Non-Traditional Insurance Risks for Non-Traditional Project Delivery Methods

Non-traditional project delivery methods are being increasingly used in construction projects, and these delivery methods can bring non-traditional insurance risks. Non-traditional project delivery methods may require project participants, such as designers, contractors and owners, to hold additional types of insurance to guard against risks that their typical insurance does not cover.

Insurance that is commonly required on a construction project is commercial general liability ("CGL"), builder's risk, and professional liability. CGL insures against injury to third parties and damage to property of third parties. Builder's risk insures against injury to the property or building being constructed. Professional liability, which is commonly referred to as errors and omissions insurance, insures against professional malpractice. In a design-bid-build setting, generally a contractor holds general liability and builder’s risk insurance, and a designer holds professional liability insurance.

Project participants must be vigilant about the limits of their insurance coverage on non-traditional project delivery methods. Under non-traditional project delivery methods, project participants can face more liability because their job duties are expanded and often overlap as opposed to the separated job duties under the design-bid-build method. Each project participant should thoroughly examine the conditions, terms, and exclusions of their insurance policy; know the claim notification procedures; and confirm the policy complies with the project requirements. The remainder of this article will discuss common insurance concerns for design-build, integrated project delivery, and public-private partnerships.

Design-Build

Under the design-build method, the owner contracts with a single design-build entity that conducts both the design and construction services. A design-build project may be performed by a joint venture between a contractor and designer, by a contractor that subcontracts with a designer to design the project, or by a designer that subcontracts with a contractor to build the project.

Under the first two scenarios, a contractor is primarily responsible and can assume design liability that is normally limited to the designer under the typical design-bid-build method. A contractor’s CGL policy may cover some claims related to the design, such as bodily injury or property damage. But, the contractor’s general liability insurance does not cover design services performed in-house or economic losses, such as design defects or claims for cost overruns by the owner. A contractor should not rely on the designer’s professional liability coverage because these policies frequently do not cover claims arising from activities of related controlled entities; for example, a designer that is affiliated with a contractor. A contractor taking on the additional risk of design liability should obtain additional coverage, such as the design-builder rider, the errors and omissions rider, or the contractor’s protective professional indemnity policy.

A contractor’s protective professional indemnity insurance can provide coverage for design services that are self-performed or subcontracted to a designer. In addition, the protective professional insurance may include “differences in conditions” coverage, which provides coverage for the differences in insurance provisions between the designer’s professional liability policy and the contractor’s professional liability policy. A contractor may acquire the protective professional insurance on individual projects or as a blanket coverage for all projects. A contractor should also obtain its own professional liability policy to guard against potential insurance lapses in its subcontractor’s professional liability policy.

If an owner contracts directly with a designer, who then contracts with the contractor, the designer is primarily responsible and may take on liability that is usually limited to the contractor under the design-bid-build method. Under this method, the designer is responsible to the owner for the design and construction, but a designer’s professional liability insurance only covers design errors or professional negligence. The designer takes on extra risk because the designer’s professional liability insurance does not cover the contractor’s workmanship or construction “means and methods.” Accordingly, designers that lead a design-build project are likely to have fewer insurable claims. In light of these additional risks, a designer should require the contractor on a design-build
project to insure their own risk by carrying contractor’s professional liability insurance.

An owner should require the design-builder to provide all insurance, such as a design professional project policy that includes an extended discovery period. The benefit of a project policy is that it reserves coverage for that specific project so other claims will not limit the coverage and the coverage will not be subject to cancellation at project completion.

**Integrated Project Delivery**

Integrated project delivery is a collaborative method where major project participants share the risk and rewards of construction. The project participants work together early in the construction process to identify project issues, conflicts, establish performance guidelines, and scope of work. One of the main insurance problems caused by integrated project delivery is that job duties overlap.

Similar to design-build, a contractor involved in integrated project delivery may need to guard against design errors by obtaining errors and omissions coverage.

Due to the widespread collaboration under the integrated project delivery method, project participants may want to obtain a specially written insurance policy. A specially written policy may cover errors and omissions, third-party claims, first-party claims, and both direct damages and economic loss caused by a design deficiency. Under these policies, the insurer may require each project participant to inform the insurer if the party discovers an error prior to conducting any remedial work.

**Public-Private Partnership (“P3”)**

The public-private partnership (“P3”) method allows a private entity to be more involved in a public project by designing, financing, constructing, and controlling the long-term operation and maintenance of the public project. A P3 usually exists on a large construction project that will have a revenue stream because the private entity will frequently operate and maintain the project and receive the revenue as a reimbursement for financing the project. Accordingly, a P3 will have specific insurance needs for each project participant. Similar to the integrated project delivery method, P3s may require specially written insurance policies.

On a P3, the private entity has many of the same insurance risk considerations as under the design-build or integrated project delivery methods, but the private entity usually also needs to obtain insurance for the long-term operational phase of construction. The added risks of a long-term P3 project can create significantly different and greater risks than under a traditional project delivery method. Due to the long-term nature, project participants may even want to obtain directors’ and officers’ liability insurance to guard against the adverse impact of a directors’ or officers’ act or omission, or political risk insurance to guard against political or war risks.

A private entity on a P3 may also want to enhance its insurance with rectification coverage, which covers the entire design and construction team, and insures against the cost of remedying a design defect that is identified during construction.

**Conclusion**

Non-traditional project delivery methods can create non-traditional insurance risks that project participants are normally not accustomed to under the design-bid-build method. To guard against these additional risks, project participants should review their existing insurance policy, determine if any coverage gaps exist, and consider obtaining additional insurance coverage.