

Design and Construction Management Professional Reporter

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\$4 Million Lawsuit Dismissed Against Architect

On April 6, 2009, a Massachusetts Superior Court judge dismissed a \$4 million lawsuit brought by Middle Oak Insurance Company against the architect, contractor and other parties involved in the construction and design of a multi-building apartment complex that was damaged during a fire occurring three years after the project's completion. The law firm Donovan Hatem LLP represents the architect in the lawsuit. The decision, *Middle Oak Insurance Company v. Tri-State Sprinkler Corp., et al*, granted the architect's summary judgment motion and held that the waiver of subrogation clause contained in the standard AIA contract between the Owner and Contractor precluded the insurance carrier from asserting claims against the parties for post-construction losses. The case confirms in Massachusetts a nationwide trend in extending AIA waiver of subrogation provisions beyond the completion of construction projects.

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Indiana Appeals Court Holds Economic Loss Doctrine Bars Negligence Claims Against Professionals

By John W. Dennehy, Esq.

THE INDIANA COURT OF APPEALS recently held that design professionals were not responsible for \$40,000,000 in remediation costs and consequential damages associated with structural repairs to a public library renovation and addition project where the design professionals had not contracted with the municipality. The court reasoned, in part, that remediation work to the project itself did not constitute property damage. Indianapolis-Marion County Public Library v. Charlier Clark & Linard, P.C. et al., 900 N.E.2d 801 (Ind.App. 2009).

In February 1998, the Architect entered into an Owner/Architect Agreement for services in connection with the design and construction for renovations and additions to a public library (the "Project"). Thereafter, the Architect entered into a standard agreement with a Subconsultant to provide structural engineering design services for the Project. The Architect entered into another agreement with a separate engineering firm for construction administration services related to the structural design, Subconsultant CA.

The Architect's agreement with the subconsultants contained standard provisions limiting the subconsultants' responsibilities on the Project:

[Subconsultant] shall not be responsible for the acts or omissions of the Architect, Architect's other consultants, contractor, subcontractors, their agents or employees, or other persons performing any of the Work.

Nothing contained in this Agreement shall create a contractual relationship with or cause of action in favor of a third party against either the Architect or [Subconsultant].

On August 14, 2003, Subconsultant CA visited the site and observed deficiencies related to the placement of steel reinforcements and noted this in its Construction Observation Report, which also included a statement that not all discrepancies were apparent or visible from site observations.

In February 2004, the Owner discovered major voids in concrete beams and columns in the garage and became concerned about the structural integrity of the garage. Hence, the Owner retained an independent engineering consultant to conduct a forensic investigation. The independent investigation revealed several construction and design defects in the garage, which placed the garage at serious risk of structural failure if construction were allowed to continue.

The Owner sued the Subconsultant on August 27, 2004, and then amended the complaint to add Subconsultant CA on June 2, 2006. The claims included breach of contract, negligence, gross negligence, violation of statutory and regulatory duties, fraud, and bad faith. No claim for negligent misrepresentation was filed against either defendant. The Owner settled its claims against the contractor and the Architect, and entered into a release and settlement agreement with the Architect on August 23, 2006, which included a provision wherein the Architect assigned its rights to assert claims against its subconsultants to the Owner. The Owner did not argue that this assignment provided an exception to the Economic Loss Doctrine.

The trial court ruled that the Economic Loss Doctrine barred the negligence claims and then dismissed them reasoning that the plaintiff was not in privity of contract with either subconsultant, and the damages were solely economic in nature, not involving personal injury or property damages. The Court of Appeals of Indiana upheld dismissal reasoning that the Economic Loss Doctrine maintains the distinction between tort and contract, protects parties' freedom to allocate economic risk by contract, and encourages the party best situated to assess risk to insure against that risk. The court cited with approval to Gunkel, a case that applied the Economic Loss Doctrine to construction litigation holding that, absent privity of contract, a party to a project cannot be held liable for negligence when only economic damages are claimed. See Gunkel v. Renovations, Inc., 822 N.E.2d 150, 153 (Ind. 2005). In Gunkel, the court stated that damage to the product itself, including costs to repair or reconstruct, is an economic loss even though it may have a component of physical destruction.

The court found as a matter of law that the defendants were not in contractual privity with the plaintiff, and that the remediation costs for the garage and any ensuing consequential damages were economic, and thereby barred by the Economic Loss Doctrine. The court was not persuaded by arguments that the allegation of imminent danger

of collapse constituted property damage. The court cited further with approval to [Bamberger](#) and reasoned that an imminently dangerous condition to third persons must cause injury or physical harm to the property other than the product itself. See [Bamberger & Feibleman v. Indianapolis Power & Light Co.](#), 665 N.E.2d 933, 938 (Ind.Ct.App. 1996). The court refused to address the plaintiff's allegations of negligent misrepresentation as an exception to the Economic Loss Doctrine because such a claim had not been plead.

This decision provides the defense of design professionals with a well-written and strongly supported opinion to guide trial courts in countering arguments that destruction during remediation constitutes property damage. ■

\$4 Million Lawsuit Dismissed Against Architect

By Meghan L. McNamara, Esq.
(Continued from page 1)

Construction projects occasionally experience unexpected perils such as fire, water damage or collapse which are typically covered by an Owner's property or "builder's risk" insurance. The standard AIA General Conditions require the Owner to purchase and maintain property insurance for the entire Work performed at the site. The General Conditions define the term "Work" to include construction and services required by the contract documents, whether fully completed or partially completed, and may constitute the Project, either in whole or in part. When a calamity occurs, the insurance policy will generally cover the loss. However, where the cause of the loss is believed to be the result of a design or construction error, the rights of the Owner will "subrogate" to the insurer who has paid out the loss, and the insurer can then maintain an action against the design professional or contractor for the loss.

There are contractual provisions contained in the AIA Standard Form Agreement between the Owner and Contractor which can protect the design professional from claims brought by property insurance companies. These provisions are called "waiver of subrogation" provisions and are found in Section 11.4 of the General Conditions. A "waiver of subrogation" precludes an insurer from seeking recovery from a third party (i.e., the Contractor) for the amount it paid to the policyholder for a loss caused by that third party. Section 11.4.7 of the General Conditions explicitly applies the waiver of subrogation to the Architect and its consultants or subcontractors. Therefore, the insurer is precluded from bringing a claim against the Architect or its agents for losses covered by the insurance policy regardless of design error.

Courts have traditionally upheld waiver of subrogation clauses where the loss occurs during the actual construction phase of a Project. However, there has been debate over whether these "waiver of subrogation" provisions extend to losses occurring after a Project's completion. Section 11.4.5 of the General Conditions provides that if an Owner procures separate property insurance from that insuring the Project during the Project's construction or, if after final payment, separate property insurance is provided that covers the completed Project, the Owner waives all subrogation rights for damages caused by fire or other causes of loss covered by property insurance. Many jurisdictions, including Colorado, Georgia, Indiana, New Jersey, and Ohio have held that section 11.4.5 extends the waiver of subrogation to post-construction losses, including additional insurance policies after construction has been completed. No appellate court in Massachusetts had ever specifically addressed the issue. However, in [Lumbermens v. Mutual Insurance Co. v. Grinnel Corp.](#), 447 F.Supp.2d 327 (D.Mass. 2007), the District Court of Massachusetts went against the weight of authority from other jurisdictions and interpreted the standard language as limiting the waiver of subrogation in section 11.4.5 only to losses occurring during the construction period.

As noted, in [Middle Oak Insurance Co. v. Tri-State Sprinkler Corp.](#) et al, the Court overruled the decision in [Lumbermens](#) and adopted the majority's interpretation of section 11.4.5. In doing so, it ruled that the AIA waiver of subrogation provision applies to post-construction losses. In [Middle Oak](#), the Owner entered into a contract with its Contractor to construct a multi-building apartment complex in Georgetown, Massachusetts. The contract consisted of

two standard AIA forms: A101-1997, "Standard Form Agreement Between Owner and Contractor," and A201-1997, "General Conditions of the Contract for Construction." Section 11.4.5 of the General Conditions stated, in relevant part:

If during the construction contract period the Owner insures properties, real or personal or both, at or adjacent to the site by property insurance policies from those insuring the Project, or if after final payment property insurance is to be provided on the completed Project through a policy or policies other than those insuring the Project during the construction period, the Owner shall waive all rights in accordance with the terms of Subparagraph 11.4.7 for damages caused by fire or other causes of loss covered by this separate property insurance. All separate policies shall provide this waiver of subrogation by endorsement or otherwise.

The Project was completed and occupied by May 2004. On January 7, 2007, a major fire occurred on the third floor of one of the buildings, causing over \$4 million dollars in damages. Middle Oak insured the complex at the time of the fire and brought claims against the Architect, the Contractor and others to recover the monies it paid to the Owner for its loss.

The Architect and other defendants moved for summary judgment based upon the waiver of subrogation clause contained in the agreement between the Owner and Contractor. The Court granted the Architect's motion for summary judgment, stating that the contract language in the AIA forms "demonstrates the parties' intent to extend the applicability of the waiver of subrogation to post-construction losses." The Court reasoned that this interpretation "comports with the strong public policy reason for supporting waiver of subrogation clauses, i.e., encouraging parties to anticipate risks and to procure insurance covering those risks, thereby avoiding future litigation and facilitating and preserving economic relations and activity," citing Great Northern Insurance Co. v. Architectural Env'ts, Inc., 514 F.Supp.2d 139, 143 (D. Mass. 2007). The ruling is significant, because it affords design professionals additional protection from future losses that may occur years after the Project's completion under the AIA contract between the Owner and Contractor. ■

Colorado Court of Appeals Recently Interpreted the Economic Loss Rule as Barring a Fraud Claim

By Sa'adiyah Masoud, Esq.

IN A POSITIVE RULING FOR DESIGN PROFESSIONALS, the Colorado Court of Appeals recently interpreted the economic loss rule as barring a fraud claim. This is good news for design professionals as many attorneys representing contractors and other third-parties have been alleging claims of fraud, negligent misrepresentation and other intentional torts against design professionals in an effort to avoid the economic loss rule and unfavorable contractual provisions.

The economic loss rule is a traditional principal of law that limits tort law and bars its use where the claimant and the defendant are contractually connected. Attorneys representing design professionals have used this rule for years in dismissing negligence claims against design professionals. As the Colorado Court of Appeals describes it, a suing party "suffering from only economic loss from the breach of an express or implied contractual duty may not assert a tort claim for such a breach absent an independent

duty of care under tort law." Some courts have held that claims of fraud, negligent misrepresentation and other such intentional torts are exceptions to this rule, and independent duties of care.

While the Colorado Court of Appeals did not hold the economic loss rule always bars fraud claims or other intentional tort claims, the court demonstrated that it would carefully review and scrutinize the source of an intentional tort-sounding claim

before determining whether it is an appropriate exception to the economic loss rule. This decision shows that Colorado, like the courts in Pennsylvania, New Jersey and Michigan, will look beyond the mere form of the allegations to examine whether the claims being pursued are truly intentional torts or disguised contractual claims presented as intentional torts.

The decision in Colorado concerned a national engineering firm that, pursuant to a contract with the City of Louisville, provided contract administration services on a road-and-bridge project in Louisville, Colorado. Hamon Contractors, Inc. v. Carter Burgess, Inc. et al., Nos. 07CA0987, 07CA0988, 07CA2342, 2009 WL 1152160, at *1 (Colo. Ct. App. April 30, 2009). During the Project, the general contractor was delayed by excessive water on the site, and had to take measures to stabilize oversaturated soil on the site. The general contractor submitted change orders asking for additional payments for its efforts. The change orders were largely denied by the City pursuant to the engineering firm's recommendation. Subsequently, the City (via the engineering firm's recommendation) also notified the general contractor that it was being assessed liquidated damages for the delays on the Project and ultimately withheld \$413,000 in liquidated damages from the general contractor.

The general contractor sued all of the parties involved and claimed in particular that the engineering firm fraudulently concealed and misrepresented project problems. The Colorado court concluded that the general contractor essentially was suing the

engineering firm for failing to provide truthful information about the drainage problem. The damages were economic, and related to the engineering firm's alleged wrongful disapproval of change orders and imposition of delay damages, all of which were within the scope of the engineering firm's contract with the City. This alleged fraud was really a claim for alleged breach of a contractual duty that was not independent of any contract duties between the engineering firm and the City.

As explained best by the Colorado Court of Appeals,

The economic loss rule can apply to fraud or other intentional tort claims based on post-contractual conduct. The question in any case where the economic loss rule is alleged to apply is whether the duty alleged violated exists independently of the contract. With respect to fraud claims specifically, this depends on whether the alleged fraud arises from duties implicated by a party's performance of contractual terms or whether the alleged fraud concerns a matter extrinsic to the contract. Where the alleged fraud arises from duties implicated by a party's performance of contractual terms, the claim is barred by the economic loss rule.

In sum, this is a great decision for design professionals and will assist design professionals in defending against intentional tort allegations in Colorado and elsewhere. ■

Acting Beyond the Scope of One's Contract May Confer Liability for Project Safety

By Michelle L. Moshe, Esq.

DESPITE CONTRACT PROVISIONS TO THE CONTRARY, design professionals can unknowingly be charged with voluntarily assuming safety duties under certain circumstances.

As a general rule, in New York, a design professional incurs no statutory or common law obligations to another absent contract language to the contrary. See generally Gonzalez v. Pon Lin Realty Corp., 34 A.D.3d 638 (App. Div. 2nd Dept. 2006); Boyd v. Lepera and Ward, P.C., 275 A.D.2d 562 (App. Div. 3rd Dept. 2000); Valasquez v. Long Island Power Auth., 16 Misc.3d 1128, 2007 WL 2684815 (N.Y. Supp. 2007); Davis v. Lenox School, 151 A.D.2d 230 (App. Div. 1st Dept. 1989). Moreover, before a statutory duty is imposed upon a party to provide a safe work area, that party must have authority to control the activity that could result in an injury and, as such, to enable it to avoid or correct an unsafe condition. Davis v. Lenox School, 151 A.D.2d 230 at 231.

However, New York law also provides that, if a design professional undertakes any efforts relating to safety issues, that design professional may have imposed upon itself statutory and/or common law duties regarding those issues. See generally, Duda v. John W. Rouse Contr. Corp., 32 N.Y.2d 405 (1973); Zolotar v. Krupinski, 36 A.D.3d 802 (App. Div. 2nd Dept. 2007). For example, if an architect directs workers to perform their work in a manner which ultimately results in injury or damage, then the architect

may be found liable for the alleged damages. Zolotar v. Krupinski, 36 A.D.3d 802 at 802.

Accordingly, design professionals who practice in New York, and undertake work beyond the scope of their contract which may impact project safety may find themselves liable for any resulting injuries or damage. ■

Claims of Professional Negligence Must Be Asserted in a Timely Manner and Be Supported by Expert Testimony

By Jordan S. Rattray, Esq.

IN ITS DECISION in Tin Cup County Water and/or Sewer District ("Tin Cup") v. Garden City Plumbing & Heating, Inc. ("Garden City") and Druyvestein Johnson & Anderson, Inc. ("DJA"), the Supreme Court of Montana upheld precedent helpful to the defense of professional negligence claims. The Court ruled that the appropriate statute of limitations is determined by the gravamen of the allegations alleged and not the causes of action identified by a plaintiff. The Court also upheld existing caselaw that requires expert witness testimony to support allegations of professional negligence when understanding of the issues presented is beyond the trier of fact. Both of the Court's rulings uphold a standard which a plaintiff must satisfy in order to be successful in a claim for professional negligence.

The plaintiff, Tin Cup, operates a dam originally constructed in 1906 which provides irrigation water to farmers in the Bitterroot Valley near Darby, Montana. In 1997, it became clear that the dam needed to be repaired. Tin Cup retained DJA to render engineering services in connection with the replacement of the dam's outlet conduit pipe. Ultimately, Tin Cup filed suit against DJA and the contractor alleging professional negligence, breach of contract and indemnification. At the close of discovery, DJA filed a Motion for Summary Judgment on the grounds that Tin Cup's claims were barred by the statute of limitations. The statute of limitations begins to run when a plaintiff has been damaged and has the right to bring an action against a defendant. In Montana, like most jurisdictions, there are different statutes of limitation for different causes of action. The Montana statute of limitations for actions arising out of a contract is eight years, and a cause of action for negligence must be asserted within three years. If the statute of limitations has run, then the plaintiff is barred from recovering under that cause of action.

DJA argued in its motion that the allegations asserted by Tin Cup while titled both negligence and breach of contract were truly claims of negligence; therefore the three-year statute of

limitations should apply to all allegations asserted by Tin Cup. The Court agreed with DJA and found that the gravamen of Tin Cup's argument is that DJA was professionally negligent in performing its duties to supervise, coordinate and inspect. The Court pointed out that Tin Cup did not allege that DJA breached a specific provision of the contract.

The Court also ruled that Tin Cup failed to meet its burden of proof that Garden City and DJA caused it to incur damages because Tin City did not present an expert witness to testify that the defendants had caused the damages. The Court stated that expert testimony is necessary when the issue presented is sufficiently beyond the common experience of the trier of fact, and the expert testimony will assist the trier of fact in determining the issue or understanding the evidence. The Court pointed out that a determination of causation as to Tin Cup's damages required an understanding of the dam's structural history, dam engineering and hydrology related to a rock and earthen dam and dam safety, the knowledge of which is beyond the understanding of the trier of fact. ■

Changes to the AIA Agreements Regarding Statute of Limitations

By Justin M. Jagher, Esq.

THE CHANGE IN THE AIA ACCRUAL PERIOD WAS HIGHLIGHTED in a recent case in the First District Court of Appeals of Illinois. In Federal Insurance Company v. Konstant Architecture, an insurance company brought a subrogation action against an architect alleging breach of contract with respect to its design of a residence. The parties agreed that the residence was built in 1997. Water and mold damage was discovered in 2002, and remediation costs exceeded \$300,000. In its complaint, the insurer alleged that the architect failed to properly design and supervise the building of the home, specifically the roof, and that the architect failed to warn the homeowners about possible ice damming, water infiltration, and possible mold infestation.

The architect moved to dismiss the case, arguing that the cause of action was time-barred because suit was not filed within the four-year limitation period governing the construction of improvements to real property. The circuit court granted the architect's motion and dismissed the case, and the Appellate Court affirmed.

The Court applied a four-year tort limitation statute because even if the claim was for breach of contract, it was based upon an act or omission involving design, planning, supervision, observation or management of construction, or construction of an improvement to real property.

The Court focused on Article 9.3 of the parties' Agreement, an AIA B141-CMa 1992 form that provided as follows:

Causes of action between the parties to this Agreement pertaining to acts or failures to act shall be deemed to have accrued and the applicable statutes of limitations shall commence to run not later than either the date of Substantial Completion, or the date of issuance of the final Certificate for Payment for acts or failures to act occurring after Substantial Completion.

Article 9.3 was inapplicable because it was not based upon the discovery rule. After reviewing relevant law from other jurisdictions, the Court held that it was not against public policy to contract for alternative limitation periods than those statutorily provided for, and found no reason to alter the contractual intent of the parties. Finding for the architect, the Court stated: "[We] find that Article 9.3 of the AIA contract in this case controlled the accrual date of the applicable statute of limitations and precluded application of the discovery rule..."

The discovery rule has frustrated many owners, and its variation by jurisdiction makes it difficult to determine the rules that will

be followed regarding the ability to bring an action. Thus, owners were losing a right to bring an action under the previous AIA documents in jurisdictions that follow the discovery rule.

The new AIA documents contain a sea change from the contractual benefit that was previously available to architects and other design professionals. For example, the AIA B101-2007 Owner-Architect Agreement provides that:

The Owner and Architect shall commence all claims and causes of action, whether in contract, tort, or otherwise, against the other arising out of or related to this Agreement in accordance with the requirements of the method of binding dispute resolution selected in this Agreement within the period specified by applicable law, but in any case not more than 10 years after the date of Substantial Completion of the Work. The Owner and Architect waive all claims and causes of action not commenced in accordance with this Section 8.1.1.

This change in the AIA eliminates the opportunity to reduce the limitation period found in many statutory schemes, and provides owners far greater leeway in the time to commence an action because it is now based on the discovery rule addressed, but rejected in *Konstant*.

As such, although this is a positive development for owners, design professionals may find that it is to their distinct advantage to try to negotiate a shorter limitation period at the creation of the parties' contractual relationship that is in keeping with the accrual period found in the prior AIA forms. ■

About Donovan Hatem

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