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The New Frontier: Liability and Coverage Issues Facing 21st Century Design Professionals

The roles and exposures of design professionals continue to morph and change with the development of new technologies and new or reimagined delivery systems. Design professionals as well as their insurers, brokers, and attorneys are all being asked to take a fresh look at different risks in the 21st century and how those risks can be better anticipated, managed, and controlled.

I. Design-Build

Design-build is a common project delivery method in today's construction industry where a single entity undertakes responsibility to an owner/developer for providing comprehensive design and construction services. Unlike traditional design-bid-build methodology where an owner/developer will retain the design professional to design a project and a contractor to build it, design-build contemplates the retention of either a design professional or a contractor to both design and build the project. Design-build has gained popularity as owners/developers recognize the benefits of having a single point of responsibility to look to for delivery of the finished project. When it works right, design-build should also be faster and less expensive.

A. History of Design-Build

If you research design-build, you will learn that the ancient master builders of the Parthenon (432 B.C.), the Royal Abbey Church near Paris (12th century), and the Florence Cathedral Dome (15th century), all had responsibility for both design and construction. Design-build aficionados may even assert that a singular responsibility for design and construction was codified as far back as Hammurabi's Code (1750 B.C.) and then again by the Roman writer and designer Vitruvius in the first design handbook (40 B.C.). *See*, Design-Build: Planning Through Development, Jeffrey Beard, Michael Loulakis, Esq., and Edward Wundram (2001).

More recent history reveals that the separation of the responsibilities for design and construction occurred during the Industrial Revolution due, at least in part, to the complexity of industrial facilities, the need for specialization and expertise in design, and the ability and need for one design to be used in multiple locations. The largely

intellectual process of design and the physical nature of construction allowed for relatively easy separation of design from the construction industry. Professional societies such as the AIA and ASCE formed and reinforced the separation of designers and builders. *Id.*

Ironically, it can be argued that the ever more technically demanding nature of 21st century structures and building systems and the related need for more coordination of effort between designers and builders is one of the primary reasons for the reunion of the design and build functions. Owners looking for a coordinated, cost-effective, and time-efficient delivery method once again sought a single source of responsibility.

While there was resistance to this "new" delivery method, particularly from the government sector, design-build projects—although not necessarily using that nomenclature—began to appear in earnest in the early 1980s. The AIA introduced its first Design-Build forms in 1985. The Design-Build Institute of America (DBIA) was founded in 1993 and has been promoting and supporting design-build as a project delivery method for over 20 years. Legislation authorizing design-build in public projects peaked in 2009 cementing the role of the delivery method across all sectors.

A 2014 study prepared for DBIA showed that the design-build delivery method represented 40% of the non-residential U.S. construction market, a 10% increase over 2005. The same study showed that the number of traditional design-bid-build delivery projects decreased 14%. Design-build became used heavily in the military sector with more than 80% of those projects employing design-build. Commercial building construction and medical buildings became the second and third largest market segments using design-build. Design-build is also the preferred delivery method for projects over $10 million being used in over half of such projects but, conversely, it is used in only a quarter of the non-residential projects less than $10 million. *See*, "Design-Build Project Delivery Market Share and Market Size Report," Reed Construction Data/RSMeans Consulting for DBIA, May 2014.

The DBIA study confirms that design-build continues to grow in popularity as a delivery method for the biggest and most technical projects. This only increases the importance of understanding and managing the risks associated with design-build for design professionals.

B. Designer-Led or Contractor-Led Design-Build?

There are two common types of design-build arrangements—contractor-led design-build or designer-led design-build. Each of these arrangements requires the design-builder to subcontract for the services which the lead cannot provide. A contractor-led design-builder will be required to retain a design professional or design team to provide the design and construction documents for the project. Likewise, a designer-led design-builder must retain a contractor to construct the project.

While the early trend was for contractor-led design-build, designers—particularly architects—were loath to relinquish their role as first to advise and contract with the owner. Architects had to be convinced that they should consider accepting risk which they had so studiously avoided for a century or more but maintaining control of the design led many designers to pursue designer-led design-build projects. Articles were written by both architects and lawyers encouraging designers to consider designer-led design-build and touting the advantages of the delivery system when led by a designer. *See e.g.*, "The Hopes and Fears of Design-Build," Solomon, AIA, *Architectural Record* (Nov. 2005); "Designer-Led Design-Build," Friedlander, Esq., *Masonry Design Magazine* (May/June 2008). However, contractor-led design-build has maintained its prominence and is becoming even more frequently used in some sectors such as infrastructure projects.

In addition to formats with the contractor or designer as the prime, DBIA also recognizes a joint venture between contractor and designer to create a single purpose design-build entity, a design-build entity comprised of multiple construction contractors for large contract value situations, and developer-led design-build. DBIA issued a position statement in 2010 recognizing all of these organizational forms as appropriate for design-build as long as a single entity holds the contract with the owner, the entity is responsible for both design and construction and the entity has the financial and managerial resources to perform the design-build contract, and risk for both design and construction is appropriately assigned to the party best able to manage, price, or insure the risk. *See*, DBIA Position Statement: Organization of the Design-Build Entity (2010). Whatever form the design-build entity may take, design professionals must evaluate the increased risks from being the single point of responsibility as the design-builder or ceding at least some portion of its control over the design to the design-build entity with which it contracts.

II. Design-Build Risk Mitigation

Both contractor-led and designer-led design-build arrangements present additional risks to the design professional which can and should be managed through contractual protections and risk transference. When the architect or engineer undertakes the role of design-builder, it is assuming responsibility for design, project management, supervision, and construction of the project. With that comes the responsibility for safety in the execution of the work and the use of proper and safe means, methods, techniques and sequences of construction, responsibilities which the design professional does not typically undertake in a traditional design-bid-build delivery method.

A. Contract Drafting

Although the risks to the architect or engineer are greater when in the role of the design-builder, in either scenario the importance of good contract drafting cannot be overstated. The design-build method of project delivery is fraught with potential tensions between the contractor and designer. For example, architects and engineers

place a high value on the quality of design, long term performance of the project, and operating costs to an owner, whereas the contractor may be focused on the economics of the project and a desire to meet a minimum standard of design. Some of these tensions can be managed by contract language and others can be managed through proper insurance.

For contractor-led design-build projects, the designer is in effect a subcontractor to the design-builder. The owner/design-builder agreement will typically contain provisions relating to indemnification, insurance requirements, ownership of documents, dispute resolution, and liability for various types of damages. The subcontract agreement will likely contain language which makes these provisions "flow down" to the design professional so that the designer is bound to the design-builder in the same manner and to the same extent that the design-builder is bound to the owner. It is recommended that the design professional insist on review and input into the terms of the design-build agreement to be sure that there is fair and proper protection in place, the designer can insure the professional obligations it is assuming, and the designer is being paid a fair and reasonable fee for the services and the risks it is undertaking.

The following is a sample indemnification clause to consider in a contractor-led design-build agreement with a design professional:

> The Design-Builder shall be solely responsible for all cost estimating, quantity surveys or other predictions of expected project cost. The Design-Builder shall verify quantities or other information furnished by the Design Professional and shall use its knowledge and experience as a construction professional in developing its bid and pricing for the work, and shall include in such bid an appropriate degree of contingency for additional cost resulting from the post-award design development and finalization process. The Design Professional shall not be responsible for project costs, direct, indirect or consequential, that result from the design development and finalization process.

B. Contract Administration

Of particular concern with contractor-led design-build is the designer's contract administration services. In a typical design-bid-build project, the design professional typically provides a full range of contract administration services, such as periodic site visits, rejection of non-conforming work, responding to requests for information, review and certification of pay application, and review and approval of submittals, all of which provide a check and balance system to the owner that the architect's design is being properly carried out in accordance with the approved construction documents by the owner's contractor. The same check and balance system typically does not exist in a contractor-led design-build project. The design-builder may reduce or eliminate some or all of contract administration services because it does not want to pay for those services. The ability of the design professional to observe construction quality and non-conforming work is hindered, and the potential for owner claims on the project increases. Further, the

design-builder may assume the design intent of the construction documents instead of issuing a request for information to clarify such intent, which may led to deviations from the construction documents. To protect the designer from potential claims made against the design-builder being passed through to it, the design professional may find it desirable to insist providing contract administration services as an added protection to itself and the owner.

C. Insurance Coverage

Another way to manage risk on a design-build project is to shift the risk to others by way of insurance. The most common types of insurance required for design professionals on design-build projects are commercial general liability, auto liability, workers compensation/employers liability, umbrella/excess insurance and professional liability insurance. Care should be taken to make sure that the policy limits, particularly the professional liability limits, are sufficient for the project undertaking since design-build projects are frequently higher cost projects. Since professional liability insurance is written on a claims made basis, in the event of a change in firms or organizational structure, the design professional needs to be sure maintain the coverage for a period of time after the project has been completed to protect itself from claims made or discovered after project turnover. It is suggested that the design professional also require the design-builder to name it as an additional insured on the design-builder's general liability insurance policy so that it will be covered for non-professional risks through the design-builder's insurance.

Unlike general liability insurance, no additional insureds are permitted to be added to a professional liability policy including any joint venture that may be created to pursue a project. The design professional should make sure that a contractor in a design-builder role obtains its own professional liability coverage as part of its insurance program. In addition, it is recommended that the design professional review all of the design-builder's insurance requirements to verify that the design-builder is properly and adequately insured for the project. In the event the design-builder is not insured for a loss, it will no doubt be looking to the design professional and its insurance to indemnify the owner for such loss. Indemnification provisions should be carefully drafted to maximize the insurability of the provision for the design professional and to make sure that the indemnification provision does not transfer liability to the design professional for damages it would not otherwise be legally liable to pay in the absence of the indemnification provision. Indemnifications running in favor of design-builder's subcontractors, other consultants, and suppliers should be avoided.

In the design-build arena, best practices require careful contract drafting and a clear understanding of insurance coverages available to protect the design professional. It is prudent to send the insurance requirements for both the contractor and designer for design-build projects to the design professional's insurance agent for review and comment. The insurance agent can prove to be an invaluable resource for managing risks of design professionals on design-build projects.

III. Other 21st Century Risks

Design professionals and their insurers may be feeling that the biggest risk in the 21st century is the attempt to make the design professional responsible for everything. Some examples are finding the designer responsible for financial forecasting or ignoring a defense or absolute bar "in the best interest of the public." There are some specific risks arising from advances in the 21st century construction environment.

A. Cyber Liability

As news reports show, cyber exposure is real and can be devastating. All professional liability insureds, including design professionals, should explore the purchase of a comprehensive privacy and security policy to provide coverage for cyber liability. The exposure is heightened in design-build projects and/or where building information modeling (BIM) is used as electronic document sharing between offices and companies can increase the likelihood of a data breach.

B. Building Information Modeling

BIM is a process involving the generation and management of digital representations of physical and functional characteristics of places. With BIM technology, one or more accurate virtual models of a building are constructed digitally. Building information models support design through its phases, allowing better analysis and control than manual processes. The exchanged information maybe in proprietary formats and contain proprietary data. BIM brings its own unique risks. Some considerations for minimizing the risks created when BIM is part of a project are:

1. Set Expectations

2. Organization, hosting, and administration of the Building Information Models – who is responsible?
   a. Who, how and where for Design Team?
   b. Who, how and where for Build Team?
   c. Who, how and where for Owner's management after construction?
   d. Use Agreements to assist in setting expectations
   e. Digital Data Transfer Agreement and BIM execution plan

3. AIA C106-2013 digital Date Licensing Agreement is used in situations where there is a need to send digital data to someone for that person's use on a design or a project and there existing agreement with that person to cover the use of the data.

4. E203-2013 Building Information Modeling and Digital Data Exhibit. Not a stand-alone – must be attached to an existing agreement such as the AIA

B101-2007 Agreement Between Owner & Architect or the A101-2007 – Agreement between Owner and Contractor.

5. Sample BIM disclaimer

> Any uses of graphical depictions derived from Architect's 3-D model data contained in this model, just as traditional two-dimensional design drawings, are issued to facilitate construction by expressing the intent of the designer and do not serve as instructions for construction sequences, ways, and means to the Owner, Contractor, or Subcontractor. Recipients of this 3-D model acknowledge this 3-D model data does not contain all details, components, and information necessary for complete installation, nor does it likely represent the only solution to meet the requirements in some areas. Recipients acknowledge and agree that others, not the Architect are solely responsible for construction installation sequencing and construction means and methods.

IV. New Coverage Options for Design Professionals

As discussed above, there are new risks for design professionals and new coverage options available to address those risks. In addition to cyber and tech coverages, there are additional coverages which may be available, often by endorsement to an existing professional liability policy. Some examples of recently developed endorsements are:

Product Exclusion Exception Endorsement

L. PRODUCTS - The design, manufacture, sale, supply or distribution of any goods or products by any Insured, any subsidiary or any entity which wholly or partly owns, operates, or manages the Insured or any subsidiary of such entity, or by any person or entity under license from the Insured;

1. Except this exclusion does not apply to:

   a. Computer programs or software created or modified specifically for a client in connection with Professional Services performed by the Insured for that client; or

   b. To the design of goods or products which are specifically designed by the Insured and produced for one particular project.

Crisis 360

Provides coverage for PR and crisis management services for catastrophic events that make the national news. Coverage includes PR assistance, hospital and funeral expense assistance.

1. Crisis ThreeSixty. The Company will advance Crisis ThreeSixty Costs directly to third parties on behalf of the Named Insured, regardless of fault, arising from a Crisis Management Event first commencing during the Policy Period, up to the amount of the Crisis ThreeSixty Limit of Insurance.

2. Specialty Casualty Fund. The Company will pay Crisis Management Loss on behalf of the Named Insured arising from a Crisis Management Event first commencing during the Policy Period, up to the amount of the Specialty Casualty Fund Limit of Insurance.

Rectification Coverage

The Insurer will reimburse the Insured for Rectification Costs in excess of the Rectification Retained Amount reasonably and necessarily incurred by the Insured to redesign and/or remediate a Design Defect that would otherwise lead to a Claim covered under the policy. All of the following conditions must be met in order for Rectification Cost reimbursement to apply:

a. the Design Defect must be caused by or result from Professional Services rendered by the Insured on or after the Retroactive Date specified in Item 3. of the Declarations and prior to the end of the Policy Period specified in Item 2. of the Declarations; and

b. the Design Defect must first be discovered during the Policy Period and prior to the earliest of either:

   I. the issuance of a certificate of substantial completion, or

   II. the date that the constructed project has been put to its intended use by any person other than a contractor or subcontractor; and

c. prior to incurring or committing to incur any Rectification Costs the Insured must provide written notice to the Company during the Policy Period, but in no event later than fifteen (15) calendar days after the end of the Policy Period; and

d. the written notice provided to the Company must include the proposed corrective action and supporting documentation that the Design Defect could result in a Claim being made against the Insured.

The market will continue to adapt to the changing risks impacting the design profession in the 21st century. Design professionals and their brokers and attorneys must continue to inform and work with their insurers to manage these new challenges.