Blueprint

for Design Professionals

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Navigators
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Welcome to our fourth edition of Blueprint For Deisgn Professionals. The articles for this issue provide a primer for the claims process and on green construction risks. Let us know your thoughts as it helps us to deliver to you information relevant to your practice. Send us article ideas, risk management questions, and any other comments you might have to David Soltero at dsoltero@navg.com. While we may not be able to respond to you directly, we will do our best to incorporate the answers and ideas in future issues.

"According to McGraw Hill Construction, 25% of all new construction activity in 2010 was green"

Green Construction Risks Revisited

By Craig S. Thompson

It has been more than a decade since the U.S. Green Building Council (USGBC) developed the Leadership in Energy and Environment Design (LEED) rating system for the design and construction of green buildings. The LEED rating system quickly became the standard for measuring the effectiveness of green design and construction, and remains so to this day.

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Reporting Claims and Potential Claims – How, When & Why

By David Soltero

A question that is often asked by our insureds is, "When does a matter have to be reported?" As you should be aware, there are two events which should be reported to your carrier – claims and potential claims. Before we go any further, it is first necessary to understand the definition of a "claim".

Referencing the Navigators Design Professionals Liability Policy:

> Claim means a demand for money or services received by the Insured arising out of a wrongful act or pollution incident in the performance of professional services. ….

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Many expected that with the proliferation of green construction over the past decade there would be a corresponding increase in claims against the design professionals working on these projects. And while there have been claims, most would agree that the green building evolution has not yet produced the type or extent of claims that were predicted.

So, what are we to make of the lower than expected claim activity on green projects? Did we over estimate the risks of green construction? Absolutely not. The number of green construction projects has risen exponentially each year in the past decade and will continue to do so. According to McGraw Hill Construction, 25% of all new construction activity in 2010 was green, and nonresidential green building activity is expected to triple between 2010 and 2015. The "green" phenomenon is unquestionably here to stay, along with its inherent risks.

The construction industry has been busy adapting to the changed landscape of green construction and its unique challenges. One theory is that we were too busy over the past decade learning the green system to be distracted with claims and litigation. Owners, design professionals, and contractors also shared a common interest in furthering the fledgling green construction industry. Another factor has been the cost and uncertainty of litigating a green construction dispute where no precedent exists. Green construction case law is sparse, but that will no doubt change as existing cases work their way through our courts.

The uncertainty in financial markets over the past decade also contributed to lower claim volumes. A more robust economy would have resulted in more green construction projects. This would have compressed the learning curve and resulted in errors and claims that were otherwise avoided.

We know that claim activity lags construction. It takes time for defects to surface and mature into claims. It is theorized that there is a more pronounced lag in green construction claims because new and experimental designs, materials, and construction techniques are still being evaluated. For example, a building owner would have a difficult time proving a "high utility cost" claim without data from a comparable green building. This type of performance data is now readily available due to the passage of time and proliferation of green construction. Similar data is becoming available on construction materials that were new and innovative 10 years ago.

A combination of some or all of the above factors contributed to lower than expected claim volumes over the past decade. The same cannot be said for the next decade, which means now is not the time to relax in our efforts to manage risks on green projects. A good place to start is making sure that your contracts properly allocate the rights and responsibilities of the parties involved in the green construction project. It is recommended to use one of the new series of green construction contracts from the American Institute of Architects (AIA).

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These contracts have been carefully written and coordinated to properly allocate risks on green projects. In 2011, the AIA launched an entire series of sustainable project (SP) contract forms based on their existing 2007 series of contracts. These are not simply green "addendums" to existing contract forms, instead they are complete contracts dedicated to green construction projects. A helpful resource from the AIA is their *Guide for Sustainable Projects* released in May 2011. The guide can be downloaded for free at www.aia.org.

We are currently in perhaps the most competitive atmosphere that the construction industry has ever seen. The pressure to secure new work is enormous. Overstating or guaranteeing a specific project outcome will create significant claims exposure, and will not be covered by insurance. The design professional needs to avoid giving verbal or written assurances regarding obtaining project entitlements (e.g. tax credits), LEED certification, building performance and financial savings. While insurance products available to the green construction industry have expanded, there is still no insurance that will protect the design professional from claims relating to the above representations. Your contract should clearly indicate that the design professional does not guarantee a building will meet prescribed energy efficiency levels or achieve/retain LEED certification.

The ever expanding regulatory scheme for green projects poses a risk to the design professional. As green construction has evolved, so too have the efforts to regulate it. Various green initiatives including legislation, ordinances, executive orders, and resolutions have been adopted at the federal, state and local levels throughout the country. One such example is the International Code Council's new International Green Construction Code (IgCC). It has already been adopted by many states and requires green design and construction regardless of whether the owner intends to achieve LEED certification. This type of regulation arguably elevates the standard of care for all design professionals. More so than ever, the design professional must carefully review the codes and requirements of the jurisdiction where the project will be built. A green consultant should be retained (or the project passed on) if there is any question on whether the designer is properly qualified.

It is inevitable that green construction claims will escalate in the next decade. Design professionals who remain vigilant in their approach to green construction and its inherent risks will be best suited to avoid and/or minimize the impact of same.

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A wrongful act:

> means an act, error or omission in the performance of professional services by the Insured or by any entity or person, including joint venture for whom the Insured is legally liable.

The definition of a claim, as a demand for money or services, is generally consistent across professional liability carriers. A design professional is frequently presented with "demands" over the course of a project. Are all of these claims as defined by the terms of your professional liability policy? The answer is clearly, "No." There are two parts to the definition of a claim and both must be met: (1) there must be a demand for money or services; **and** (2) that demand must be related to a wrongful act of the insured. If you are faced with a claim, you need to report it to your carrier.

Here is an example:

> The house I designed is experiencing moisture infiltration around the windows. When I went on sight, I noticed the contractor did not install any flashing even though it is noted on the plans and I provided the detail. The contractor is saying that he followed my plans exactly. The owner is not blaming me, she just wants it fixed and has asked us and the contractor to share the expense of remediation.

Is this a claim? The answer is, "Yes." It is surprising how many insureds (and brokers who do not specialize in design professionals) believe that a claim means the insured is being sued. Furthermore, it is not uncommon for an insured to think that only the person s/he contracted with can make a claim. In the above example, the contractor is asserting the design was deficient and the owner, who only wants what she paid for, is asking the design professional to contribute based on the contractor's representations. The truth of the allegations is irrelevant.

What is a potential claim? Again, quoting from the Navigators policy, a potential claim exists when the design professional "becomes aware of any act, error or omission which may reasonably be expected to be the basis of a claim against any Insured …". A design professional is required to provide specific information to demonstrate there is a potential claim. Under the terms of the Navigators policy, an insured must provide:

a. The specific act, error or omission;

b. The dates, entities and persons involved;

c. The identity of anticipated or possible claimants;

d. The **professional services** or activities the **Insured** provided or engaged in;

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e. The circumstances by which the **Insured** first became aware of the potential **claim**; and

f. Potential damages or injury;

Not everything that goes wrong during the design and / or construction phase qualifies as a potential claim. For instance, the mere fact that a contractor and owner are arguing over money is not sufficient to report a potential claim. Now, if the design professional believes that the argument is over work the contractor claims it had to perform to correct problems in the insured's design, this could meet the threshold. If the design professional is told an HVAC system it designed is not keeping a building cool enough in summer, but no demand has been made - this could be a potential claim.

If you are served with a subpoena for documents or for the deposition of an employee related to a project, this would generally be considered a potential claim and you should absolutely seek pre-claim assistance. In most cases, your carrier will retain an attorney to assist you in responding to the document request or to prepare you and defend you at the deposition.

One of the most significant sources for potential claims is the dreaded fee claim, where the client refuses or ignores the design professional's requests for payments. Not all fee claims are potential claims; they still need to meet the requisites listed above. For instance, if a design professional is not paid due to economic issues, this would not be a potential claim. However, if the design professional believes its client has not paid it because she was not satisfied with the insured's work product, this would be a potential claim. Whether or not fee claim is considered a potential claim, you should be sure to discuss these with your broker and your carrier before deciding to file a collection action. In the vast majority of fee cases, the client will file a counterclaim against the design professional for negligence and the costs of the action wind up dwarfing the amount of the original fee claim.

Another question that is often asked is, "Why should I put the carrier on notice of a potential claim?" The initial answer is that often pre-claim assistance is a free service provided by carriers, such as Navigators. By doing so, you tap into the expertise of your carrier to assist you in either keeping the potential claim from becoming a full-fledged claim, or reducing the expense of the claim through early intervention. Additionally, if a potential claim is submitted to Navigators and it is believed an attorney needs to be retained, as in a subpoena, or a forensic expert needs to be hired, e.g., where the contractor is faulting the design and the design professional is faulting the construction, the expense will generally be borne by the carrier and will not be applied to the limits of liability set forth in the policy. Lastly, if a potential claim is reported and accepted, the insured is provided coverage if the matter becomes a claim, even if the policy under which the potential claim was reported has long expired.

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As to when a claim or potential claim should be reported, the quick answer is as soon as practicable. The more technical answer is that professional liability policies are "claims made and reported" policies. This means that an insured must report a claim that is made against an insured during the effective dates of the pertinent policy. These policies typically provide a grace period after the expiration of the policy for the insured to report claims that occurred during the effective dates of the policy. Potential claims can only be made during the effective dates of the policy.

The above information is intended to be general in nature and does not define any rights under an insurance policy or otherwise. All insurance coverage is provided according to the terms of your specific insurance policy

David Soltero manages Architects and Engineers liability claims for Navigators. If you would like more information with regard to this article, please do not hesitate to contact David at (212) 613-4357 or at dsoltero@navg.com.

Upcoming Webinar

Learn how copyrights not only protect you, they may help you get paid!

Please join Navigators Insurance Company, in conjunction with the AIA Pasadena & Foothill and the law firm of Collins, Collins, Muir & Stewart, LLP, for a complimentary webinar on Architectural Copyrights. The webinar will address ways design professionals can utilize copyright provisions in their contracts to protect their designs, ensure payment of fees, and protect themselves from future liability. Webinar attendance is eligible for an AIA continuing education credit.

Topic: Copyright for Architects and Engineers
Date: Wednesday, May 16, 2012
Time: 3:00 pm, Eastern Daylight Time (New York, GMT-04:00)
Meeting Number: 761 578 742
Meeting Password: Navigators1

1. Go to https://navg.webex.com/navg/j.php?ED=164287792&UID=0&PW=NMmU1YTRkNzAw&RT=MiMxMQ%3D%3D
2. If requested, enter your name and email address.
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