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The column format frees me from constraints imposed by academic writing, but adds those of space and time, which may be worse. But here goes!

In preparing the recently published fifth edition of my Legal Aspects of Architecture, Engineering and the Construction Process, (no talk show invitations, so ...) among my card notes I saw one captioned “The Symphony.” Between 1966 and 1975, I taught a course for architectural students in Berkeley, California. One student paper drew an analogy between the performance of a symphony and creating a building. Who is blamed if the music sounds bad or the building is judged a failure? Let me develop that analogy.

Who are the major actors involved in the symphony? (For simplicity I shall omit guest soloists.) The symphony association, with trustees and an artistic director, raises the money, provides the hall, engages the conductor, pays the musicians, and may, through the artistic director, play a role in selecting the program and musicians.

The composer—most dead, but some alive—provides the score.

Generally, the conductor chooses the musicians, selects the program, conducts rehearsals, interprets the score, sets the tempo, coordinates the musicians and playing, and has general control of music activities. To underscore his importance, he is paid handsomely, figures prominently in marketing, and is the star of the show. The musicians and their instruments actually create the sounds.

Since we will talk of success and failure, we must include those who evaluate the performance: the audience, the critics, and key association members—and big donors.

If the performance is a success, the major credit will go to the conductor. To be sure, a live composer may get some kudos, as may the artistic director and trustees who hired the conductor. But the main sniffer of the sweet smell of success will be the conductor.

But suppose it fails? The audience hates the music, leaves early, refuses to applaud, and even makes a few cat-calls. Also, the critics savage the performance, and prospective donors keep their checkbooks in their pockets.

There can be many reasons for failure. The music may have been too modern, too boring, or too long. The musicians may have played badly because they had no talent or too few rehearsals. Their individual performances may have been adequate, but badly coordinated. The interpretation or tempo may not have done justice to the score nor the intent of the composer and offended the musical sensitivities of the audience or critics. The conductor had control over all these causes. Others, such as the musical director, may take some of the blame, but the main hit is taken by the conductor. He basks in glory when things go well. He is blamed when it does not.

Now, to the building project. We all know the main actors and their roles when the project is built under AIA documents. I shall note exceptions, such as the use of design/build (DB), a construction manager (CM), or an experienced owner who take control.

Who gets the credit if the project is successful? In building there are more varied evaluators and criteria for evaluation and more actors upon whom credit (or blame) can be spread. Evaluators can include the owner, prospective owners, users, communities of architects and contractors, and the public. At the risk of oversimplification, if the building looks good, works well, and came in within budget, the credit will go to the architect. Evaluators who can judge quality will credit the contractor for high-quality workmanship. The contractor will also receive credit if the project is “on time.” Others may share in the credit with major recipients. The architect in the AIA system plays a role in monitoring performance and may receive some credit for execution, and the contractor, through subcontractors, may be a part in design and share design credit. But we must conclude the architect receives most of the credit for success because of design centrality and his site role.

Now failure. For simplicity I define failure as a building that looks bad, functions poorly, is of poor quality, cost too much, and took longer to build than planned. If it looks ugly, works badly, or cost too much, the architect is blamed. If the workmanship is poor and completion is delayed, the principal culprit is the contractor, with some blame being placed upon the architect because of the broad powers given him under AIA documents.

Any DB takes all the credit and the blame. A CM may participate in credit and blame for activities under his control, such as budget, coordination, and workmanship. An experienced owner, who runs the show, gets credit and blame.

Now let us compare the actors in these two ventures. Clearly, the association is the owner and the composer is the architect. The difficult question is who is the conductor of the symphony using the AIA system? Using the credit–blame criterion, it is the architect. Both architect and conductor are the principal recipients of the credit and the blame.

Looking at the functions they play makes slotting more difficult. The conductor, as with the conductor, assembles, coordinates, interprets, and executes. But the powers given to the architect under AIA documents, in addition to his furnishing the design, make him look more like the conduc-

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Different types of coverages. As a result of the catastrophic Many of these companies were permitted to write several policies in which they tightly defined the risks covered. Subclassifications of fire, marine, and casualty insurance. Being classified into two broad categories: life insurance and anything other than life. The latter category included subclassifications of fire, marine, and casualty insurance. Construction insurance is helpful in understanding the scope and limits of insurance coverages that are now available. The inherent flexibility of the inland marine coverage brought with it widespread acceptance. This, coupled with the relaxation of statutory controls, slowly led to multiple-line coverages in which one insurer would cover numerous risks. 

Construction Insurance
(continued from page 1)

Alternative construction delivery systems, including design/build, construction management, and multiple prime contractors present unique questions of risk allocation and insurability. Malpractice policies for design professionals typically include an exclusion for projects where the construction is performed by a company that is partially or wholly owned by the architect/engineer (A/E). Contractors Commercial General Liability (CGL) policies exclude coverage for errors and omissions committed by A/E's. These nontraditional systems warrant careful evaluation and analysis to ensure that certain risks are adequately covered by insurance.

Risks don't end when construction of the project is completed. In fact, the collapse of the walkways in the atrium of the Hyatt Regency Hotel in Kansas City provides a sobering example of the severity of the risks after a project is completed. The time lapse between an A/E's or contractor's errors, omissions, or negligence and the resultant damages or injury can be months or even years. These delayed damages are insurable, but not without some careful planning with a knowledgeable insurance advisor so as to develop an integrated insurance program in order to prevent uninsured gaps in coverage.

Historical Background of Construction Insurance

Most practitioners take for granted the present type and availability of insurance, which protect risks inherent in the construction process. A brief study of the historical roots of construction insurance is helpful in understanding the scope and limits of insurance coverages that are now available. The American insurance industry today is the result of centuries of evolution. So-called modern insurance began with marine insurance in the 1400s, and fire insurance in the 1600s after the Great Fire of London in 1666. Interestingly, as late as just a few years ago, some marine insurers were still using policy language very similar to that used in policies dating back to the 17th century. As the insurance industry developed, insurance was being classified into two broad categories: life insurance and anything other than life. The latter category included subclassifications of fire, marine, and casualty insurance.

Early United States insurers usually wrote their own policies in which they tightly defined the risks covered. Many of these companies were permitted to write several different types of coverages. As a result of the catastrophic Chicago Fire in 1871, which resulted in the failure of many small companies, the National Convention of Insurance Commissioners recommended and pushed through legislation prohibiting life insurers from taking on any other type of risk. This led to the birth of the American system that required other coverages, e.g. fire, casualty, and workers' compensation, to be distinct from the other, and, to some extent, handled by separate companies. The rationale behind this approach was that companies had a greater chance of remaining solvent if they specialized and if they were carefully regulated. The rigidity of the American system soon led to the development of hybrid insurance policies such as the inland marine policy, which covered standard transportation risks as well as other more unusual risks. Eventually, inland marine policies provided all risk insurance for property at fixed locations rather than risks only associated with property in transit. This concept was readily adaptable to construction risks, since the title to materials and equipment eventually incorporated into the project passed through several parties, including suppliers, subcontractors, the contractor, and then the owner. 

The inherent flexibility of the inland marine coverage brought with it widespread acceptance. This, coupled with the relaxation of statutory controls, slowly led to multiple-line coverages in which one insurer would cover numerous risks. Ironically, risk-taking by insurers in offering multiple-line coverages, which threatened insurance industry solvency, gradually led to standardization of coverages and forms. Standard, printed forms, however, were available as early as 1779.

Today, standard policy forms are written by insurance industry groups and associations, including the Insurance Services Office, formed in 1971 by merging five major national rating and statistical organizations. Also, many states have prescribed forms for some policies, or regulate the approval of policy forms and provisions.

Most practitioners take for granted the present type and availability of insurance, which protect risks inherent in the construction process.
The standard policy forms available in today’s market, regardless of the risks covered, are triggered by either an “occurrence,” as defined by the policy, or when a claim is made. Workers’ compensation, commercial general liability, and builder’s risk policies have traditionally been occurrence policies, although as recently as 1985 the insurance industry began offering a claims-made policy for certain general liability coverages. On the other hand, professional liability policies are written almost exclusively as claims-made policies. The distinction between the policies will be discussed later.

With this brief historical background, we are now ready to launch into a discussion of the insurance coverages commonly available to insure the risks involved in the construction industry. This discussion is limited to the four basic policy forms: builder’s risk, commercial general liability, professional liability, and workers’ compensation.

**Overview of Construction Insurance**

**Builder’s Risk**

Builders risk insurance provides property coverage that reimburses the insured for damage to, or destruction of, a
project under construction, regardless of the insured’s fault. It is similar in concept to homeowners’ fire-extended coverage policies, or automobile collision damage insurance, but differs from those well understood coverages in important particulars, most of which relate to special needs or problems in the construction process.

Who Is the Insured?

It may seem obvious that an owner of a construction project needs protection against accidental casualty, but brief reflection suggests that almost everyone connected with a project needs such protection, at least for short periods of time. A critical difference between builder’s risk and other types of property insurance is the unusual number of insurable interests that are accommodated. By its nature, builder’s risk insurance covers the interests of all the parties to the construction process as their interests may appear.

One cannot overestimate the importance of this type of coverage to the construction process. Delay is the enemy of the construction process, and any impairment of cash flow usually causes a delay with consequent loss. If partially completed construction or construction materials are destroyed, without a ready source of reimbursement of the costs to replace or repair the loss, the parties simply invite dispute, which will inevitably delay the project. The owner, particularly, is at risk from a substantial uninsured casualty, even though technically the risk of the loss falls on others.

For example, if a major fire loss during construction causes the general contractor’s insolvency, which results in its inability to proceed, the owner will at best incur substantial unrecoverable legal costs trying to keep the project afloat. At worst, such a loss could ultimately impair the solvency of an owner whose finances are tight. The owner, of course, ultimately pays for all insurance on the project, either directly or indirectly as a cost of the contractor and subcontractor.

Not surprisingly, then, most standard form contracts give the owner the responsibility for obtaining the builder’s risk insurance. Because the continuity of the project, and therefore the owner’s interest, depends to some degree on all trade contractors being reimbursed, standard documents typically require the owner to purchase coverage for all parties to the process. These documents likewise usually require coverage for the insurable interests of the owner, contractor, subcontractors, or suppliers, although the latter two interests may be specifically excluded.

Of course, the owner can vary these terms so that other parties provide all or part of the builder’s risk insurance. However, because the owner has a very real stake in the continuity of the project, and because the owner will ultimately pay for the coverage, the owner should buy and maintain control of the coverage.

What Property Is Covered?

During construction, many different types of property find their way to the job site. The constructed but uncompleted work is the most obvious. Many others, which are not as apparent, do pose a risk of loss to one or more of the construction participants. The subcontractor may have materials stored in a trailer on the site for later use in the project. The contractor has expensive equipment such as cranes, lifts, bulldozers, and other equipment on the job site every day. A failure to insure the structure, materials, or equipment may imperil the success of the project.

“So, just what property is insured?” one may ask. The answer depends upon the specific coverages stipulated in the policy. Several standard policy forms vary significantly with important consequences.

The most desirable form, and the most expensive, is the so-called “All Risk Policy Form,” which insures the property of all of the insureds at the construction site, whether or not already incorporated into the project. (For example, lumber destroyed or stolen while stockpiled on a site would be covered.) The standard American Institute of Architects (AIA) documents require this type of form. Coverage can even be purchased for material in transit, material delivered for the project but stored off-site in a designated warehouse, or tools and equipment. By contrast, other forms provide coverage only for property actually incorporated into and made part of the project. Among the property losses at a construction site, damage, destruction, or theft of building material stored there is certainly not uncommon. Therefore, these forms could result in substantial uninsured risks to several of the construction parties if those parties decide not to insure those risks on their own.

Term of Coverage

Generally, builder’s risk coverage applies only to buildings under construction and it lapses or is cancelled once the structure is completed and/or beneficially occupied by the owner. Coverage presumably begins when construction commences. Ascertaining when construction begins and ends can be problematic.

For example, in a Mississippi case, the insurer denied coverage when fire destroyed an existing building, arguing that the contractor’s disconnecting of old plumbing and gas lines was merely preparatory to renovation of the building. In other words, the insurer claimed that the loss had not occurred “in the course of construction.” Fortunately for the contractor and owner, the court found coverage, since it was necessary to the renovation as any subsequent new construction.

Likewise, determining when coverage ends usually
depends on the specific language of the policy. Some policies provide that coverage ceases when the structure is occupied or used for its intended purpose. Others define several events that trigger the expiration of the policy, including: (1) when the insurable interests in the property cease; (2) when the policy term expires; (3) when the property is accepted by owner as complete; or (4) when the policy terminates, whichever occurs first.

Determining the date of completion, acceptance, or occupancy—if those are the triggering events—is not always clear. The difference between substantial completion and final completion may have a significant impact on when coverage expires. Some courts have held that substantial completion is the operative date even if minor punchlist work remains to be completed, while others have indicated that the owner's formal acceptance of the project controls. Still others have decided that a project is not deemed occupied with resulting termination of coverage “if the structure is never put to more than a transient or trivial use.”

To avoid gaps in coverage that may result at the end of the job, owners are encouraged to obtain property insurance on the structure at or just before substantial completion or occupancy of the building. This covers the risk of an unfavorable decision by a court in determining when the builder's risk coverage expired.

Special Considerations

Another important consideration is the standard policy exclusion for loss or damage caused by or resulting from faulty or defective workmanship or material, except in cases in which the defect caused a resulting peril such as a fire or explosion, which is not otherwise excluded. The intent of the exclusion is to require the insured to pay for its own defective design or construction. The "ensuing coverage loss" exception to the exclusion is fairly easy to understand. The practical application of it, however, may be more difficult.

In a related vein is the problem of deductibles. Many property coverages, such as automobile collision and the standard homeowners' coverages, allow the insured to buy deductibles that will drastically reduce the premiums. While deductibles in such coverage are usually a good idea, one should remember that in the peculiar circumstances of construction, which sometimes make multiple casualties more likely, the imposition of separate deductibles may unintentionally create a rather large uninsured loss.

For example, in Bob Bros. Construction v. Board of Levee Commissioners, the owner of a project to build a breakwater and retaining wall for a marina bought builder's risk coverage with a $50,000 deductible, for which it received a substantial premium reduction. During construction, the work was damaged by storm tides and wind on 19 different occasions. Each loss was thousands of dollars, though none, separately, met the deductible; however, the aggregate loss greatly exceeded $50,000. The court held that the policy did not provide coverage since the deductible was never exceeded for any one occurrence.

Waiver of Subrogation

A sometimes misunderstood aspect of builder's risk coverage is waiver of subrogation among the insured participants. A typical construction casualty is caused by the individual incidents of negligence attributable to one or more contractors or subcontractors. Without builder's risk coverage, each property insurer would pay its insured's loss, take a subrogation, and then attempt to recover its payment from the tortfeasor. This process results in substantial legal costs, and is counterproductive to the overriding goal of cooperation and understanding among parties to a project.

Therefore, most standard contract forms include a waiver of subrogation provision in the policy by which each insured waives subrogation against the other. In other words, in the event of a loss, the insurer pays each insured its own loss, and the matter ends there. For example, if the electrical subcontractor's negligence caused damage to the drywall subcontractor, the subrogated insurer, after payment of the drywall contractor's loss, could not sue the electrical sub.

Commercial General Liability

Covered Risks

The CGL policy provides coverage for accidents and injuries arising out of the operations of the contractor. It's intended to cover accidental damage caused by the contractor, but not the contractor's poor performance of the work called for in the contract.

For example, damages resulting from the insured's failure to perform the contract where the only damage is to repair or correct deficiencies in the work are not generally covered. However, damages other than the work itself, which result from the insured's negligence, are usually covered. Also, damages that are a reasonable, foreseeable consequence of the insured's actions are not considered accidental. Moreover, a contractor's breach of an express or implied warranty is not generally covered.

The CGL policy provides coverage for both bodily injury and property damage, and defines these terms to require that the injury result in some actual physical injury or damage. Economic losses and emotional distress damages, without a concurrent physical injury, are not usually covered by the CGL policy. At least one court has held that emotional distress damages, without some physical mani-
festation of injury, are not covered. Likewise, property damage must result from some actual physical manifestation of damage. Many courts have also held that lost profits or diminution in value of a building are not property damage within the meaning of the policy.

**Occurrence Trigger**

CGL policies are now written on both an occurrence and claims-made basis, although the occurrence basis is still the most prevalent. Under an occurrence policy, an accident or injury is covered if the accident occurred during the policy period. Under a claims-made policy, the accident or wrongful act or omission must happen during the policy period and the claim must be made during the policy period.

With an occurrence policy, the coverage clause of the policy is triggered only upon an “occurrence,” as that term is defined in the policy. Current policies define an occurrence as “an accident, including continuous or repeated exposure to substantially the same general harmful conditions.” Standard policies before 1986 defined an occurrence generally the same, except the phrase “neither expected nor intended from the standpoint of the insured” is included at the end. Both definitions were intended, but not always interpreted, to exclude damages that result from the insured’s intentional acts. This issue has received considerable attention in latent disease cases, such as asbestosis and silicosis. From these cases, four theories have emerged for determining the trigger of an occurrence.

1. Exposure theory: Coverage is triggered when the person or property is accidentally exposed.
2. Manifestation theory: Coverage is triggered when the injury or damage first manifests itself.
3. Date of injury theory: Coverage is triggered at the onset of the injury or damage.
4. Continuous trigger theory: Coverage is triggered by any of the previous three triggers.

For property damage claims, which most commonly arise during construction, the courts have most often adopted the exposure theory.

**Standard Exclusions**

The CGL policy is written with a number of standard exclusions to ensure that coverage does not exceed its intended scope; only the most critical exclusions are discussed below.

The first of these exclusions, which used to be written into the definition of occurrence, is for damage expected or intended from the standpoint of the insured. Clearly, if the policy is intended to cover accidental damage, then damage that is not accidental should not be covered. This exclusion recognizes a broad social policy against allowing persons to obtain insurance to cover intentional damage caused to others. If the contractor has the ability to control whether the damage or injury occurs, then the damage or injury is not considered accidental and isn’t covered. Battery on a person is an example of an intentional act excluded under the policy.

Another key exclusion is for damage to the work or product of the insured, commonly known as the business-risk exclusion. Generally, damage caused by the contractor’s faulty or defective work is not covered if the only damage is to the work itself. The purpose of the exclusion is to prevent coverage for the contractor’s breach of contract in providing defective workmanship. However, the CGL policy will cover incidental damage or damage to another contractor’s work resulting from the insured’s failure to properly perform its work, assuming, of course, that an occurrence has taken place. Based on recent policy changes, the general contractor’s CGL policy will provide coverage for damages or injury arising out of a subcontractor’s defective work, including costs to repair or replace the damaged work.

The owned-property exclusion is a sometimes overlooked but important exclusion. This exclusion denies coverage for personal property in the “care, custody, or control of the insured”; real property on which the insured is working; and property that must be repaired because the insured’s work was improperly performed. This exclusion denies coverage for property owned by the insured and for property not owned by the insured, but which the insured is in possession of or has control over. The purpose of this exclusion is to eliminate coverage for items normally covered by the contractor’s property or builder’s risk insurance policies.

Not unexpectedly, determining whether property is in the care, custody, or control of the insured has confused some judges. A number of courts have held that exclusive control over the damaged property is required for the exclusion to apply. In other situations, the courts have required mere possessory control to trigger the exclusion. However, property that is merely incidental to the work, or to which the insured had a mere right of access, is generally not considered to be under the insured’s control. In still other cases, courts have decided that the exclusion is inherently ambiguous, and have refused to enforce it.

**Generally, damage caused by the contractor’s faulty or defective work is not covered if the only damage is to the work itself.**

As a result of massive litigation involving toxic substances and the costs for remediation and cleanup, the pollution exclusion in the standard CGL policy has received considerable attention and scrutiny. Prior to 1986, this exclusion generally excluded coverage for bodily injury or property damage arising out of the discharge, dispersal, release, or escape of toxic substance or waste materials unless such discharge, dispersal, release, or escape was sudden and accidental. This exclusion focuses on the polluting activity itself rather than the result of the polluting activity.
As could be expected, determining the meaning of “sudden and accidental” caused the courts great difficulty, with many courts going to great lengths in finding coverage.\textsuperscript{45} Recently, however, some courts are giving the exclusion a strict construction and giving the word “sudden” a temporal meaning.\textsuperscript{49}

The current version of the pollution exclusion eliminates the sudden-and-accidental exception and expands its breadth to include the threatened discharge of pollutants and toxic waste. The new exclusion also excludes coverage for CERCLA response costs, which was found covered under the prior exclusion by many courts.

Recent court decisions have started limiting or defining the scope of this new exclusion. Damage to chicken parts contaminated by odors emitted by flooring materials made of styrene was declared outside the exclusion since styrene was a raw material and not a pollutant.\textsuperscript{50} Also, tort litigation arising from a city’s spraying operations to control insects was considered covered under the city’s CGL policy since the chemical used for spraying was not a pollutant recognized as such in the industry or by government regulations.\textsuperscript{51}

One final exclusion worthy of note is the contract-liability exclusion, which denies coverage for liability assumed by the insured under a contract or agreement. However, this exclusion does not apply to an insured contract or liability that the insured would have in the absence of the contract. An insured contract is defined as that part of any contract under which one assumes the tort liability of another. In other words, the policy provides coverage for liabilities that would be imposed by law absent the contract or agreement. Standard indemnity provisions usually fall into this category. However, this exclusion does not usually apply to situations in which indemnification by operation of law applies.\textsuperscript{52}

**Policy Terms**

Insurance coverage is provided only for accidents that occur during the policy period. Additionally, the damage must occur while the insured is performing operations,\textsuperscript{53} unless extended or completed operations coverage is purchased.

CGL insurance is typically provided in two separate coverages: premises operations and completed operations. Premises operations coverage provides coverage while the contractor is on the construction site and performing operations. Completed operations provides coverage for damages arising from an occurrence that happens after the contractor has finished construction and is no longer on-site. Both coverages must be purchased to give the contractor comprehensive coverage for his work. If the contractor does not obtain completed operations coverage, accidents occurring after he has finished his work are not covered since occurrences happening after the contractor has left the site are specifically excluded under the premises operations coverage.

Naturally, courts have grappled with the concept of when an operation is completed. In the latest revisions to the policy, the term “completed” was rewritten and expanded. An operation is deemed complete when the work has been put to its intended use by someone other than another contractor or subcontractor.

Work that needs service, maintenance, correction, repair, or replacement, but which is otherwise complete, is usually deemed complete.\textsuperscript{54} The latter provision was added to counter adverse holdings of many courts that concluded that work that needed repair or work that was improperly performed was not complete.\textsuperscript{55} In situations in which additional operations are anticipated by the insured and the owner, the courts have also refused to construe the word “complete” literally.\textsuperscript{56}

**Design Professional's Liability Insurance**

**Claims-Made Policy and Coverage Trigger**

Professional liability or errors and omissions (E/O) insurance for the A/E—for purposes of this section, design professional or A/E will refer to architects, engineers, landscape architects, and surveyors—is generally written on a claims-made basis. The claims-made policy provides coverage for an act, error, or omission (sometimes referred to as a wrongful act) as long as the claim is made and the wrongful act occurs during the policy period.\textsuperscript{57} This is in contrast to the occurrence policy, discussed earlier, which provides coverage for accidents or wrongful acts that are committed during the policy period regardless of when the claim is made.\textsuperscript{58} The distinction between the two policies was succinctly stated in *Civic Associates v. Security Ins. Co.*\textsuperscript{59}

A claims-made or “discovery” policy of insurance provides coverage for claims that are discovered and brought to the attention of the insurer during the term of the policy. A claims-made policy of insurance is usually best understood in contrast to an occurrence policy of insurance. An occurrence policy of insurance protects a policyholder from liability for any act done while the policy is in effect.

Thus, the trigger for coverage for a claims-made policy is the date when claim is made against the insured.\textsuperscript{60} “Claim” is defined in most policies as the receipt of a demand for money or services, naming the insured, and alleging a wrongful act. Receipt implies a written demand, although an oral one is conceivably covered. To trigger coverage, service of a lawsuit is not necessary; a demand letter will suffice. However, any demand must include an allegation that the insured committed a wrongful act, i.e., a negligent act, error, or omission arising out of the performance of professional services.

Having determined that a timely and appropriate demand has been asserted, the next inquiry is which time period

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**CGL insurance is typically provided in two separate coverages: premises operations and completed operations.**
applies to define the coverage window. Coverage is available only for those wrongful acts that occur after the effective date of the policy but before expiration of the policy term. “Effective date” is generally defined as the inception date of the first policy issued and continuously renewed by the insurer. By way of example, a policy with an effective date of January 1, 1990, does not provide coverage for wrongful acts that occur before that date. This concept is misunderstood by both insureds and their lawyers and can result in uninsured gaps in coverage. (This is especially true when the A/E changes insurers. Typically, unless an endorsement to the policy is negotiated, the effective date of the policy becomes the beginning date of that particular policy term.)

The effective date can be amended by an endorsement allowing retroactive coverage for prior acts, as long as a claim is not pending or a circumstance known that the insured believes could give rise to a claim on the date when such coverage is requested and/or purchased.\(^6\)

Retroactive or prior acts coverage is especially important for the retired design professional. Not only should the policy cover prior wrongful acts, but should also include a coverage “tail” for claims made during a specified time period in the future. Without either of these features, a retired partner’s coverage could be eliminated if his previous firm failed to renew or decides to cancel its current policy.\(^6\)

Knowing what you are getting from a professional liability policy is sometimes difficult to ascertain. In *Hodge v. Garrett*,\(^6\) remanded for clarification of what specific knowledge the insured had of the coverage provided, a New Jersey court ruled that absent special circumstances a claims-made policy must automatically provide retroactive coverage or the court will treat the policy as an occurrence policy. To help obviate this problem, the insurance agent or broker or possibly the insured’s lawyer should explain to the insured that the policy does not automatically include retroactive coverage.\(^6\)

*Hodge* is one of several instances where a court incorrectly interpreted the coverage provisions of a claims-made policy. For example, one court in describing claims-made policies said “[t]he typical claims-made policy provides insurance coverage for acts or omissions occurring either before or during the term of the policy, provided the claim is discovered and reported during the same policy term.”\(^6\) This court clearly ignored the provision of the policy requiring the wrongful act to occur during the policy term.

As noted earlier, the cancellation or termination of a claims-made policy also terminates coverage, regardless of whether the policy includes an extended reporting provision. By illustration, where the policy stated that the insurer would not be liable for any claims reported after the termination date of the policy, a Louisiana court found that “while some reasonable extension of reporting time for last-minute claims might be allowed, the intent of the policy was to restrict liability to those claims discovered and reported during the policy period.”\(^6\)

Several states have notice-prejudice provisions, which provide that an insurer cannot disclaim liability coverage for failure to give timely notice of a claim unless the insurer shows that the delay prejudiced the insurer.\(^6\) In one case, a Maryland court held that notice-prejudice provisions did not apply to an insurer’s denial of coverage on a claims-made policy when the claim was made after the policy had expired, because to do so would effectively rewrite the insurance contract.\(^6\) This case emphasizes the fundamental requirement that a claim must be made during the policy period. Extended reporting periods do not alter this requirement, but merely give the insured additional time to report a claim made during the policy period.

Some courts have read into the policy an extended reporting period, even though the policy required that the claim be reported during the policy period, thus construing such provisions as void against public policy\(^6\) or deciding that late reported claims should be honored on the basis that the carrier was not actually prejudiced by the late notice of claim.\(^7\)

**Covered Risks**

Unlike other liability policies, which cover only negligent acts, the design professional’s liability policy protects the A/E from claims arising out of negligent acts, errors, or omissions, as well as from contractual breaches of the A/E’s agreement with the owner that arise from wrongful acts during the performance of the A/E’s professional services. The operative test is whether the A/E failed to exercise “his skill and ability, his judgment and taste, reasonably and without neglect.”\(^7\)

A typical coverage clause obligates the insurer to pay all amounts in excess of the deductible up to the limit of liability which the insured becomes legally obligated to pay resulting from a wrongful act. The coverage clause defines the risks that are insured. A closer look at the clause and the policy’s exclusions helps to clarify the covered risks.

The coverage clause, by its own terms, requires a legal obligation to pay. Mere gratuities, without a corresponding legal obligation, do not result in coverage. Also, equitable remedies, which aren’t legal damages, are typically not covered.

More important is the clause’s requirement, by the definition of wrongful act, that the act, error, or omission arise out of the performance of or the failure to perform professional services. Professional services are defined, generally, as those services that the design professional is legally
qualiﬁed to perform for others as an architect, engineer, land surveyor, landscape architect, construction manager, or as deﬁned by an endorsement to the policy.

The term “professional services” has not been clearly deﬁned by case law. In Atlantic Mutual Insurance Company v. Continental National Insurance Company,72 the New Jersey Superior Court disagreed with the insurer’s argument that failure to report safety code violations of the contractor’s trenching operations was a nonprofessional act or omission. The court examined the ordinary meaning of professional services and concluded that such services involved a vocation, calling, occupation, or employment involving specialized knowledge, labor, or skill where the labor or skill is predominantly mental or intellectual rather than physical or manual.73

Other courts have concluded that supervision or administration of construction pertains to an A/E’s performance of professional services.74 However, some courts, although not addressing a professional liability policy, have held that allegations of the insured’s failure to warn and report unsafe conditions are covered acts of ordinary negligence under an A/E’s CGL policy.75

Policy Exclusions
Coverage is further limited by the standard exclusions listed in the policy. These exclusions include the following:

a) intentional or fraudulent acts;
b) failure to complete drawings or schedules on time, as well as failure to act in a timely fashion upon shop drawings;
c) faulty construction cost estimates;
d) express warranties or guaranties;
e) consulting in the area of asbestos abatement or hazardous waste;
f) professional services performed by the A/E as part of a joint venture;
g) claims made against the A/E by an enterprise wholly or partially owned by the A/E;
h) projects for which the A/E performed professional design services in conjunction with performing construction services (this would be the typical design-build project);
i) punitive damages or exemplary damages; and
j) ﬁnes or penalties.

At least one insurer, by endorsement, has removed from its policy exclusions b and c. This was done, in part, as a result of unfavorable court rulings in the interpretation of these claims.76

Coverage Limits
The policy describes the coverage limit of liability. Unlike standard occurrence liability policies, the professional liability policy has a depleting coverage limit. In other words, the policy limits are reduced by payment of judgments, settlements, or claim expenses. Claim expenses include attorney’s fees, expert costs, court costs, and other investigative expenses. Since the policy is also typically written on an annual aggregate limit of liability, all claims asserted in a particular policy term deplete the coverage limit.

Conceivably, a policy can be depleted entirely by claim expenses without any payment of claims. Once the coverage limit is reached, the insurer has no further duty to defend. This raises an ethical question of whether a lawyer engaged by the insurer to represent the insured can withdraw from the case when the coverage limit is exhausted.

Some policies include a provision that limits the insurer’s liability to the coverage limits in effect at the time of the wrongful act or the amount stated in the current policy, whichever is less.77 Such a provision is very seldom understood by the insured, and could come as a big surprise to the insured if invoked by the insurer.

Workers’ Compensation

Since the turn of the century, every state has passed legislation requiring employers to compensate their employees for work-related injuries. (Hawaii was the last state to do so, adopting a compensation statute in 1963.) The purpose of these workers’ compensation statutes is to provide monetary relief as a function of employment without regard to employer negligence. The philosophy is that injuries on the job should be borne by industry, not the by injured worker. Thus, workers injured in the course and scope of employment are entitled to receive, in addition to medical expenses, a percentage of their wages during the time they cannot work. Because these benefits are statutory entitlements, the worker does not have to prove the employer’s negligence in order to recover; on the other hand, neither can the worker sue the employer in tort for a larger recovery than the statutory benefits.78

Prime contractors are required to provide compensation for their employees, but not for independent contractors, who are excluded from the scope of workers’ compensation acts. The distinction between an employee and an independent contractor is not always easy to determine. The test largely turns on the degree to which the prime contractor or employer has the right to control the means, methods, and time of work.79 The less the right to control exists, the less likely there exists an employment relationship. However, general contractors are required to provide workers’ compensation insurance for the employees of their subcontractors, as are subcontractors, in some instances, for the employees of their sub-subcontractors.80
Scope of Coverage

All states require employers to secure workers’ compensation liability to protect against possible insolvency or bankruptcy. Various means are allowed, including self-insurance and insurance in state funds, but the prevailing method is private insurance.

Because compensation benefits are statutorily mandated, workers’ compensation insurance policies are subject to the compensation statute. Thus, even though the relationship between the employer and the insurer is governed by general insurance law, the relationship between the worker and the insurer is governed by the workers’ compensation statute. The effect is to limit the coverage defenses normally available to an insurer.

For example, fraudulent statements or material misrepresentations on applications usually provide the insurer with a defense to coverage. The same would be true if the insured failed to pay the premiums. In workers’ compensation policies, if the employer makes such fraudulent statements, or fails to pay the premiums, or incorrectly estimates the employee’s wages for premium calculation, the insurer is still obligated to pay the employee’s benefits.

An insurance company may avoid liability if it can prove that the policy was null and void at the time it was issued, but this is rare and often depends on clear and convincing evidence of particularly egregious instances of fraud. One example is where the employer obtained insurance without telling the insurer that an accident had occurred earlier in the morning on the same day.

Although the insurance company cannot generally deny benefits to the employee because of the employer’s misconduct, the insurance company may be able to defeat the employer’s claim for reimbursement of benefits, or may assert a separate claim against the employer for reimbursement of benefits paid. The converse may also be true. If the insurance company misrepresents the coverages, the employer may assert a claim for the excess premiums paid.

Workers’ compensation statutes require two types of minimum insurance coverage: full coverage and modified full coverage. Full-coverage statutes require full coverage for the full range of compensation benefits for all employees, including borrowed servants and statutory employees. Modified full-coverage statutes allow insurance companies to limit coverage to employees at specified business locations. These modified full-coverage statutes allow employers to secure their liability for less premium cost, and are particularly useful in the construction industry where the work is job-specific.

Coverage Issues

Difficult coverage questions arise in connection with successive injuries and occupational disease cases, such as asbestosis and silicosis, and are made more difficult when the employer changes carriers. One approach favored by the courts is the “last injurious exposure test,” which imposes liability under the policy in effect when the last injury causally related to the disability occurred. The rationale behind the rule is that it “apportions liability in a fundamentally equitable manner because ‘all employers will be the last employer a proportional share of the time’.”

Thus, in new injury cases, the last insurer on the risk is liable, unless the injury is not causally related to the disability. For the insurer to be liable for aggravation of an old injury, the second injury must have independently contributed to the disability. Otherwise, the injury may be deemed to be a recurrence of the old injury for which the previous employer and his insurer remain liable. The test used in occupational disease cases, though difficulties arise in determining the date of injury, is as follows:

[T]he employer during the last employment in which claimant was exposed to injurious stimuli, prior to the date upon which the claimant became aware of the fact that he was suffering from an occupational disease arising naturally out of his employment, should be liable for the full amount of the award.

CONCLUSION

You have now completed your journey through the sometimes overwhelming subject of construction insurance. Many issues will need further exploration and refinement. I hope that you’re up to the task. Beware that there are many pitfalls that you will face as you expand your knowledge on construction insurance. The interrelationship between insurance coverages are fraught with possibilities of gaps in coverage and risks that are either uninsurable, or, under certain circumstances, not insured.

As in other areas of the law, construction insurance law continues to develop and change. New risks are identified, and the insurance market assesses the need and economic feasibility to insure those additional risks. With additional risks, emerge a new body of law on the subject.

Endnotes

3. Insuring agreements date back at least 5,000 years. See 21 Encyclopedia Britannica 689 (1985).
5. Smith at 95.
6. Mowbray at 70, 272.
7. Id at 244.
9. The same would be true if the insured failed to pay the premiums. In workers’ compensation policies, if the employer makes such fraudulent statements, or fails to pay the premiums, or incorrectly estimates the employee’s wages for premium calculation, the insurer is still obligated to pay the employee’s benefits.
10. Smith at 95.
Batson-Cook Co. v Aetna Ins. Co., 692, 574 NE2d 160 (1991). For a contrary view, see Pacific Mut. Life Ins. Co., NW2d 450 (Minn 1977); Supply Co., insured for loses that one insured negligently inflicted on another United States Fire Ins. Co. v Colver, 593 (1985); formed by the drywall contractor. ages not only the electrical and mechanical work, but also work per-

395 F2d 12 (8th Cir 1968), where the policy excluded loss caused by 410 A2d 658 (1980).

St. Paul Mutual Ins. Co., Risk Form, No. IMR 3092 (June 1980). building and began litigating tort/contract responsibility for a loss. has lead to disputes that destroyed projects when the parties quit

tractor under contractual circumstances that would leave title for a

construction contracts and local law. For example, a supplier may deliver

owner, there would be a lien or other security interest in the project.

brief period with the supplier, or subject to the supplier's lien. tor, and the owner, but even if ownership vested immediately in the

showed no evidence of an occurrence within the policy period. While the policy was in effect,....
Chair's Letter

(continued from page 2)

Many activities are taking place and more help is needed. Call or write those Division chairs, listed elsewhere in this publication, who lead activities in areas of your expertise. Call or write the Governing Committee members and volunteer your time.

Participate today in the success of the Forum.

James J. Scott, Chair

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Dear Editor:

Please accept this letter as a small supplement to a top-notch and otherwise exhaustive article entitled “Sick Building Syndrome and Building-Related Illness Claims: Defining the Practical and Legal Issues,” which appeared in the October 1994 issue of your magazine. As is clear from the article, the “sick building” case often turns on a battle of experts. Two courts, following Daubert v. Merrell Dow Pharmaceuticals, Inc., 113 S Ct 2786 (1993) have held that evidence relating to multiple chemical sensitivity syndrome, while generally accepted on the talk show circuit, has no place in federal court.

In Conde v. Velsicol Chemical Corp., 24 F3d 809 (6th Cir 1994), the Sixth Circuit affirmed the trial court’s entry of summary judgment in favor of the manufacturer of a chlordane-based pesticide applied to plaintiff’s home. In Conde, the trial court excluded the medical/chemical evidence before Daubert, but the Sixth Circuit affirmed the trial court’s result since the evidence, even if admissible, was “insufficient to allow a reasonable juror to conclude that the position more likely than not is true” quoting Daubert, Daubert, 113 S Ct at 2798; Conde, 24 F3d at 813. The court found the nonmedical doctors unqualified to diagnose the alleged victims and the medical doctors unqualified to relate any diagnosis to the pesticide.

In a far-reaching and insightful opinion, Bradley v. Brown, 852 F Supp 690 (ND Ind 1994), the court threw “clinical ecology” and “multiple chemical sensitivity syndrome” evidence out unequivocally and until further notice. The court held “plaintiff’s own evidence clearly established that the ‘science’ of MCS’s etiology has not progressed from the plausible; that is, the hypothetical, to knowledge capable of assisting a fact-finder, judge, or jury.” Id. at 700. Stripped of their MCS claim, the three plaintiffs received $2,500—total—for a single exposure to an airborne Pyrtox/Kerosene mixture. Id. at 701.

It appears then that the tide has turned against admitting evidence comprising the multiple chemical sensitivity “science.”

William C. Ahrbecker
Bose McKinney & Evans
Indianapolis, Indiana

Dear Editor

The August 1994 issue of The Construction Lawyer contained an article entitled “Economic Loss Doctrine and Its Impact Upon Construction Claims.” This article advocates compensation for owners of construction projects when they receive less than that for which they contracted, whether with a developer, contractor, or design professional, and regardless of whether there was any contract between the owner and the person from whom it seeks damages. The author would permit an action in tort without regard to whether a general duty was owed to the public at large or whether there was a limited contractual duty owed only to one party or a specified group of parties.

The basis for liability is not whether harm has occurred, but whether that harm foreseeable resulted from the breach of a duty. The source and nature of that duty is critical to a reasoned analysis of the basis for liability. Parties to a contract can adjust and allocate risks by the creation of duties through agreement. Those to whom that sort of duty is not owed should not be allowed to recover for its breach. Otherwise, a party owing a contract duty becomes an insurer that future property owners will be satisfied with their bargain.

Although not cited in the August 1994 article, The Construction Lawyer has published other articles which address issues of recovery for construction defects from the perspective of who is liable for the harm rather than from the perspective of “someone’s going to pay for this.” These articles are “The Center Holds: Continuing Role of the Economic Loss Rule in Construction Litigation” by Sidney R. Barrett, Jr., and “The Economic Loss Rule: A Fair Balancing of Interests” by Luther P. House, Jr. and Hubert J. Bell, Jr. Both these articles were published in the April 1991 issue of Construction Lawyer. In addition, another article concerning the economic loss rule, which adopts Mr. Lesser’s view, was published in the November 1990 issue of Construction Lawyer. The reader should review all of these articles for a well-rounded overview of the issues.

I cannot agree that imposing tort liability on those involved in the improvement of real estate is desirable, because doing so lacks a reasoned jurisprudential foundation. There are legislative options which could be adopted, however, including a requirement that a developer furnish a bond naming purchasers as obligees to protect them from loss due to defective design or construction or by making at least first-tier purchasers intended third-party beneficiaries of contracts for design and construction. Expressly making first-tier purchasers intended third-party beneficiaries of the contract between a developer and a contractor or design professional permits the assertion of personal defenses not otherwise available in a tort action. There is no need to interfere with the current liability of the builder-vendor, since the purchaser already has recourse in contract.

Hubert J. Bell, Jr.
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PLENARY SESSION TOPICS

- Expanding the Use of Design/Build
  This introductory session will view 1) the expanding marketplace for design/build services in the public sector (federal agencies, military branches, state and local government, school and construction); 2) response in the industry; and 3) concerns of traditional design and construction firms that are restructuring to meet the market.
  Speaker will be construction industry executive from a firm engaged in the design/build market.

- How the Design/Build Process Addresses the Owner's Concerns
  A panel of public owners expresses their views concerning singular responsibility, reduced administrative burdens, risk allocation, early estimating of construction costs and quality. This session also overviews successful design/build projects.
  Speakers from the American Public Works Association and West Coast Public Entities

- The Industry Response to Design/Build
  A panel discussion of representatives from AIA, AGC, DBIA, ASCE, NSPE and ACEC; and highlights of association activities and positions in connection with a growing demand for design/build services.

- Nuts and Bolts of the Design Process
  This session will provide a practical explanation of the design/build process using a federal project-specific example.

- Legislative and Case Law Developments Affecting the Use of Design/Build on Public Projects
  This session will provide an overview of current 1) enabling legislation, 2) model legislation, 3) licensing laws, and 4) cases.
  Speakers from the Building Futures Council

- Risk Allocation Between Design/Build Team Members
  Panel discussion to identify the basic risks and suggest allocation. For example, allocating risk to a professional service firm.

- Drafting Contracts to Implement the Process
  Panel discussion examines 1) industry forms and government contracts; and 2) joint venture agreements; and will provide useful forms and clauses.
  Speakers from the Contracts Committee

- Procurement Protests
  The Process and Basic Rules and Protests are examined in the Design/Build context.

WORKSHOPS AND CUE TOPICS

- The Procurement and Selection Process
  The explanation of selection methods such as competitive negotiation.

- The Role of an Independent Owner’s Representative
  An analysis of the reasons for an independent representative and an overview of activities. This workshop will also cover the role of the program manager and CM. Examples of contracts will be provided.

- Bonding and Insurance
  Examine trends in project wrap-up insurance and workers’ compensation resolution panels. Examine the basics regarding professional liability coverages and bonding in the design/build context.

- Site Safety and the Design/Build Process
  An update of current safety legislation and cases. Examine the design/builders' safety responsibility.

- International
  Overview of the use of design/build and other delivery systems in Asia.

- Environmental Issues
  Overview of the use of design/build and other delivery systems on federal cleanup projects.

- Dispute Resolution within the Design/Build Team
  Examine the use of mediation and suggest the contractual provisions to implement resolution procedures.

- Recent Developments in Environmental Cleanup Technology Protection

- The Consequences of Ignoring State Licensing Laws

- To What Extent Should Design Be Completed Prior to a Fixed Price?

- Criminal Prosecution for False Certification of Claims

For more information, call for the Forum’s Construction Industry FAX Catalogue at 800/636-7867.