “property damage” to third parties caused by an “occurrence” (“accident”) and “personal and advertising injury” (injury arising out of commission of specified offenses, injury which is rarely involved in a claim against a design professional)

Professional Liability (E&O) Coverage: Designed to provide coverage for liability arising from the mistakes inherent in the practice of that particular profession or business and caused by a negligent act, error, or omission committed by the insured in the course of providing professional services. The intent is to cover only breach of the professional's traditional duty of care (duty to use the degree of care and skill expected of a person in the same profession).

Key differences:

1. CGL coverage is typically occurrence-based whereas Professional Liability coverage is typically claims-made;
2. CGL policies typically have no limit regarding defenses costs payments while Professional Liability policies typically limit total payment, including defense costs, to the limit of liability purchased (i.e. they are eroding aka burning, limits policies);
3. CGL policies usually carry low deductibles, whereas many Professional Liability policies apply high per-claim deductibles;
4. CGL coverage responds to bodily injury and property damage, whereas Professional Liability policies provide coverage against a broader array of damages, including economic damages;
5. As a general rule, CGL insurers allow their insureds to add additional insureds to their policy at little or no additional cost, whereas Professional Liability insurers generally do not.
6. E&O coverage requires negligent act during the policy period to trigger coverage whereas CGL coverage requires “property damage” (or “bodily injury”) caused by an occurrence and occurring during the policy period.
7. E&O coverage does not require an “occurrence” (“accident”).
8. E&O coverage typically requires that the named insured consent to a settlement, and this requirement has implications regarding reporting and ability to settle.

Evaluation of the coverage issues for design professionals requires careful consideration of the **exclusions** on the different policies. First, for the CGL policies, the following exclusions generally apply:

Professional Liability – Liability arising out of rendering or failure to render professional services. Applies to professional negligence. Does not apply to (coverage would still be afforded for liability for) breach of general, nonprofessional duty of due care which would be expected on the job from any conscientious and competent contractor, e.g. breach of duty owed by all involved in a project to report and warn of unsafe conditions; failure to properly supervise construction; administrative error (clerk fails to timely provide plans); garden variety negligence (ex. mistakenly cutting pipe during construction) rather than conduct requiring application of specialized knowledge. Where “professional service” is not defined in the policy, typical interpretation: business activity conducted by the insured that involves specialized knowledge, labor, or skill, and is predominantly mental or intellectual as opposed to physical or manual. Exclusion only applies if the insured was performing professional services with respect to the specific event on which the claim is based, not merely during the performance of professional services in general (ex. Architect on construction site in professional capacity but conduct is limited to warn of dangerous condition he notices).

E&O Exclusions:

Prior Acts – retroactive date

High-Risk Design (ex. unusual or experimental professional services or procedures; surveys, soil testing, subsurface conditions; air conditioning; heating; sewage or hazardous waste treatment; asbestos; pollution)

Contractual Liability (exclude breaches of contract based on other than professional negligence – e.g., failure to provide accurate cost estimates or timely complete plans and specifications, express warranties and guarantees, contractual indemnification of others).

Construction (e.g. liability arising out of “[a]ctual construction activities by the insured; assembly, construction, erection, fabrication, installation or supply of products or materials by the insured”)

Deliberate misconduct (e.g. dishonest, fraudulent, or criminal acts, error, or omissions; intentional torts including libel or slander; infringement of copyrights, trademarks, or patents; industrial piracy, unfair business practices, misappropriation of trade secrets; punitive damages; fines or penalties.)

When a complaint alleges that an injury occurred both because of negligent professional services and negligent services of some other kind, both CGL and professional liability insurers are likely to owe a duty to defend the design professional.

III. Changes in The Coverage Issues with The Changes in The Industry

Traditionally, there have been three standard (ISO) Contractors Professional Liability endorsements available to modify CGL coverage where insured provides at least some architect, engineer or surveyor services. Which ISO endorsement is used makes a difference in the scope of coverage:

A. CG 22 43 – Exclusion - Engineers, Architects, or Surveyors Professional Liability:

This has become known as the “clean sweep” exclusion. The basic standard CGL coverage form excludes, by way of an exception to the policy definition of “insured contract,” any liability under a contract or agreement that indemnifies an architect, engineer, or surveyor, or under which the insured, if such a professional, assumes liability arising from its rendering or failure to render professional services. When the CG 22 43 endorsement is used to modify the coverage form, it excludes from CGL coverage all other professional liability which could otherwise attach. The purpose of this endorsement is to keep the CGL insurer from paying a loss that can be covered under a Professional Liability policy.

B. CG 22 79 – Exclusion – Contractors Professional Liability:

Designed to be added to policies covering construction contractors that also provide professional engineering, architectural, or surveying services to others. The CG 22 79 endorsement excludes liability for professional engineering, architectural, or surveying services (1) that the named insured provides to others in the capacity of an engineer, architect or surveyor; and (2) that the named insured provides, or hires independent professionals to provide, in connection with construction performed by the named insured. However, the endorsement specifically preserves coverage for “services within construction means, methods, techniques, sequences, and procedures employed by you in connection with your operations in your capacity as a construction contractor.” This exception to the exclusion clarifies that services that are part of construction operations will not be excluded by the professional services exclusion.

C. CG 22 80 – Limited Exclusion – Contractors – Professional Liability:

Designed to be added to policies covering construction contractors who may provide professional services to others. The CG 22 80 endorsement is similar to the CG 22 79 endorsement in that both endorsements exclude professional errors or omissions in connection with engineering, architectural, or surveying services that the named insured provides in its capacity as an engineer, architect, or surveyor. However, in contrast to the CG 22 79 endorsement, the CG 22 80 endorsement does not exclude coverage for the liability of a contractor who designs and builds a project for others, whether the design work is performed by the named insured or by a subcontractor.

IV. Hybrid Policies

Carriers are now offering new insurance products that provide coverage for businesses involved in the building industry that previously would not have purchased E&O insurance, but as their roles evolve the scope of the services they provide is expanding to include some design activities, e.g. HVAC vendor that provides HVAC maintenance but also provides consulting services in connection with the design of a HVAC system. Their typical CGL policy would not provide coverage for any claims arising out of the design consulting services they provided. They can purchase a package policy that provides the coverages in a CGL policy as well as pollution and professional liability coverages. These specialty package policies typically include 4-5 coverage parts that will cover property damage, bodily injury, pollution liability and professional liability. The challenge presented by these policies is to determine whether or not professional services were actually provided, and which coverage should apply since several may be triggered. In addition to these package policies, carriers are drafting specific Professional Liability endorsements directed at non-traditional design professionals to cover atypical situations where some design services are provided.

In addition to package policies, carriers are also providing hybrid policies that tailor the coverage specifically to contractors, and other similar businesses, that also provide some design services.

Unlike the package policy, these do not offer CGL coverages but instead provide E&O coverage on a claim made basis. The exclusions and definitions are tailored to the fact that the insured also provides construction services, which would not be covered. The definition of Professional Services is also usually very specific. Often a thorough investigation into the services provided by these insureds is required to make sure that professional services were rendered which would trigger coverage under these hybrid policies. Given that these insureds often provide maintenance services, these activities are specifically excluded under the Policy.

One other coverage that these package and hybrid policies provide that is not typically provided under a CGL policy is pre-claim assistance. We have found that carriers and insureds often take advantage of this additional coverage, whether it's responding to a subpoena or dealing with an ongoing design issue before it ripens into a claim, since pre-claim assistance can decrease costs for all involved if the matter is resolved before it becomes a claim involving multiple parties.

In recent years, however, changes in technology and project delivery mechanisms have impacted design professionals and contractors in several ways that impact their liability and exposure in construction defect cases. The construction industry has lagged behind other industries in adopting technology changes and advocating for new technology uses. However, in the last several years, design professionals and contractors alike have started to embrace technology changes, including the use of Building Information Management ("BIM"), drones, construction management software, and delving into the use of virtual reality and wearable technology.

Of critical importance to design professionals is the impact of these technologies in changing how design of construction projects is performed and who is actually performing the design work. With the use of BIM, all parties to the project may have access to and be involved to some extent with adjusting and adapting the design of the project during the course of construction. If there is a change, for example, to the location of the mechanical, electrical and plumbing, by the mechanical engineer, is the architect somehow responsible for those changes by virtue of the architect being the final approval on the BIM software? Do other parties then step into the design professional role? These questions have been addressed in the course of construction over the last several years, but little has been seen in the actual dispute resolution arena or published decisions on how this impacts the liability for non-professionals and/or for the architect or engineer of record on the project.

The changes in technology also raise legal issues of the standard of care for a design professional. To the extent the project is using BIM, the architect or engineer will be required to have sufficient knowledge and skill in use of the technology. Moreover, the standard of care in the industry is changing such that this is becoming the minimum standard for an architect or engineer to not only be capable of using the technology, but also having sufficient staff and expertise not only in the use of the software but also being able to address the technical issues and difficulties that may arise during the design and construction phase.

The changes in delivery mechanisms for projects have also impacted the liability exposure and coverage needs for parties involved in the construction process. Not only are architects, engineers, landscaping and architects responsible as design professionals, but with changes to design-bid-build programs and P3s (public-private partnerships), contractors and subcontractors are often being held responsible for design elements for the project, thereby essentially putting them into the shoes of a design professional. These changes raise potential liability issues for a contractor delving into serving as an unlicensed design professional. Contractors and subcontractors must ensure that if they are performing work in these arenas that they either have on-staff licensed professionals or are retaining the necessary consultants. Furthermore, contractors must carefully review and evaluate their insurance coverage to ensure that they have sufficient and proper insurance available for any design-related work. Most CGL policies exclude coverage for design professional work, and thus careful assessment of the work to be performed must be evaluated and the scope of work determined early. If changes occur during the course of the project, additional coverage and risk management assessment may be needed. Therefore, it is imperative to be abreast of the changes in coverage available to contractors and design professionals.