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Faulty Workmanship Coverage: A new insurance solution for trades who self-perform their work



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Risks confront every construction project, no matter the size or application.

As a result, an increasing number of firms are now looking to protect themselves with Contractor's Professional Liability (CPrL) policies that cover the damages arising from the covered negligent acts, errors and omissions related to the professional services performed by or on behalf of the insured. These services commonly include everything from design (whether in-house or subbed out) and construction management to the selection and management of subcontractors and even value engineering ("I can amend this design a little bit AND save the owner money!") This is especially true of the construction professionals who are currently experiencing an uptick in severe claims within the civil, healthcare, commercial building, and habitational project arenas. Of course, the specific coverage is always dependent on the policy's terms and conditions as well as the circumstances surrounding the loss.

In general, CPrL liability lines are often drawn for artisan subcontractors self-performing "your work." This is because the coverage for an insured's "self-performed work" doesn't usually exist within today's GL policies. Typically the only coverage available applies to the work performed by the insured's subcontractors, In fact, many CPrL carriers insure against the loss or damages arising from design or construction management services and/or work designed or fabricated by the insured, but generally do not cover the "actual or physical work" or "defective products used in the course of your work."

It's also important to note that many, if not all CPrL carriers offer an exception to the typical Faulty Work exclusion. Many polices normally read something like "This exclusion does not apply to negligent acts, errors or omissions in the performance of covered professional services." While exclusions worded this way may appear to fill the gap related to the exclusion for repairing or replacing faulty work or material costs, they generally do not. This exception usually only covers the damages resulting from negligence in the performance of professional services, not the faulty work performed on the part of the insured. If the faulty work does not result from negligent professional services, the coverage will often not apply.

In general, claims against contractors which include the "mismanagement of subcontractors" or "failure to properly inspect or direct subcontractors" would usually be covered by a CPrL policy that's written with the above-described exclusion. This includes events where the contractor is found negligent in the proper performance of these services and responsible for the resulting damages involving the cost to repair or replace the faulty work. However, this coverage typically only pertains to the costs needed to repair or replace the faulty work of subcontractors, not the insured's own faulty work.

But again, this coverage depends on the specific wording of the policy. Therefore, attention should always be paid to the professional services actually performed by the insured and

the definition of “professional services” in any insurance policy.

True Faulty Work Coverage – What it is and where can it be purchased?

So, where does this leave contractors who are looking for an insurance coverage that may apply to their faulty work? True Faulty Workmanship coverage forms commonly serve as a separate insuring agreement, which can be offered in carrier-specific CPrL policies. As discussed above, this type of specialized policy generally provides coverage for the claims arising out of the workmanship of “your work” or the use of defective materials or products used in “your work.”

Specifically designed to cover self-performed work and not the work of 3rd party subcontractors, the Faulty Workmanship coverage is typically triggered when a claim is brought against the contractor by an owner or other 3rd party. Faulty Workmanship coverage commonly dovetails with the exclusions for self-performed work found in most commercial general liability policies and includes the materials, parts and equipment that are used to perform the insured’s work. These may include items like steel beams, epoxy activators, anchor bolts, etc.

However, insureds should know that these policies do not cover all faulty work circumstances; exclusions do apply. For instance, Faulty Workmanship policies normally do not offer bodily injury and property damage coverage. They also generally do not protect against the business risks arising from the decisions of unhappy customers. For example, if the insured follows the agreed-upon specs and performs the work properly but the owner is unhappy with the final result, the Faulty Workmanship policy would not generally cover the alleged losses. In addition, professional services, project delays and consequential damages are also normally excluded under the Faulty Workmanship portion of the policy.

For instance, here are several examples of where Faulty Workmanship terms and conditions could benefit the insured, assuming the policy was drafted with the appropriate language:

- A contractor was hired by a municipality to rehabilitate 13 manhole covers in a residential neighborhood. When complete, the new manholes sat two inches above street grade causing numerous complaints. The cost to remove and re-install the covers was \$125,000. The initial job cost was \$150,000.
- Drywall was installed throughout the new wing of a hospital. Unfortunately, the contractor’s purchasing team accidentally ordered and installed several truckloads of three-eighths-inch drywall rather than the half-inch drywall originally specified. The error was eventually discovered necessitating the drywall’s removal and re-installation.

- A sewer contractor installed a course of concrete pipe that cracked, failed and collapsed after it was backfilled. A subsequent inspection found that the poorly manufactured pipe had defects prior to installation. The cost to remove and reinstall the sewer work was \$75,000.
- An electrical contractor working in an area with codes that varied from National Electric Code (NEC) regulations installed the incorrect wire gauge within a large commercial building. As a result, the building failed inspection and the entire building had to be re-wired. The cost to remove and reinstall was \$300,000.

The Emerging Faulty Workmanship Marketplace

The marketplace for true Faulty Workmanship coverage forms have grown from one carrier in 2014 to approximately four or more today. Typically offered as part of a blended contractor's professional and pollution product, Faulty Workmanship coverage is generally designed to cover faulty workmanship and the defective products used in the course of "your work" and is available in limits ranging from \$1M to \$5M. With premiums starting as low as \$2500-3,500, carriers are often selective when it comes to residential exposures and project type. Coverage has even been offered by regional P&C carriers but often with extremely low sublimits and more underwriting restrictions.

Who's the best fit for Faulty Workmanship coverage?

The beneficiaries of today's Faulty Workmanship coverage forms are artisans as well as general and trade contractors who are self-performing work. This includes electricians, plumbers, HVAC and mechanical contractors, interior finishers, masons, utility contractors and flooring contractors. Conversely, exterior insulation and finish systems (EIFS) roofing, structural and environmental contractors are often excluded from eligibility. The other caveat is that the moment these contractors sub out their work, perform construction management or delegate design, the risk management or coverage automatically shifts toward professional liability exposures rather than Faulty Workmanship.

The benefit for most contractors, however, surrounds the ability to cover "your work" faulty workmanship claims triggered by third-parties against the insured – a potential advantage for certain construction professionals.

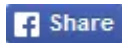
PLEASE NOTE: This is a corrected version of an article that originally appeared here and in our print version on March 24, 2020. Nothing in this article is intended to, or shall, constitute legal advice.

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