

# Claims<sup>®</sup>

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# DEFENDING CONSTRUCTION DEFECT CLAIMS

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**T**he easiest way to avoid liability for construction defect claims is by preventing them altogether. However, since prevention of a claim is not always possible, it is important that adjusters take early steps upon receipt of a new construction defect claim in order to limit liability and ensure the most efficient expenditure of defense costs.

## When does liability arise?

A construction defect generally occurs when a construction project either fails to conform to contractual requirements and specifications, or fails to comply with generally accepted principles governing the industry standards, resulting in damages. Whether your insured is an architect, builder or contractor, they can generally be held liable for negligence for failure to perform their duties consistent with the generally expected degree of competence that a reasonably skilled professional would exercise under similar conditions. Some of the common construction defect theories of liability include:

- **Quality of work issues**

One of the driving forces behind construction defect claims are defects attributed to poor workmanship or quality of work. Whether your insured is a design professional, developer or subcontractor, a requisite expertise and standard of care set the minimum threshold requirements for the work performed. Construction defect claims are often categorized as being either patent (obvious or reasonable discovery) or latent (concealed). Latent defects may exist during construction, but are not discovered or identified until several years following its completion. These defects can include differential settlement due to improper soil compaction resulting in cracks to foundational structures



and walls, water penetration due to improper flashing and installation of exterior windows, or even catastrophic fire damage due to faulty electrical wiring.

While not all latent defects create an immediate threat of emergency, as time lapses, a particular defect could pose a risk of substantial harm. Note, it will be important to know your jurisdiction's statute of limitations and statute of repose for patent defects, as well as any tolling provisions related to latent defects to determine whether the claims are timely.

- **Code violations**

In addition to the reasonable and professional standards of care that govern work performed on a construction site, there are also local and national building codes and safety standards imposed by law that must be followed. Failure to comply with the codes or standards can result in a claim for defective design or defective construction. For example, in cases in which an architect incorrectly calculates the requisite number of vents to be installed per square foot in an attic, that is a per se construction defect, regardless of whether or not there is evidence of deterioration to the existing roof components.

- **Scope of work violations**

Whether your insured is working on a new residential home, commercial development or a home renovation, every construction project is typically undertaken according to project

specifications that provide instruction on what to build, how to build it and the specific quality of materials to be used. Such plans are often prepared by architects, engineers, developers, contractors and subcontractors, each of which have different scopes of work. Claims can therefore arise if a party overextends its work scope or fails to comply with the terms of their work contract.

### Practical tips for defending construction defect claims

Construction defect claims seldom offer obvious evidence of liability. It is paramount to have an in-depth knowledge and understanding of all concepts to be investigated. However, before any analysis of the merits of the claim is performed by an adjuster, it is important to ensure that several key steps are taken. Gathering information on each of these checklist items will ensure that liability and defense costs associated with a construction defect claim are managed appropriately:

#### 1. Information Gathering

Start with some basics, as information takes time to collect and the other side could want the construction defect claim to move quickly:

- Any and all correspondences, contracts, subcontracts, invoices, plans, drawings, change orders and photographs from the beginning to the end of the project.

- Identify all current and former employees who worked on the subject project, including identifying their scope of work.
- Establish a main contact person for your insured, preferably one who knows the information you will need without needing to reference documents, call other people, etc.

#### 2. Identify the scope of work for the insured

The correspondences, contracts, subcontracts, invoices, plans, drawings, change orders and photographs collected in the above checklist item will be the primary documents governing the applicable scope of work for the insured. However, once the documents are obtained, look beyond the plain language of the contracts to determine the specific physical areas within the project in which the insured worked to determine if this was beyond the scope of work or within the confines of the agreements between the parties.

#### 3. Identify the scope of work for other parties involved

Often overlooked when a construction defect claim comes in is performing a detailed analysis of the scope of work for parties that are not the insured. However, understanding the scope of work of other parties involved in the project will enable you to determine who was acting within their proper scope and who was not. Doing so will help determine who may have additional liability or complete liability other than your insured, as well as who else should be at the table to share in defense costs for the claim.

An additional tip is to request proof of a contractor's license or architect's license, as well as proof of good standing as a business to ensure that the parties were licensed to perform the work that they ultimately undertook on the project. There may be liability issues for other parties related to performance of work for which they are not licensed, which opens up other avenues for filing cross claims to reduce the liability of your insured.

#### 4. Duty to defend and indemnity considerations

In addition to reviewing job contracts to determine factual and scope of work issues, the contract should be scrutinized to determine if the language requires the insured to indemnify or defend other parties on the project.

Further, the insurance policies applicable to the claim may have terms under which the insured is named as an additional insured on another party's insurance policy (or vice versa). What other policies does your insured have for the project? Do any of them have time on the risk provisions? Do any of the policies have indemnity or duty to defend clauses? Answering all of these questions from the outset are important, as they affect not only the defense of the claim, but also any resolution of the claim.

#### 5. Issue Reservation of Rights correspondence

Initial investigation may ultimately lead to the conclusion that there is no coverage under the policy. When initially agreeing to accept the tender of a new claim, it is important for the adjuster to advise the insured that such acceptance is subject to a reservation of rights to withdraw acceptance of the defense based upon newly discovered facts that result in a change of analysis.

## One of the driving forces behind construction defect claims are defects attributed to poor workmanship or quality of work.

### Considerations for retaining expert witnesses

Construction defect litigation can be rather complex and is heavily driven by expert testimony. Thus, it is critical to have a competent expert witness who can serve as an independent party tasked with the role of determining whether a claimed defect can actually be attributed to the insured. The expert must also be able to clearly explain complex issues in a manner that can be understood.

Thus, it is important to not only identify an expert with relevant experience concerning the alleged defect at issue, but also one who possesses specialized expertise in the matter, as courts may exclude those experts who do not. For example, while a licensed professional engineer may offer a general opinion as to why they observed foundational cracks in garage flooring, a geotechnical engineer will have the requisite expertise to determine if those cracks were causally related to differential settlement as a result of defective soil compaction during construction.

Depending on local evidentiary rules, consideration should be given to retaining a consulting expert (as opposed to a testifying expert). A testifying expert is required to divulge opinions in accordance and compliance with expert discovery rules. However, in some instances, a consulting expert may be able to opine as to whether allegations have merit and allow the adjuster to evaluate liability without fear of opinions being discovered through discovery.

Alternatively, if consulting experts are treated the same as testifying experts, a thorough evaluation should be performed on a case-by-case basis prior to deciding whether to proceed with expert retention. An effective expert can be the difference in a jury's ability to agree with your theory of liability and return a verdict in your favor. 🍷

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