CONSTRUCTION RISK MANAGEMENT REPORTER

ERNSTROM & DRESTE LLP

ContrACT

WINTER 2018 ISSUE 22

AIA A201 Updates: New Risks and a Few Rewards

TIMOTHY BOLDT

The vigilant contract risk manager will closely scrutinize the American Institute of Architects' 2017 update to its A201 General Conditions. With the sunsetting of the 2007 A201 in October, 2018, the time is now to understand both the improvements to this foundational industry standard form, but more critically the new risks to be managed.

The New Insurance and Bonding Exhibit A

Insurance and bonding terms previously found in Section 11 of the A201 have been significantly expanded and are now primarily located in a seven-page Exhibit A to the A101-2017 Owner/Contractor Fixed Sum Agreement and alternative agreements. The new Exhibit A presents parties with greater flexibility to establish bond and insurance programs and may help reduce the need for extensive supplemental insurance and bonding terms.

Also new is a section that prohibits contractors from using Commercial General Liability (CGL) policies with exclusions or restrictions of coverage for certain risks including:

- Claims by one insured against another insured
- Claims for bodily injury other than to employees of the insured

CONTINUED ON PAGE 2

When the Additional Insured Causes the Loss

KEVIN PEARTREE

Every day, owners, contractors, subcontractors, their respective lawyers, and insurance consultants transact contract language that seems so common place they may think they know the full scope of its meaning. But real life facts can test the meaning of seemingly ordinary contract terms, and what once seemed clear is no longer. What do the words "*caused, in whole or in part, by*" mean in the context of additional insured coverage? Should a project owner enjoy additional insured coverage on a contractor's CGL policy when the owner itself was arguably the true cause of a loss? Even the judges of New York's highest court could not all agree on the meaning of those words and the standard to be used applying this policy language.[1]

Breaking Solutions supplied concrete-breaking excavation machines and personnel for a subway construction project for the New York City Transit Authority (NYCTA) and the Metropolitan Transit Authority (MTA). Breaking Solutions was required to name the NYCTA, MTA, and the City of New York as additional insureds, via the latest ISO Form 20 10 additional insured endorsement or equivalent. When Breaking Solutions' excavator struck an energized electrical cable buried below the concrete, an explosion occurred injuring a NYCTA employee. A personal injury lawsuit followed, involving all parties.

The City, NYCTA, and MTA each sought defense and indemnification as named additional insureds under the policy issued for Breaking Solutions by its carrier, Burlington Insurance Company. Burlington provided the defense subject to a reservation of rights on the issue of whether the explosion and injuries were caused by Breaking Solutions' acts or omissions. The additional insured endorsement provided coverage only to the extent that the additional insured's liability was "*caused, in whole or in part, by*" the acts or omissions of Breaking Solutions or those acting for it. Discovery showed that while Breaking Solutions' excavator caused the explosion, there was no fault or negligence by Breaking Solutions or its operator who were unaware of the electrical cable. Rather, NYCTA, which was required to identify any underground hazards, failed to identify, mark, protect, or shut off the power to the buried cable, leading to the explosion.

Burlington disclaimed coverage for NYCTA and MTA, and commenced a declaratory judgment action seeking a determination that no coverage was owed because there was no evidence that the explosion resulted from any negligence or fault of Breaking Solutions. A lower court agreed, but the Appellate Division, First Department reversed holding that the operative language required only that the loss be *"caused, in whole or in part,"* by an act or omission of the named insured. Because Breaking Solutions' act of striking the electrical cable caused the explosion, coverage was triggered, even though there was no negligence or wrongful conduct on its part. A risk that the owner was contractually required to identify, control, and avoid – and did not – would be borne by the contractor's insurance carrier, with all the resulting impacts to the contractor's insurance program and premiums.

Appealing the decision to the New York Court of Appeals, Burlington Insurance argued that *"caused, in whole or in part, by"* the named insured implied a negligence standard.

CONTINUED ON PAGE 2

IN THIS ISSUE

CONTINUED "WHEN THE ADDITIONAL INSURED CAUSES THE LOSS"

If the named insured contractor was not shown to have acted negligently, there could be no coverage for the additional insured. The insurer also argued that the named insured must have proximately caused the loss; that is, Breaking Solutions actions were than just one cause leading to the outcome. The NYCTA, MTA, and City argued that only "but for" causation need be shown for coverage to apply – "but for" Breaking Solutions having struck the unidentified, energized electrical cable buried below the concrete, the explosion would not have occurred. Where "but for" causes bear some connection to an outcome, they do not always lead to legal liability. A proximate cause, the court majority noted, refers to a legal cause that results in liability. That determination is informed by policy considerations and a sense of justice as to the proper limits of liability beyond which a court should not go.

The court majority rejected the insurance carrier's insistence upon a negligence standard that would defeat additional insured coverage unless the named insured could be shown to be negligent. The majority also rejected the putative additional insured's call for mere "but for" causation that could result in an additional insured being covered even when it was solely responsible for a loss. *"Caused, in whole or in part, by"* requires proximate causation, the majority held. The "but for" cause of Breaking Solutions coming into contact with the cable was not enough to establish liability, and coverage, when Breaking Solutions was not negligent or at fault in operating its excavator, or in not knowing the existence of the energized cable. The proximate cause of the injury was the failure of NYCTA to identify, mark or de-energize the cable. Liability existing where there is fault, the additional insured endorsement language limits coverage to when the named insured's negligence, or some other actionable acts of omissions lead to a loss. E&D

1 *Burlington Ins. Co. v. New York City Transit Auth.*, 29 NY3d 313 (2017).

CONTINUED "AIA A201 UPDATES: NEW RISKS AND A FEW REWARDS"

- Claims for indemnity arising out of injury to employees of the insured
- Claims or loss excluded under a prior work endorsement
- Claims related to residential or other habitational projects, if the work is to be performed in such a project
- Claims related to roofing, if the work involves roofing
- Claims related to exterior insulation finish systems (EIFS), synthetic stucco or similar exterior coatings or surfaces, if the work involves such coatings or surfaces
- Claims related to earth subsidence or movement, where the work involves such hazards
- Claims related to explosion, collapse, and underground hazards, where the work involves such hazards.

Mandatory Neutrality for IDM's (1.1.8)

The new A201 expressly requires Initial Decision Makers (IDM) to render decisions in good faith and to "not show partiality to the Owner or Contractor." Although architects are compensated by owners, and often have strong relationships with them, under the A201 the IDM must remain neutral and impartial. This language should help architects explain and justify these obligations to project owners, who often expect some measure of loyalty when disputes arise.

Under §6.1 of the A101, architects receive the IDM role by default, unless the parties specifically appoint a different individual. This may not be the best practice. An architect may prefer to avoid being in the middle of an owner-contractor dispute or be reluctant to make a decision against the owner, who is paying its fees. Further, owners are likely to be unhappy if their architect renders a decision against it and contractors are skeptical about the ability of the architect to be neutral.

This explicit language requiring neutrality and good faith is a positive addition to the contract. Still, a better approach may be to remove the architect-by-default provision and require the parties to affirmatively select the IDM.

Email Finally Welcome, Except for Notices of Claim (1.6)

The AIA has finally accepted email as a valid means of communication on construction projects. Two caveats: parties must specifically select email as an accepted method of communication, and email cannot be used to deliver notices of claims. Claim notices must still be delivered by certified mail, registered mail, or by courier with proof of delivery. A party personally hand delivering a notice is no longer an effective option because there is no proof of delivery.

While this change is a good one, it does not go far enough. Neither party should have to wait for a hard-copy notice to be made aware of a claim. For now, the better practice is for claim notices to be delivered by both email and hard copy, with receipt being effective upon delivery of the hard copy.

The Risk of Dictated Means and Methods (3.3.1)

A Contractor remains solely responsible for construction means, methods, techniques, sequences, and procedures and for job site safety of such. However, when the Contract Documents dictate specific means and methods, the Contractor has a duty to both spot unsafe procedures, and now to specify a safe alternative. Arguably, the risk has been shifted from the Architect who specified the unsafe procedure to the Contractor. The Architect is required to evaluate Contractor's proposed alternatives for conformance with design intent; and, unless Architect objects, Contractor shall perform its Work using its alternatives. Unanswered is the question of what happens if the alternative approaches are contrary to the Contract Documents. The risk would appear to be the Contractor's.

Project Schedule Requirements (3.10)

Recognizing that the Contractor may not be the one preparing the project schedule, the 2017 A201 no longer contains the word "prepare." Section 3.10 now mandates certain minimum content including identification of milestone dates and an apportionment of work by construction activity, though the provision does not rise to the level of a scheduling specification.

Minor Changes Risk (7.4)

The 2017 A201 permits a contractor to challenge minor change directives. If a contractor believes that a minor change directive will affect the contract sum, time, or scope, it has the right, upon proper notice, to refuse the directive. The risk to the Contractor is that if it proceeds with the work before giving notice, it explicitly waives its claim. The impacts of minor changes cannot be taken lightly.

Important "AND" Added To Termination For Cause (14.2)
Termination for cause by the owner under the A-Series contract forms is at least a three-step process: architect certification that sufficient cause exists to justify termination for cause, service of a seven-day notice upon the contractor and the surety, and termination.

The 2017 version includes the word "and" which clarifies that the certification is a distinct step in the process. Although this change is a step in the right direction, further clarification would help. The 2017 provision states in relevant part:

When any of the reasons described in Section 14.2.1 exist, and upon certification by the Architect that sufficient cause exists to justify such action, the Owner may, without prejudice to any other rights or remedies of the Owner and after giving the Contractor and the Contractor's surety, if any, seven days' notice, terminate employment of the Contractor.

Unfortunately, at least three important questions remain: 1) What constitutes a "certification by the Architect"?, 2) Is the seven-days a cure period or may the owner restrict project access during this period?, and 3) Does termination self-effectuate at the end of the seven days, or does it require an additional communication to effectuate termination? Although case law provides guidance, it would be preferable to spell it out plainly in the contract provisions.

Narrowed Role for IDM (15.1.3.2)
There is no need to submit to the IDM claims that first arise after the "period for correction of Work" under the 2017 A201. All that is required is written notice to the other party. Also, no IDM involvement is needed for claims that arise under the contract terms governing hazardous materials, emergencies, and settlement of an insured loss.

60-Day Limitations Period for Challenging Decision of IDM (15.3.3)
Article 15 now effectively establishes a sixty-day limitations period for challenging decisions made by the IDM. The triggering event is a demand from one party that the other party file for binding dispute resolution. What remains troubling is the unchanged language from the 2007 A201 that provide if the other party does not file for binding dispute resolution within 60 days after receipt of the demand, then both parties waive their rights to binding dispute resolution (i.e., arbitration or litigation) with respect to the initial decision.

Contractors must continue to be vigilant with the timing of contesting IDM's decisions if they want to maintain their right to challenge a decision. E&D

Subcontract Termination is Not Automatic

MATTHEW HOLMES

A decision by the federal district court for the District of Pennsylvania highlights a couple of important lessons for contractors and subcontractors.[1] Hirani was the general contractor on a U.S. Army Corp of Engineers flood protection project on a public street in Washington D.C. Hirani hired subcontractor American Civil Construction, LLC (ACC) to provide project supervision. The Corps terminated Hirani for default on April 26, 2013. Hirani did not officially terminate ACC's subcontract until May 2, 2013, according to ACC, which also argued that its last day of work was on May 1, 2013. In the few days following Hirani's termination, ACC, in addition to demobilizing, did a number of things including clean up, installing fencing, and moving signage, apparently to protect the site, having been told by Hirani that the default termination would be challenged.

Ultimately, ACC sued Hirani for wrongfully refusing to pay amounts due, for delay damages, and for terminating the subcontract without notice. ACC also made claim against Hirani's payment bond. ACC filed its action on April 29, 2014. That timing proved critical, as the parties argued regarding the dates of termination and whether ACC's payment bond claim was time barred under the language of the Miller Act that requires actions to be brought within a year of the date "when the last of the labor was performed or material was supplied."

Hirani argued that ACC's "last day" was in March, 2013, and alternatively no later than the date when Hirani was itself terminated by the Corps, there being no subcontract work to perform because the prime contract was terminated. But the subcontract did not provide for automatic termination upon the owner's termination of the prime contract for default. The subcontract only addressed termination of the subcontractor for default and in the event the prime contract was terminated for convenience. Further, applicable Code of Federal Regulations required Hirani, upon its termination, to terminate all subcontracts related to the terminated work, something Hirani delayed in doing.

The District Court for the District of Columbia found that the "subcontractor is only bound by the subcontract", which operated independently of the prime contract. Termination of the subcontract required a separate, affirmative act by Hirani, which did not occur until sometime after April 29, 2013 and may not have complied with the notice requirements of the subcontract. ACC's "last day" for Miller Act purposes was not established by Hirani's termination by the Corps. Left to be determined at trial was the nature of the work ACC performed in the days before it was officially terminated. If the work was compensable as part of the original subcontract, and not repair or corrective work, then the one year Miller Act statute of limitations would run from that work.

This case illustrates several important lessons. The termination of the prime contract does not automatically terminate the subcontract. The subcontract must so provide or the termination provisions of the prime must be properly "flowed down" to the subcontract. Also, it is always risky to wait to file an action until nearly the last day to do so. Though it prevailed in this decision, had ACC filed its action a few days or weeks earlier, it could have avoided the legal fees required to defeat this argument of Hirani. E&D

1 *U.S. f/u/b/o American Civil Construction, LLC v Hirani Eng'g & Land Surveying, PC et al*, 263 F.Supp.3d 99 (D.D.C. 2017).

NEW YORK
925 Clinton Square
Rochester, New York 14604

Visit us online at:
WWW.ERNSTROMDRESTE.COM

Ernstrom & Dreste, LLP also publishes the Fidelity and Surety Reporter. If you would like to receive that publication as well, please contact Clara Onderdonk at conderdonk@ed-llp.com. Copies of ContrACT Construction Risk Management Reporter and The Fidelity and Surety Reporter can also be obtained at Ernstrom & Dreste, LLP's website (ernstromdreste.com).

FIRM NEWS

In January, Kevin Peartree and Matthew Holmes presented E&D's annual Construction Law Update, *"Lessons Learned and Re-Learned in 2017,"* for the Builders Exchange of Rochester.

In January, Kevin Peartree was a panelist for a joint Rochester CSI/DBIA Upstate New York Chapter presentation entitled *"Procurement Front-Ends/Contracts".*

Martha Connolly and Kevin Peartree authored new chapters for the 2018 Cumulative Supplement to the ConsensusDocs Contract Documents Handbook, published by Wolters Kluwer.

Kevin Peartree recently authored an article for ROBEX magazine titled *"The Subcontract Bucket Challenge".*

In March, Kevin Peartree will be master of ceremonies for the Builders Exchange of Rochester 2018 Craftsmanship and Lifetime Achievement Awards.

We are pleased to announce that Brian J. Geary is now of counsel to E&D. Brian has over 35 years of experience in construction, engineering, business and law. As a licensed professional engineer and successful construction supplier and businessman, Brian brings valuable technical and financial experience to the representation of E&D's clients.