

# Do You Need Real Estate Development Professional Liability Insurance?



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By John Schmidt, Account Executive

## Coverage Basics

In addition to General Liability coverage, which responds to claims involving bodily injury and property damage to third parties, a Real Estate Development Company should also consider Professional Liability exposures and the need for Professional Liability insurance.

A Real Estate Development Professional Liability policy provides coverage for defense and damages an insured is legally obligated to pay resulting from a settled claim involving a “wrongful act” that was committed or allegedly committed by the insured.

A “wrongful act” means an actual or alleged breach of duty, neglect, act, error or omission committed in performing “real estate development professional services.” These “Real estate development professional services” include all normal and usual service provided by a property developer and more specifically includes:

- Preparation, transmittal, and awarding of design and construction bid packages;
- Management, coordination and supervision of design and construction;
- Identification and obtaining of applicable permits, variances, consents, easements & other rights;
- Real estate agent, title agent, notary public, and property manager services

## Policy Form

The vast majority of professional liability insurance policies are written on a “claims-made” or “claims-made & reported” form. Under a “claims-made” policy, coverage is triggered by the date an insured is first made aware of the claim (vs. the actual date of the alleged, initial wrongful act or occurrence). The policy coverage period for a “claims-made” policy typically extends back in time for past wrongful acts that develop into and are brought forth as claims during the current policy term. Some policies extend back in time without limit, but most have a retroactive date which excludes coverage for

wrongful acts that occurred prior to the retroactive date.

A “claims-made & reported form” engages a similar coverage approach except it limits the coverage trigger to when a claim is actually reported to the insurer. This is typically more restrictive than a pure “claims-made” policy due to a time restriction applied on how long an insured has to report a claim for a particular policy term - say, 60 days after policy expiration date.

## What’s Not Covered

Every policy varies, but most have a detailed list of exclusions for claims involving:

- Fraud, dishonesty, criminal conduct, or any knowingly wrongful, malicious, or deliberate acts or omissions - usually as established via adjudication
- Gain of any profit or advantage to which the Insured was not legally entitled - usually qualified as “in fact” or as established via adjudication
- Wrongful acts committed prior to coverage period (i.e. retroactive date)
- Wrongful acts that have been reported under another policy prior to the policy period
- Insured vs. insured claims
- Employee Retirement Income Security Act of 1974
- Securities Act of 1933 & Securities Exchange Act of 1934
- Workers Compensation, Unemployment Compensation, Employers Liability or Disability Benefit Law
- Bodily injury and property damage
- Contractual liability including breach of warranty/guarantee - unless such liability would have existed in the absence of such contract
- Pollution including asbestos and mold

- Discrimination and other employment related torts
- Infringement of copyright, trademark, trade dress, trade name, patent or other intellectual property

Please note the above is just a sampling of common exclusions and it is important to review each company's specific exclusions.

Most policies also include warranties confirming third party members of the development team (including architects, engineers, consultants, etc.) have their own professional liability coverage in effect.

### Claim Scenarios

(1) A developer completes a development of several homes. Three years later, several homes' foundations crack because the developer did not have the site properly graded. The affected homeowners collectively bring suit against the developer and general contractor.

Since the developer acted as a construction manager and/or the responsible party for obtaining and preparing the grading plan, the claim could fall outside of a General Liability policy. Coverage for cracking that arose from design errors or failure to manage the construction would be considered under a Professional Liability policy.

(2) A developer engages an architect firm to design a structurally unique apartment building. As a result of the unique design, project costs are 15% above initial proposals. The developer "sells" the unique architecture and convinces outside investors that the artistic nature of the structure will demand higher rent and effectively improve their investment opportunity. Four months into the project, the architect determines his original design will only support a smaller structure. The change minimizes the artistic affect of the building and creates an additional \$470,000 of "re-engineering" and "re-construction" change orders. The new design ultimately adds 6+ months to completion date due to revised permitting. Further complicating matters, upon completion, recession hits and pushes the rental market in the wrong direction.

The investors, after unsuccessful negotiations with both the architect and developer, bring suit against both. The architect firm, in an effort of cost containment, had decided to lower their professional liability limit to \$500,000; in addition, unbeknownst to the developer, the architect had already exhausted over \$200,000 of that limit by fighting a similar claim on another out-of-state project. Coverage would be considered under the developer's Professional Liability policy to respond to such allegations of design coordination and supervision errors or omissions.

If you have a potential exposure for Real Estate Development Professional Liability, please contact your Parker Smith & Feek Account Executive, who will be happy to help you evaluate your Professional Liability risks.