

Faulty Workmanship – Is Your Business Properly Protected?

Faulty workmanship is a risk that specialty contractors, such as utility and excavation contractors, face with each project they take on. Problems can come from a variety of factors and often take years to arise. For this reason, utility and excavation contractors need insurance coverages built for their unique exposures. To address this need, business insurance carriers are beginning to offer contractor errors and omissions policies, which can protect your company from significant losses.



Diamond Partner

Deconstructing Contractors Errors and Omissions Coverage

Historically, professional liability policies were designed to protect firms against risks beyond the coverage of their general liability (GL) policies — specifically claims resulting from design errors and omissions. Today, professional liability policies have evolved into a more robust contractors errors and omissions policy that expands coverage to include faulty workmanship and the use of defective materials and/or products. As a utility and excavation contractor, it is important to understand the limitations and benefits of professional liability policies, for both your firm and the design professionals you are hiring. More and more contract requirements are emphasizing the need for this type of coverage, which signals the need for additional in-depth coverage.

Commercial general liability (CGL) policies were never intended to serve as warranties of work. Damage to self-performed work is considered to be a “business risk” and is excluded in most situations. Exceptions would be damage to property that is not the work itself or, possibly, damages caused by or to the work of a subcontractor done on behalf of a general contractor.

Some insurance carriers have long held that faulty workmanship never satisfies the commercial general liability insuring agreement, because there is no accident and, therefore, no property damage that could be considered a covered “occurrence.” Case law is often split by state on this issue. Since 2005, at least 20 jurisdictions have issued decisions to support defective construction as an “occurrence” with respect to damage to property other than the work itself.

Courts in other states, such as Arkansas, Hawaii, Pennsylvania, South Carolina and, most recently, Ohio, ruled that faulty workmanship is not an occurrence. To add another layer of complexity, and in response to those court decisions, South Carolina and Arkansas joined other states in enacting legislation to support the opinion that faulty workmanship, which causes damage to property that is not the self-performed work, is indeed a covered occurrence.

While court decisions may change how CGL policies are construed, insurance carriers do offer endorsements to clarify that the exceptions to work exclusions, and damage to property that is not the work itself, are deemed to be an occurrence. Utility and excavation contractors should partner with brokers and carriers that can properly explain these options and whether they are even needed in a particular state.

Digging Deeper into Why You Need Contractors Errors and Omissions Coverage

Faulty workmanship claims not only damage a company’s reputation but ultimately affect their bottom line. Utility and excavation companies are putting themselves at risk every day by not having the proper business insurance coverage.

To put the faulty workmanship issue in more realistic terms, suppose, for example, ABC Sewer Co. was hired to rehabilitate 13 manhole covers in a residential neighborhood. The firm contracted with the local municipality and was solely hired for construction without any design work required. The total project bid was \$150,000 and the scope of work included excavating around current manholes, removing, replacing and re-asphalting.

After completion of work and settlement of the new asphalt, it was revealed that all of the new manholes sat approximately 2 in. above street grade. This issue brought multiple complaints from homeowners regarding unsafe driving conditions and potential damage to their vehicles while driving on the street.

After holding an investigation, it was discovered that ABC Sewer did not install the manhole cover plate and coupling at the right depth, thus when the new asphalt settled, the cover was protruding from the street. As a result, all of the manholes would need to be removed, installed at the correct depth and the street re-asphalted. The estimated cost to redo the work was \$125,000.

In this case, if the firm does not have errors and omissions coverage within their insurance policy, they will have to pay \$125,000 out of pocket in re-work to rectify their faulty workmanship. Basically, any resulting property damage or bodily injury from the faulty work is likely covered by a GL policy, however, only errors and omissions coverage would provide coverage for faulty workmanship.

Get Properly Equipped for Faulty Workmanship Claims

With many claims similar to the ABC example above, carriers like CNA have taken steps to recognize the coverage need for what had previously been considered a pure business risk — faulty workmanship self-performed by a subcontractor. The Contractors Errors and Omissions and Pollution Liability (CEO) policy was developed in response to a number of requests for a product to address construction errors and omissions.

Utility and excavation contractors’ work often includes an element of judgment and design in selecting the means and methods of construction. Their contractual scope of work, however, is construction driven, and they do not generally deliver design documents as a work product. Claims regarding work by specialty contractors are typically driven by faulty workmanship. The CEO product responds to that market need. It is designed for specialty contractors that do not have a professional exposure per se, but do have an exposure from errors or omissions in construction that may cause damages not covered by the ISO Commercial General Liability (CG 0001) form or traditional professional liability forms.

Unrelenting change in the construction industry has truly become the “new normal.” The best utility and excavation contractors, brokers and insurance companies will follow the trends in 2013 and work in partnership to assure coverage needs are understood and addressed.

If you have any questions regarding Contractors Errors and Omissions coverage, contact **Helen L. Prince**, CIC, CRIS, at 214.220.5724 or helen.prince@cna.com or **Jason Oswald**, ACI, ARM, CRIS, at 303.858.4146 or jason.oswald@cna.com.

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