

CLIENT ADVISORY

PROTECTION FOR PROJECT OWNERS AND DEVELOPERS: WHICH POLICIES WORK BEST?

Condo Builder, Inc. is to build a residential development of 50 condos on a parcel of land that has been acquired by Condo Builder's newly formed subsidiary, Haven Hills, LLC. As the project owner, Haven Hills will contract directly with Quality Contractors, Inc., an unrelated general contractor, to perform all construction work. At this point, the owners of Condo Builder begin to think about liability insurance to protect Haven Hills as the project owner. Which coverage works best for Haven Hills?

Additional Insured Protection – General Contractor's CGL Policy

In the past, Condo Builder had not purchased liability insurance for the project owner, but instead had relied solely upon the owner's status as an additional insured on the general contractor's CGL policy. After all, the general contractor is in control of the construction site – so how could the owner be liable?

Unfortunately, Condo Builder learned some hard lessons on their last project – the Garden Estates project – whose owner was Garden Estates, LLC.

Garden Estates was found negligent for failing to warn the general contractor of an old well located on the property. Apparently, an employee of the general contractor was injured when he fell into the concealed well. As the general contractor, Quality Contractors did not cause, even in part, the injury to their employee; the CGL insurer for Quality Contractors denied payment of damages on behalf of Garden Estates as an additional insured.

A further surprise to Garden Estates was that the hold harmless and indemnity agreement that was executed in favor of Garden Estates by Quality Contractors was not enforceable under the state's law that *prohibited indemnification of the negligence of another in a construction contract*. Many states have similar restrictions. Please see the attached state-by-state analysis.

This uninsured loss hammered home the point to the owners of Condo Builder – *relying on additional insured status and hold harmless and indemnity agreements was not enough to protect the project owner*.

An OCP Policy – Purchased by the General Contractor

Condo Builder then considers an owners and contractors protective liability coverage form (OCP) that the general contractor had offered to purchase on behalf of Haven Hills. Based on the Garden Estates fiasco, Condo Builder is skeptical. Condo Builder wants to get it right this time and, unlike in the past, seeks the advice of their insurance broker on the matter.

OCP Limitations

Condo Builder's broker actively discourages Condo Builder from relying *solely* on the OCP policy to protect Haven Hills. Even though there are some distinct advantages to an OCP policy when compared to being an additional insured on the policy of others, the broker points out an OCP policy is generally intended to protect the named insured owner from the *negligence of the contractor*.

Coverage for the *negligence of the owner* is severely restricted in the OCP – coverage applies to the acts or omissions of the named insured owner only if such acts or omissions are in connection with the general supervision of the contractor's operations. As the Garden Estates claim was not related to the **general supervision** of the general contractor's work, Condo Builder begins to realize the OCP will leave them just as exposed, if not more so, than they were in the past.

The discussion brings out other major coverage issues:

- A couple of years ago Condo Builder had a nasty incident in which a homeowner was injured when her deck collapsed. Because of the seriousness of her injuries, the owner and contractor were both sued. It was disconcerting to learn the OCP would not cover such a claim – *the policy excludes the products completed operations hazard*, so any injury or damage that takes place after the work is finished is *not covered by an OCP*.
- As a condition of approval, Haven Hills agreed to perform some off-site improvements for the town – and has executed a hold harmless and indemnity agreement in favor of the town for the work done. The OCP does not include coverage for the liability of third parties assumed by Haven for work done for them.
- A group of neighbors is outraged at the size and scope of the development and have publicly threatened to block any construction. If Haven Hills has the neighbors escorted off their premises and the neighbors sue for false arrest, Haven Hills has no coverage for such allegations, as the OCP does not provide personal and advertising injury coverage.

The Solution: Owner's Interest Liability – Project Specific CGL Insurance

It is now abundantly clear to Condo Builder that neither an OCP policy nor additional insured status on the general contractor's CGL policy provides them with sufficient protection. Their broker recommends a project specific, customized CGL policy, often referred to as an "Owner's Interest" policy.

While more costly than the OCP policy, Condo Builder sees the policy's substantial difference in coverage, and thus value; the owner will now have appropriate coverage for the Haven Hills project.

Owner's Interest – Extended Completed Operations Coverage

One unique feature that is often available on the Owner's Interest policy is the extended completed operations coverage – an endorsement that extends products-completed operations coverage to protect the owner for products-completed operations claims that take place *after* the project is completed and *after* the *policy expires*. The extended completed operations coverage lengthens the period of coverage for completed operations for several years *after project completion*, often matching the state's statute of repose timeframe for suits against the owner for completed work.

Why shouldn't Haven Hills rely on the contractor's completed operations coverage? There are many reasons. The contractor's limits and coverages may be inadequate for Haven Hills' needs. Haven Hills may well lose their additional insured status after the project is completed and the contractor's policy renews. And, contractors go out of business. When they do, their insurance programs expire, leaving their past clients with no protection for the contractors' completed operations exposures.

The Owner's Interest policy with extended completed operations insurance can close these potential gaps, and could possibly provide one-time, cradle-to-grave coverage for the owner's exposures on the project.

"Mini" Wrap-Up Policy

Once Quality Contractors, Inc. hears about Condo Builder's Owner's Interest CGL policy, they want to be included. In some circumstances, the insurer providing the Owner's Interest CGL will include as a named insured the general contractor, creating a "mini" wrap-up CGL policy that protects both the owner and

general contractor, including the extended completed operations coverage to protect both the project owner and general contractor. This is often a very cost-effective solution for both parties.

Conclusion

A realistic evaluation of the risk that confronts project owners during and after construction indicates most owners are exposed to considerable liability. The ownership of property (including the ownership of buildings undergoing renovation) and construction work completed by contractors are two obvious examples.

While it is true that much of the risk is with the contractors, it is a mistake to conclude the owner has no potential for liability. While obtaining the status of additional insured on the contractor's CGL policy or requiring the contractor to provide an OCP policy helps protect the owner, such coverage is quite limited and should not be the only liability coverage available to the owner. Owners of construction projects should have their own liability coverage. The Owner's Interest CGL policy is the best way to close the gaps in the owner's liability insurance program and assure more adequate protection.

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