

RISK TRANSFER FOR DESIGN-BUILD TEAMS

DESIGN-BUILD WORK IS INCREASING EACH QUARTER. CONSEQUENTLY, WE ARE FIELDING MORE INQUIRIES FROM CLIENTS REGARDING THE STRUCTURING OF - AND RISK TRANSFER OPTIONS FOR - DESIGN-BUILD TEAMS.

For most clients, competing for a design-build project requires the formation of a team that brings together the necessary architectural and engineering design experience and the construction expertise and capability for the project type. In choosing project partners, careful consideration must be given, not just to familiarity with the project type, but also to the depth of the team members' experience with design-build projects, to their financial footing and to the cultural fit between organizations.

The actual legal structuring of the team may be achieved in one of several ways, with one party (usually the contractor) contractually "priming" or leading the design-build team. Many such teams are "informal" and rely solely on some form of teaming agreement, whereas others may be formally structured, as either a joint-venture, a limited liability corporation (LLC), or as a corporation.

Design-build team or joint-venture partners may seek to allocate risk between one another by means of their teaming agreement's indemnification and insurance provisions. In the event of a serious design defect, however, such allocations may not be sufficient to obviate each joint-venture partner's contractual and legal obligations to the project owner.

Therefore, the direct and vicarious liabilities for the performance of design services that can arise in a design-build team or joint venture demand very careful evaluation – and appropriate allocation and transfer of risk.

As the prime in contractor-led design-build, the contractor is legally liable to the project owner for both the design and the construction of the project. Although the contractor may be delegating responsibility for design services to various subconsultants (who



may be providing the contractor with indemnification), as prime, the contractor remains responsible to the owner for the consequences of defects and deficiencies in the design documents.

Design-build teams and joint ventures have only a finite number of ways to try to limit their exposure in the design-build agreement with the owner.

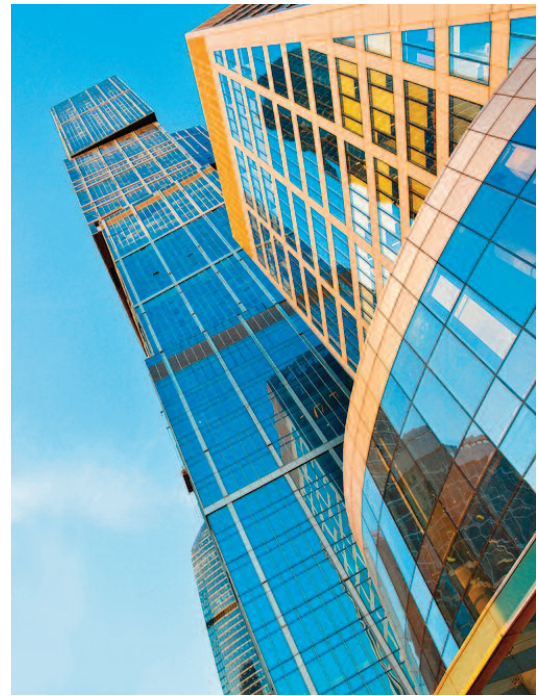
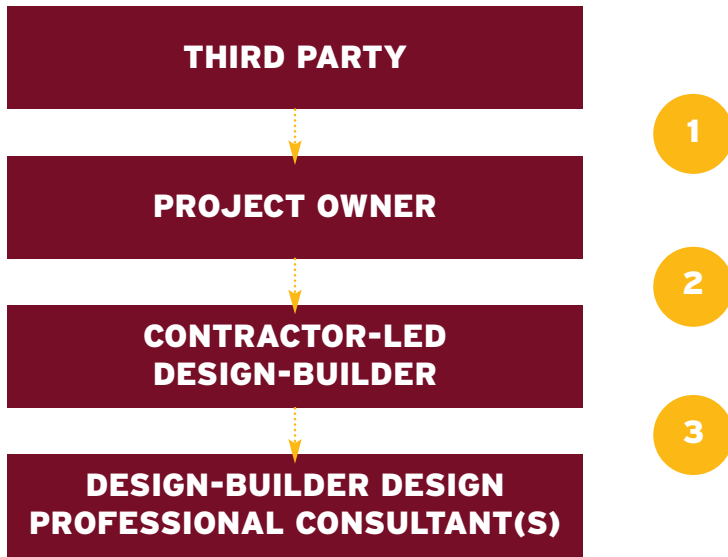
- Making use of a negligence-based standard of care
- Limitations or exclusions for consequential damages
- Limitation of liability
- Rights of reliance (in the event that they are relying on owner-furnished information or design documents)

COVERAGE FOR DESIGN LIABILITY

PROFESSIONAL LIABILITY POLICIES	
Contractor's Professional Liability Policy	<p>Provides coverage for failure to perform professional services, either directly or by entities for whom the insured is "legally liable."</p> <ul style="list-style-type: none"> ■ Note the definition of "professional services" to determine the extent to which professional services within construction means and methods are addressed ■ Note the inclusion of JV coverage (generally limited to insureds' participation in JV only)
A/E Professional Liability Policy	<p>Provides coverage for failure to perform professional services, either directly or by entities for whom the insured is "legally liable."</p> <ul style="list-style-type: none"> ■ Note the definition of "professional services" to determine the extent to which professional services within construction means and methods are excluded ■ Note the inclusion of JV coverage (generally limited to insureds' participation in JV only) ■ Contractor cannot be given additional insured status under the policy
Contractor's Professional Liability Policy (endorsed for a single project)	<p>Provides coverage for failure to perform professional services, either directly by the design-builder or by entities for whom the insured is "legally liable," on a specific-project.</p> <ul style="list-style-type: none"> ■ Design consultants will not be additional insureds ■ Will be procured by the design-builder
Project-Specific A/E Professional Liability Policy	<p>Provides coverage for failure to perform design services by the project design team on a specific-project</p> <ul style="list-style-type: none"> ■ It is increasingly common on design-build projects that the design-builder is named as an insured under the policy and is subject to the insured vs. insured exclusion ■ Professional services within construction means and methods will be excluded ■ Insureds will agree to joint defense ■ May be procured by the owner as part of an OCIP, or by the A/E or design-builder directly (terms and conditions may vary) ■ Owner may be an indemnified party
Owners Protective Professional Indemnity Policy	<p>Provides owner with indemnification excess of the professional liability limits available through the annual A/E professional liability policies of the design team involved in a project.</p> <ul style="list-style-type: none"> ■ Typically not used in design-build
OTHER CONTRACTOR POLICIES	
CGL Policy	<ul style="list-style-type: none"> ■ Professional services exclusion typical ■ CG 2279/2280 endorsements can provide bodily injury and property damage coverage ONLY
Builders Risk	<ul style="list-style-type: none"> ■ Professional services exclusion typical ■ Cost of making good "errors in design" or "defects in workmanship" are generally excluded, but "ensuing" losses are covered

In the following claim examples, we consider how the various professional liability policies referenced in the table above might respond.

CLAIM SITUATIONS



In Claim Situation 1, an unrelated third party makes a demand of the project owner alleging economic loss, bodily injury or property damage arising from the negligent acts, errors or omissions in the professional services provided to the owner by the design-builder or its consultants. Potential third parties include adjacent property owners, contractors active on adjacent projects, members of the general public, and governmental funding or regulatory agencies.

Contractor’s Professional Liability Policy	<p>The owner would not be covered under this policy for such claims. The owner would have to rely on any contractual indemnifications and other provisions for protection, and tender a demand against the design-builder (see Claim Situation 2 below).</p>
A/E Professional Liability Policy	<p>The owner would not be covered under this policy for such claims and would have to rely on any contractual indemnifications and other provisions of the design-build agreement for protection, tendering a demand against the design-builder (see Claim Situation 2 below). In most jurisdictions, privity of contract will prevent the owner making a demand directly against the design-builder design professional consultant(s).</p>
Project-Specific Contractor’s Professional Liability Policy	<ul style="list-style-type: none"> ■ The owner would not be covered under this policy for such claims and would have to rely on any contractual indemnifications and other provisions for protection, and tender a demand against the design-builder (see Claim Situation 2 below). ■ The owner may be able to obtain indemnity under the policy by means of an indemnified party’s endorsement.
Project-Specific A/E Professional Liability Policy	<ul style="list-style-type: none"> ■ The owner would not be covered under this policy for such claims. ■ The owner may be able to obtain indemnity under the policy by means of an indemnified party’s endorsement. This would be more usual when the owner has procured the policy as part of an owner-controlled insurance program. If the policy has been procured by the design-builder it is less likely that such indemnification will be afforded the owner.
Owners Protective Professional Indemnity Policy	<p>As noted above, it is not usual that this policy would be utilized in design-build. In the event, however, that the owner has contracted directly with other A/Es for design services, the owner’s protective policy may provide the owner with indemnification.</p>

In Claim Situation 2, the project owner alleges economic loss, bodily injury or property damage arising from the negligent acts, errors or omissions in the professional services provided to the owner by the design-builder or its consultants. The owner may also allege various breaches of contract, warranty, fiduciary duty etc., any or all of which may have resulted in damages to the owner for repair and rectification work expenses, payments to third parties, and consequential damages (including lost revenues).

<p>Contractor’s Professional Liability Policy</p>	<ul style="list-style-type: none"> ■ The contractor would be covered for its own acts and the acts of the design-builders design professional consultants, for whose performance it will typically be legally liable. ■ Contractor’s insurer may seek to engage the A/E insurer in the claim resolution process or proceed against them on a subrogation action.
<p>A/E Professional Liability Policy</p>	<p>The contractor would not be covered under this policy. It would be necessary for the contractor and its insurer to defend the claim and seek participation from the A/E’s insurer or subsequently proceed against them on a subrogation action.</p>
<p>Project-Specific Contractor’s Professional Liability Policy</p>	<ul style="list-style-type: none"> ■ The contractor would be covered for its own acts and the acts of the design-builders design professional consultants, for whose performance it will typically be legally liable. ■ Contractor’s insurer may seek to engage the A/E insurer in the claim resolution process or proceed against them on a subrogation action.
<p>Project-Specific A/E Professional Liability Policy</p>	<p>As noted above, it is increasingly common for the underwriters to add the design-build contractor as an insured under this policy. The contractor would therefore be covered by the policy with respect to damages arising out of the acts, errors or omissions of the design-builder design professional consultants. It should be noted, however, that coverage will not typically provide for the design-build contractor’s own professional services within construction means and methods.</p>
<p>Owners Protective Professional Indemnity Policy</p>	<p>As noted above, it is not usual that this policy would be utilized in design-build.</p>



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In Claim Situation 3, the design-builder makes a demand for damages directly against the design professional consultants for negligence (or possibly breach of contract) in failing to adequately perform the professional services. The action of the design-builder may have been prompted by owner or third-party claims as outlined in the claim situations discussed above.

Contractor’s Professional Liability Policy	<ul style="list-style-type: none"> ■ This policy would not generally provide coverage for the damages. ■ Underwriters who offer first-party excess indemnification wordings would respond to losses in excess of the design professional consultants A/E professional liability policy.
A/E Professional Liability Policy	This policy would provide the design-builder’s design professional consultants with coverage.
Project-Specific Contractor’s Professional Liability Policy	<ul style="list-style-type: none"> ■ This policy would not provide coverage for the damages. ■ Underwriters who offer first-party excess indemnification wordings would respond to losses in excess of the design professional consultants A/E professional liability policy.
Project-Specific A/E Professional Liability Policy	As noted above, it is now usual for the design-build contractor to be an insured under this policy. Due to the insured vs. insured exclusion, the design-builder’s recourse under this policy may not be possible, or be restricted to third-party BI/PD claims only.
Owners Protective Professional Indemnity Policy	If placed, this policy would not provide any coverage for this situation.

Contractors and design professionals in joint-venture or teaming relationships for design-build projects face substantial exposure for the risk of defective design – and limited contractual and risk transfer mechanisms for effectively allocating and managing the risks. In design-build contracts, the contractor and designer must work out an equitable and balanced risk management/transfer protocol or risk losing the collaborative efficiencies of the design-build approach. Done properly, design-build arrangements can reduce overall risk. Without attention to the process, contractor and designer are that much more likely to start pointing fingers at each other – or end up in litigation – when problems arise.

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