Design/Build: Risk Management

by Cynthia Turner

In the design-build market, with the roles of owner, contractor and designer crossing many responsibility lines, careful attention to how liability is shared among all involved parties is a top priority. There are significant liability issues associated with the design-build process. Therefore it is important to understand how the risks of design-build differ from those of design-bid-build and to review available options for allocating the project's risks equitably. This will help ensure success of the project and, hopefully, more profitable opportunities.

Design-Bid-Build

In the traditional design-bid-build model, the owner or developer drives the project and bears much of the risk. The owner or developer typically has separate contracts with the architect and the contractor. The owner bears the responsibility for non-performance if the plans or design specifications are defective. The contractor holds no responsibility for these issues.

Courts have long recognized an implied warranty that the plans and specifications issued by a construction project owner are suitable for the purpose intended. The leading Supreme Court case on the subject, U.S. v. Spearin, 248 U.S. 132 (1918), involved cross-claims by the owner and contractor resulting from a failure of a sewer built to specifications but determined to be inadequate to handle actual flows and tides. The Supreme Court excused the contractor's non-completion and affirmed recovery for extra costs associated with the failure. In other words, the contractor builds what is in the plans and specifications. If the result is not what the owner wanted, the contractor still gets paid. If the design is flawed or impossible, the contractor gets paid for attempts to comply. The so-called "Spearin Doctrine" has been widely followed and is based on the simple rationale that the party preparing the specification bears the risk of their accuracy.

The Risks Of Design-Build

Increasingly, owners are electing design-build because it allows for the fast tracking of projects, responsibility falls within one entity, (the design-builder, instead of multiple entities,) and the owner no longer has to "warrant" the specifications.

The design-builder, who historically has been the contractor, although there is a growing trend to designer-led design/build projects, has the responsibility for delivering a constructed and functional facility. As a result, contractors are not only responsible for ways, means, and methods for the construction of the project, but also for design, design accuracy, and performance. As a result, contractors are not only increasing their responsibilities, but also their professional liability exposures. Many contractors are not familiar with professional liability exposures and are not knowledgeable about the consequences of accepting this responsibility. Additionally, there are no more Spearin protections. Furthermore, the architects and engineers must realize that they are no longer working for the owner, but for the design/builder who has accepted this project under a lump sum arrangement. Historically, the architect/engineer has been the owner's representative and is responsible for ensuring the owner's expectations are met. In some cases, these expectations may be beyond the contractor's expectations. Now, however, as part of the design-build team, the architect/engineer must be conscious of the project costs and budgets. This requires a change in attitude from the traditional architect/engineer role since not staying within original budget restraints can jeopardize the success of a project. For example, when the architect/engineer works directly for the owner, she/he might recommend using high-end light fixtures even if the contractor bid the project with low-end fixtures. But as part of the design/build team, she/he needs to continue to recommend what was bid in order to stay within the project budget and deliver a successful project.

There are many new risks, as well as a shifting of risks, involved with this type of project. This level of risk, which at first may appear daunting, can be minimized and managed through effective risk management that includes careful project selection and definition, effective contract formation, appropriate insurance, and successful teaming and communication skills.
**Project Definition**
Regardless of the design-build form (contractor-led, designer-led, joint venture partnership), there must be a mutually understood and agreed upon definition of the project with the owner. Design-build works when the owners know what the desired end product is and adequately communicate that information to the design-builder. The most important aspects of a successful design-build project are the preparations of the scope of work and the clarification of the expectations from the owner.

**Contracts**
Once the project definition is established, a contract can be prepared that is consistent with the mutual expectations of the owner and the design-builder. The risks can be minimized by reading the entire contract — not just the indemnity provision, not just the limitation of liability, and not just the exclusion of consequential damages. It is important to make sure there are provisions that address the sharing of losses, because many projects experience losses. Additionally, the design-build team members should include provisions addressing cross indemnification of each other for any claims arising out of the other team members' work.

General conditions should address what happens when there is a dispute. You may want to include a mechanism in the contract whereby, if a dispute is not worked out in a week or two, it goes to a mediator to be solved. Disputes take time away from projects, and time is money. Mediation can help keep the project moving and minimize the potential for costly claims.

**Proper Insurance**
It is important to establish clear roles, responsibilities and liabilities of the various design and construction entities. Design professionals want to limit their risk to the design portion of the work, where they can obtain errors and omissions insurance. Contractors that are performing details of design now have a professional liability exposure and need to obtain proper insurance. A contractor's normal Commercial General Liability coverage excludes losses due to design error, project delays, pollution or other exposures that accompany design-build work. However, project specific policies and policy enhancements are available.

**Teamwork And Communication**
When the shift to design-build began, claims shifted from the owner to the parties involved. In many cases this has to do with the fact that the various parties involved in design-build are not used to being part of a team. Partnering with the same parties, project after project, will assist in reducing this exposure. Most established teams are more successful at working together.

The owner and design-builder need to work together as a team in order to maximize the probability of success, although each will approach the project from their own perspective. The owner and design-builder must clearly communicate their respective expectations, and create contract documents that accurately reflect the responsibilities and risks of each party. Problems will occur even with a solidly crafted contract, if everyone is not on the same page.

In the end, effective communication, with the owner and among the various parties involved in the project, is the single most important component to ensure the success of the project.

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